

**CDC's 9th Annual Public Meeting
Thursday, January 21, 2016 – 4 pm
Panorama Room, Delta Ottawa City Centre**

ALISTAIR JOHNSTON, CDC CHAIRMAN

Purpose, Priorities and Governance

I will begin my presentation on the CDC and its purpose, priorities and governance.

Our Purpose

Although the CDC's legislative mandate is to provide efficient producers of milk and cream with the opportunity to obtain a fair return for their labour and investment, and to provide consumers of dairy products with a continuous and adequate supply of dairy products of high quality, as Chairman of the CDC, I see our purpose to be larger in scope. We share with stakeholders the responsibility and commitment of ensuring a viable, sustainable and forward thinking Canadian dairy industry. More than a facilitator; we are here to help influence national dairy policy in Canada through meaningful collaboration and consultation with all sectors of the industry. Our success should be measured in fulfilling our mandate and by promoting and supporting industry modernization in a variety of ways:

- The promotion of meaningful and sustainable innovation
- Contribute to and encourage open and constructive "two way" collaboration/consultation
- Demonstrate modern day levels of transparency in our work and decision-making

Governance – CDC's Board of Directors

The CDC is governed by a board of directors. It is made up of myself as Chairperson, a commissioner (Hennie Bos), and a chief executive officer (Jacques Laforge). We are Governor in Council appointments based on the recommendation of the Minister of Agriculture and Agri-food. Our respective mandates are served on a part-time basis. We have long and varied experience in the dairy industry, one in processing, one in production, and sometimes one in both! This combination of experience brings a balanced approach to decision-making.

Governance – Board Responsibilities

The board is responsible for the overall stewardship of the organization and is accountable to the Minister of Agriculture and Agri-Food. We approve the CDC's corporate plan, annual report, strategic plan, budget and financial statements. We develop policies and practices for the CDC; ensure that the principal business risks are identified and that appropriate systems to manage these risks are in place. We also ensure the integrity of the information systems and management practices; the development and implementation of a comprehensive succession plan; and the follow-through on regular performance management assessments of all CDC employees.

As Chair of the board, I am committed to develop and implement a decision-making process that is accountable, transparent and relevant to the mandate of the CDC and our role within the Canadian dairy industry. Throughout my mandate as Chair, I am determined to strengthen and expand the CDC's consultative process with dairy industry stakeholders and to communicate our vision and decisions in a clear and timely manner.

Governance – Committees

The board has two standing committees: the Audit Committee and the Senior Management Team.

The Audit Committee, whose membership is the same as the board of directors, ensures proper accountability over CDC operations as required by the *Financial Administration Act*. A representative of the Office of the Auditor General regularly attends our Audit Committee meetings. This allows for greater transparency in our deliberations and reporting.

Among the many responsibilities of this committee, the main ones include reviewing the Office of the Auditor General's annual and special examination audit plans and reports; responding to the management actions stemming from these reports; reviewing the quarterly and annual financial statements and approving the CDC's annual audit and program evaluation plan.

As for the Senior Management Team, it consists of our Chief Operating Officer, the three directors and the Manager of HR. This committee is chaired by the CEO. They meet approximately every two weeks to discuss the daily operations of the CDC and to make decisions required for smooth internal operations. The SMT creates and amends CDC policies and reviews the administrative budget before it is presented to the board. It also addresses issues relating to human resources, audit, evaluation, and governance, and acts as a sounding board for the CEO on industry-related matters and recommendations to be presented to the board.

The SMT is supported by five advisory committees that develop plans and priorities, and advise management on human resources, information technology, internal audits and program evaluation, occupational health and safety, and risk and security.

Our Priorities

Having recently participated in our annual strategic planning session for the upcoming dairy year 2016-2017, the board decided to keep the same theme priorities as this current dairy year. These will therefore continue to be focused on growing markets for Canadian dairy products; helping the industry adapt to change; ensuring a well-administered supply management system and a well-managed CDC.

I believe more must be done to strengthen the partnership between the CDC and industry aimed at delivering the conditions for a vibrant dairy supply management system, engendering trust, building consensus and encouraging investment to enable the Canadian dairy industry to become a force in the global marketplace.

