



eat *Canadian* 

CANADIAN Foodservice

Private Label Industry Guide



Saskatchewan
GROCERY RETAIL & FOODSERVICE
VALUE CHAIN INITIATIVE

*Adapting to Consumers Demands and
Capturing New Market Opportunities*

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1 INTRODUCTION

1.1 Canadian Foodservice Industry

Understanding the Canadian Foodservice market will help processors understand the Foodservice Private Label market. Exhibit 1.1 summarizes the scale and breakdown of the Canadian foodservice industry.

Exhibit 1.1

Canadian Foodservice Industry Sales, 2011 and 2012 estimate

Canadian Foodservice Market		\$ millions	
Segment	2011	2012 est.	
Quick-Service Restaurants	\$ 22,080.6	\$ 22,806.8	
Full-Service Restaurants	21,846.7	22,502.1	
Caterers	4,209.4	4,339.9	
Drinking Places	2,427.2	2,407.4	
Total Commercial	\$ 50,563.9	\$ 52,056.2	
Accommodation Foodservice	\$ 5,503.0	\$ 5,764.0	
Institutional Foodservice	3,774.9	3,986.5	
Retail Foodservice	1,306.7	1,326.3	
Other Foodservice	2,304.4	2,350.5	
Total Non-Commercial	\$ 12,889.0	\$ 13,427.3	
Total Foodservice	\$ 63,452.90	\$ 65,483.50	

Source: Canadian Restaurant and Foodservices Association, Statistics Canada, fsSTRATEGY Inc. and Pannell Kerr Forster

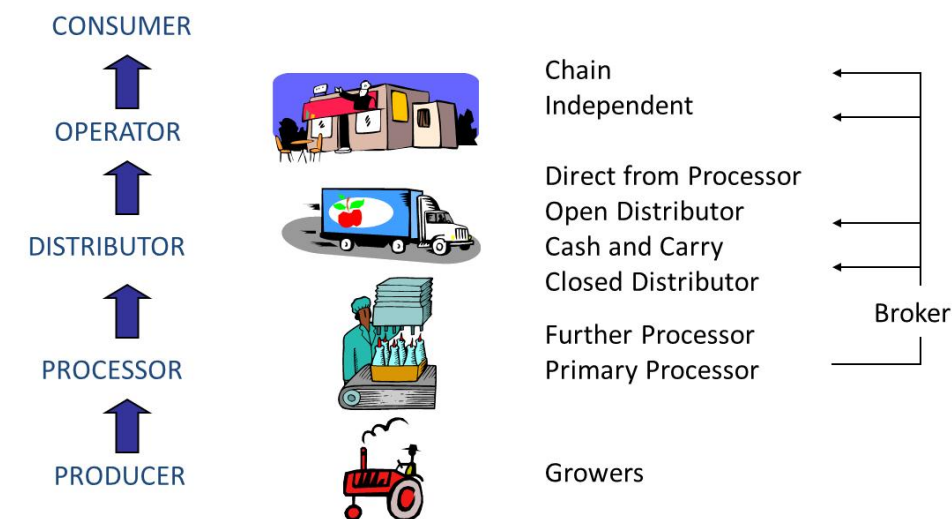


As shown, restaurants (quick-service and full-service) generate almost 70% of Canadian foodservice revenue. Furthermore, consumer data from The NPD Group Inc. shows that chain restaurants (concepts with three or more locations) represent 37% of Canadian restaurant locations, but 62.4% of Canadian restaurant sales. This illustrates the importance of chain restaurants to the Canadian Foodservice Industry.

1.2 Canadian Foodservice Supply Chain

Exhibit 1.2 graphically depicts the levels of the Canadian foodservice industry supply chain.

Exhibit 1.2
Canadian Foodservice Industry Supply Chain



Source: fsSTRATEGY Inc.

Key levels in the foodservice supply chain that are relevant to this guide are the foodservice operator¹ ("Operator"), the foodservice distributor² ("Distributor") and the food processor³ ("Processor").



¹ An entity that operates a foodservice establishment – a restaurant, cafeteria, etc.

² An entity that receives products from food growers and processors, warehouses them and ships them to Operators.

³ An entity that produces a food product from ingredients or packages food products from growers for use by Operators.

1.3 The Canadian Foodservice Private Label Industry

Private Label (“PL”) products are those that are manufactured or packaged by a Processor for the use under another company’s brand. PL products are an increasingly important part of the Canadian foodservice supply chain.