It is our intention to continue developing incentives, programs and activities aimed at achieving these priorities. We will aim to create an environment that is conducive to market growth and innovation; promote the timely supply of milk to growing markets; help the industry adapt to changing market conditions; develop new markets focusing on SNF; increase the processing capacity and efficiency in the industry; ensure that Canadian milk production meets demand; and respect interprovincial and international agreements such as pooling agreements and trade deals.

These priorities were established while taking into account the many challenges facing the dairy industry.

Industry Challenges

The Canadian dairy industry is facing significant pressures that require effective responses, short and long term. Many factors have contributed to the reasons why we are now at a crossroads. Solutions to resolve misalignment of milk production with demand, quota and allocation, structural surplus, processing capacity and market development, to name a few, must be found and implemented in a collaborative manner among all dairy industry stakeholders. We are very pleased to see the hard work producers and processors are doing to reach a consensus on how to move forward. This, we will continue to encourage - while being aware of the ever present burden of such things as the structural surplus, and the time pressures this challenge places on the system.

Key within these aspirations is to increase processing capacity in the Ingredients sector. Seeing the industry coalesce around this need is very positive. It is my hope that consensus will provide an entry point into this global sector that keeps stakeholders safe from selling commodities and instead focus on high volume niche markets. Selection and agreement of the optimal strategy for Canada will necessitate the creation of initiatives aimed at supporting this direction from a technical, academic and human resource perspective. Friends, our aspirations must be supported by an infrastructure that delivers these necessary capabilities. Let's assume we are entering new fields of endeavour for the Canadian dairy industry and collectively preparing for the next generation's success. Let this be our generation's legacy.

I am happy to report that demand for butterfat has increased by 2% per year in the last three years. This is great news for the Canadian dairy industry; consumers view butter and dairy products as being part of a healthy diet and are eating more butter! Unfortunately the impact of this increase in butterfat demand is not all positive; combined with increased imports of SNF, it contributed in large part to increased surplus structural of solids nonfat. This led to increased sales of SNF in marginal markets which lowered the producer revenues per hectoliter of milk. This was further compounded by plummeting world prices, especially of SNF, affecting the price that producers receive for their milk used in further processing (Classes 5(a), (b), and (c)) and for dairy products exported in Class 5(d).

After implementing various measures, the CDC imported butter in early and late fall to help supply the butterfat demand as supply was and continues to be a challenge due to circumstances outside of the CDC's control. The delay in corresponding production, less cream going from cheese plants to butter plants mainly because of increased use of liquid MPC imports and high private stocks continue to create stumbling blocks in supplying the butterfat demand. The shortage of CDC stocks will remain a serious concern for the coming months.

The CDC is committed to work with stakeholders in finding solutions to challenges such as these. We must look at investing in the future of the industry, having state of the art processing plants to improve efficiency. I truly believe that collaboration and commitment among all stakeholders, which characterized the creation of supply management, remain the industry's greatest strength in ensuring its continued success and sustainability in the years to come.

HENNIE BOS, COMMISSIONER AND CHAIR OF THE AUDIT COMMITTEE

Financial Report and Oversight

As Chair of the Audit Committee, I am proud to present the operating results of the CDC for the dairy year ending July 31, 2015. Because of the federal election last fall, our Annual Report has not yet been tabled in Parliament, but the financial information that I am about to present was audited and accepted by the Office of the Auditor General.

Inventory

Let's start with the CDC's main asset: Inventory.

The CDC's inventory is comprised of butter and skim milk powder (SMP) that are purchased under 3 programs:

The first, the Domestic Seasonality program, includes:

- Plan A bulk butter to be resold to processors when domestic seasonal demand increases and;
- Plan B butter and skim milk powder purchased from processors who must repurchase their dairy products within a certain period.
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The second of these programs is the Surplus Removal Program, which is used for skim milk powder to be resold in the export and animal feed markets.

Finally, the CDC purchases imported butter as part of Canada's obligations under the World Trade Organization (WTO) Agreement on Agriculture.

On July 31st 2015, the CDC's total inventory value was lower than in previous years primarily as a result of a decrease in butter stocks, as you can see in the graph. For most people here, this should not come as a surprise. During the recent increase in demand for butter, processors decided to serve those markets directly rather than selling butter to the CDC.