Foodservice PL products typically fall into one of two categories, Distributor Private Label (“DPL”) products and Operator Private Label (“OPL”) products. The number of PL products offered by Distributors or used by Operators vary greatly depending on the maturity of the PL program and the size of the brand. Combined, *fsSTRATEGY* Inc. (“*fsSTRATEGY*”) estimates that DPL products and OPL products represent approximately 37% of all Canadian foodservice industry operator purchases – approximately \$7.5 billion in 2012.

2 PRIVATE LABEL CATEGORIES

2.1 Distributor Private Labels

Distributors play a crucial role in the foodservice industry. Distributors may be national or regional, and may specialize in a single product type (such as dairy or beef) or carry a wide range of product types (known as *broadline distributors*).

Once operating primarily as logistics for Processors, Distributors have evolved, and continue to evolve, into valuable resources for Operators and Processors’ frontline sales teams. DPL products provide distributors a higher margin alternative to selling branded products, and Distributor sales teams are generally incentivized to sell these items more so than manufacturer brands. DPL products are often high volume products where brand value is less important.

fsSTRATEGY estimates that DPL products represent only approximately 19% of foodservice operator purchases in Canada. While the percentage is relatively low, the dollar value, which equates to approximately \$3.8 billion in 2012, represents half of the total Canadian Foodservice PL market because Distributors service all industry categories (commercial, accommodation, institutional, etc.).

2.2 Operator Private Labels

Full service and quick service restaurant chains are the primary market for OPL products. OPL products are used in other foodservice segments but not as frequently as with restaurant chains. A high-proportion of chain restaurant food purchases are OPL products. Again, the amount of OPL products used will vary from Operator to Operator. For well-established, larger Operators, OPL products may represent close to 100% of ingredients purchased; smaller or emerging Operators may have significantly fewer (0% to 25%) OPL products.

The most important benefit for Operators using OPL products is control. Value-added OPL products allow chain Operators to ensure a consistent product across all shifts and locations – by both standardizing the product and increasing the likelihood that franchisees and/or corporate store managers won't buy alternative products of lesser quality to save costs. Furthermore, OPL products can reduce the level of skill required for final preparation and service of the products in the Operator's units. This is of particular importance as the shrinking Canadian labour market makes the sourcing and retention of skilled labour increasingly challenging.

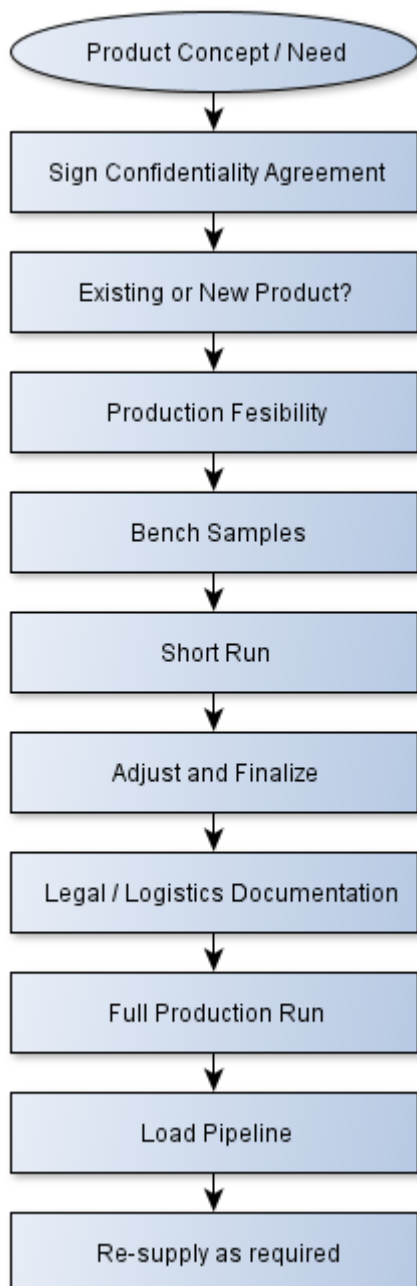
OPL products also protect proprietary recipes and formulas by reducing the number of people who have access to their formulations. Maintaining quality and protecting product formulations help Operators maintain their points of distinction in the industry.

Larger Operators are more likely to use OPL products and usually have a higher rate of compliance (less likely to buy alternative products) than smaller chains. *fsSTRATEGY* estimates that chain restaurant OPL products represents 19% of chain restaurant purchases or approximately \$3.7 Billion in 2012.



3 PRIVATE LABEL PRODUCT PROCESS

Understanding the process involved in developing a PL product is important. Evolving a product through several stages reduces the risk for both parties, as it allows for fine tuning before larger investments are made in full production. While the nature of any business relationship will vary, the following flow chart illustrates the typical steps involved in the development of a PLP programme.



3.1 Confidentiality Agreement

The first step in PL product development flow is to implement a confidentiality agreement between the Processor and Distributor or Operator (“the Parties”). The agreement should protect both Parties’ interest with regards to business plans, product concepts, processes and capabilities.

3.2 Existing or New Product

PL products aren’t always unique. Existing, branded products can also be packaged under a client’s brand. In this stage, the Parties identify whether an existing product will meet the client’s needs or whether a new, unique product formulation is required.



3.3 Production Feasibility

Production feasibility is a critical stage in the PL product process. In this stage, the parties identify and address potential issues that could impede the production of the PL product before significant resources are invested.

Examples of topics that should be explored in this phase include, but are certainly not limited to:

- Do the Processor's minimum batch sizes align with the production schedule and volumes required by the client?
- Does the Distributor or Operator have the ability to accurately forecast their production needs?
- If the client is an Operator, do they have the ability to ensure consumption compliance (i.e. ensure that units use the PLP and not an alternative product)?
- Can the Processor meet the food safety or HACCP requirements of the Distributor or Operator?
- Does the Operator have distribution in place? If not, is the Operator able to source distribution and what roles will the Processor be expected to play in the distribution/storage of the product? Can the Processor provide for those needs?
- Does the Processor have the necessary equipment and resources to produce and/or package the product in the current and future volumes required?
- If the Distributor or Operator requires a unique packaging solution, packaging issues should be resolved up front.



Can the packaging requirements be met? Does the packaging configuration require reconfiguration of the packaging line? Does the Processor have the appropriate equipment to produce and package the product?

- Are the ingredients available in a reliably sufficient quality and volume?



- Are the ingredients legal for import or purchase?
- Who will own the recipe? Who will own the process? Usually the Operator or Distributor owns the formulation and process for unique products but this is negotiable.

The core objective of this phase is to ensure that both parties understand the objectives of the process, and that those objectives can be realistically met with the available resources.

3.4 Bench Samples

Bench samples are proof of concept test samples that define the PL product. During this stage, the recipe or formulation is developed to the Distributor's or Operator's specifications. One or more variations of the PL product bench sample is often produced manually and in small batches, allowing the client to tweak and refine the product before moving to a short run production. This stage may involve several reformulation and retesting sessions.



3.5 Short Run

Once the Distributor or Operator is happy with the bench samples, a short run is conducted. A short run is a limited production of the PL product. Short runs can be produced either in the Processor's facilities or, if the volume is too low, in incubator facilities like Food Development Centres across Canada.



For Operators, short run samples are typically evaluated in select test stores to determine how the packaging and product formulations work in a live environment. Distributors may also choose to test the PL product with select customers. Survey results from the evaluations can be used to adjust, re-test, and finalize PL product formulation and packaging format.

The final short run PL products can be used to apply for pre-approval from the Canadian Food Inspection Agency ("CFIA") when the product is intended to be used inter-provincially. Where possible, seeking pre-approval is recommended as it will flag any potential concerns the CFIA has before the Processor invests in a full production run. Some Distributors or Operators will prefer to follow federal regulations even if their product is only intended for use within the province. This is because the Distributor or Operator views the federal regulations to be more stringent and therefore safer.

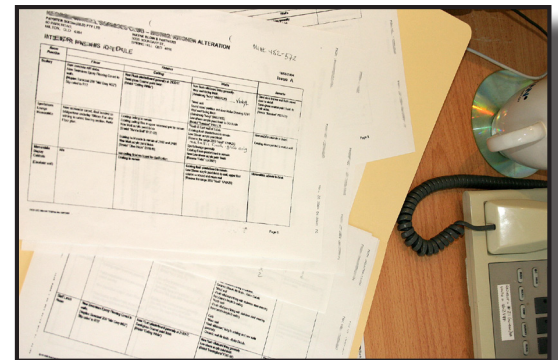
3.6 Legal and Logistic Documentation

Once the PL product's specifications have been clearly defined and documented, additional documentation is required concerning the relationship between the parties, and the handling and logistics of the product. This documentation is summarized below.

3.6.1 Handling and Logistics Manual

The Handling and Logistics Manual provides instructions (temperature, time, volume, etc.) for every step of the product life cycle including:

- Production
- Distribution
- Storage (Unit level)
- Holding
- Serving
- Storage
- Receiving
- Reconstitution (preparation, heating, cooking, etc.)



3.6.2 Co-Packer Agreement

The co-packer agreement defines the relationship, responsibilities and expectations, and protects the interests of the two Parties. The Parties should explore all potential conflicts and document amenable solutions, thereby creating a how-to manual for the relationship to avoid miscommunications or unmet expectations. A co-packer agreement may include some or all of (or more than) the following topics:

- Manufacturing Responsibilities
- Production Schedule (volume and timing)
- Manufacturing Facilities (description and location)
- Ownership Rights: Changes to Specifications
- Compensation Model
 - Basic structure
 - Handling changes to input costs
- Materials
- Risk of Loss
- Confidentiality and Non-Competition
- Indemnities (for both Parties)
- Resale of Product
- Termination Clauses (for both Parties)
- Severability
- Acceptable Notice Methodology
- Length of Term
- Lead Time Requirements
- Provision of Raw Materials, Ingredients, Packaging and Artwork
- Review
- Cost Programs and rebates
 - Delivery/Storage
 - Inspections
 - Warranties and Representations
 - Insurance
 - Use of Trademarks and Trade Names
 - Force Majeure
 - Broker Fees

The list above is not intended to represent the complete contents of the co-packer agreement. Additional content regarding governing laws, waivers and interpretation are needed, and the co-packer agreement should be crafted carefully with appropriate legal counsel.

3.7 Full Production Run

By the time this stage is reached, every detail about the PL product should be determined and formalized. The full production run is the last stage in the first run of a new PL product. The output of the full production run is used to fill the pipeline (the network of storage, distribution and operations that form the product's value chain). Following the volume requirements and the production schedule set forth in the co-packer agreement, additional runs will be needed to re-supply the pipeline as required.



4 COST PROGRAMS

Cost programs are programs in which the Processor furnishes rebates, advertising funds, or other internal payments to the Distributor or Operator according to the predetermined model. For example, a Processor may provide a rebate on the product cost once the Distributor or Operator reaches a predetermined volume of purchases.



Cost programs are typically built into the price of the product. Rebates tend to be greater for larger national brands than for OPL products. These types of programs are usually negotiable. Alternatively, processors may provide a “dead net” price that includes no allowance for any internal monies – the product is bought/sold and that is the extent of the transaction.

It is critically important that all cost program terms (including the non-existence of a cost program) are clearly and formally documented so that there are no questions regarding what the Processor’s obligations in the future. Distributor and Operator contacts can turn over. A handshake and a verbal understanding are not sufficient to protect the interest of the Parties or the relationship between them.

5 FOOD SAFETY AND HACCP

Food safety is extremely important, and many Operators and Distributors will require Processors to have a fully instated HACCP plan. HACCP stands for Hazard Analysis Critical Control Point and it is an effective method of identifying, tracking and mitigating biological, physical, and chemical food safety risks throughout the product’s life cycle. Even if HACCP certification has not been required by the client, it is highly recommended as an industry standard operating practice.

Plant audits by Distributors and/or Operators should not only be permitted, but encouraged, especially in the pre-full production phases of the PL product process so that the Distributor and/or Operator understands the standards the product will be produced within.

6 CONCLUSION



PL products offer a great opportunity for Processors to access the multi-billion dollar Canadian foodservice industry. Opportunities range in size with as much diversity as there are differences in the size Operators and Distributors. Regional, national, even international products can be developed with Operators and Distributors to add points of distinction, consistency and control to their brands.

The key to success is to not rush the product development process. As earlier shown in the PL product process flow, taking a step-by-step approach can mitigate the production risk and help ensure a quality product. Proper documentation and communication is also extremely important, as it is in any business relationship. The fewer potential issues that are left to chance, the stronger the relationship will likely be between the Processor and the Distributor or Operator.

Note to Readers:

The estimates of PL, OPL and DPL products market size are based on research conducted by fsSTRATEGY with foodservice distributors and other opinion leaders and data obtained from the Canadian Restaurant & Foodservices Association. Secondary research data is not available to confirm the estimates. Readers are cautioned to use the estimates with care. While fsSTRATEGY has undertaken its best efforts to develop reasonable estimates, it does not warrant the absolute accuracy of its estimates.



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The Agriculture Council of Saskatchewan (ACS) Inc. has developed this electronic guide for the Canadian Foodservice Industry as part of its continuing efforts to support the agriculture and agri-food industry and develop the capacity and tools for food growers and processors to enter the Foodservice Industry.

The purpose of the guide is to provide food growers and processors with a better understanding of the Foodservice Industry and how to tap into business opportunities within it. To that end, ACS has engaged *fsSTRATEGY* Inc., consultants to the Foodservice Industry, to help create this powerful reference tool. *fsSTRATEGY* is an alliance of senior consultants focusing on business strategy support – research, analysis, design and implementation – for the Foodservice Industry. Their team has extensive consulting experience in Foodservice across Canada.

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