On the other hand, as you can see, SMP inventory increased significantly this year. Two main reasons explain this. First, SMP exports were restricted by low world prices. Secondly, higher demand for butterfat and the resulting increase in production increased the surplus of solids non-fat purchased under the Surplus Removal Program.

Domestic Activities

As part of its domestic activities, the CDC purchases and sells butter and skim milk powder to regulate the supply of dairy products in the domestic market throughout the year.

In 2014-2015, domestic sales revenues decreased by \$57 million compared to the previous year, mainly as a result of the low Plan A and Plan B stocks available for sale.

This had minimal impact on profit, as product is purchased and resold at prevailing support prices. Profit decreased by \$1.2 million compared to the previous year. This was mostly due to lower returns for SMP sold on the animal feed market rather than being due to the butter situation. The lower returns on SMP were partly offset by better returns on imported butter sales.

Export Activities

I will now turn to the CDC's export activities.

Export sales revenues for 2014-2015 were significantly lower than in the previous year due to a sharp decline in world prices for dairy products. The CDC sold approximately 12,000 t of SMP in 2014-2015 compared to close to 21,000 t in the previous dairy year. Low world prices for SMP reduced the quantity of SMP that the CDC could export while respecting Canada's WTO export subsidy limits.

The CDC incurred a slight loss of \$590,000 in its export activities. The CDC purchases surplus dairy products destined for export at prices that reflect prevailing world market conditions, hoping to break even over the course of the dairy year. Because these markets are unpredictable, we sometimes finish the year with minimal gains or losses, which was the case in 2014-2015.

Other Income

I will now look at other sources of income for the CDC, apart from its commercial operations. Funding from milk pools represents the revenues obtained from producers and the marketplace to finance a portion of CDC's administrative expenses, the cost of production study, as well as the carrying charges associated with CDC butter stocks.

Funding from the Government of Canada is used to partially fund CDC's administrative expenses.

Revenues obtained for audit services relate to the milk plant utilization audits performed by the CDC in 6 provinces on a cost-recovery basis.

Operating and Administrative Expenses

This next slide shows the CDC's operating and administrative expenses for the year ending July 31, 2015.

Operating expenses, totaling 1.2M\$ in 2014-2015, are composed of industry initiatives, the cost of production study, as well as other operating charges.

As for the Administrative Expenses, they are composed primarily of salaries and employee benefits, the rest being rent, travel and administrative support.

In 2013, the government implemented a two-year budget freeze beginning in fiscal year 2014-2015. As government funding has not been adjusted to compensate for wage and salary increases, the CDC continued to find ways to improve the efficiency of its internal operations and administration.

Overall Results

This brings us to the Operational Surplus for the year ended July 31, 2015.

This year's operational surplus from seasonality and surplus removal programs amounted to \$20.2 million. As milk producers are responsible for financing these programs, this amount was returned to provincial milk marketing boards and agencies.

After taking into account the payment of this operational surplus, the CDC's "Total comprehensive income" for the year ended July 31, 2015, also known as the bottom line to most people was \$4 million.

This completes my review of the CDC's key financial elements.

Oversight – CDC's External Audit Activities

The CDC's Audit section led by Hossein Behzadi carries out several audit activities to ensure all milk components sold in various programs are used in eligible products.

Most external audits target companies participating in the Special Milk Class Permit Program. Risk assessment is used to identify high risk companies. We audit the same companies for the Import for Re-export Program if they also participate in this program. Last dairy year, 68 companies were audited, including 4(m) permit holders and IREP participants. We also perform milk plant utilization audits in 6 provinces on a cost-recovery basis. Class 3(d) audits were also performed and covered 787 pizzeria restaurants.

Oversight – CDC's Internal Audit Activities

The CDC performs internal audits and program evaluation to ensure proper accountability and effectiveness of the CDC's systems, programs, policies, and practices. We also provide expertise and promote the harmonization of procedures to the National Milk Audit Advisory Committee. This committee brings together all CDC auditors, provincial auditors and representatives from milk marketing boards and the dairy processing industry twice a year.

JACQUES LAFORGE, CHIEF EXECUTIVE OFFICER

Objectives, Results and The Way Forward

As CEO of the CDC, I am pleased to present to you our current objectives, our accomplishments to date and how we see the way forward for the CDC and the Canadian dairy industry. Our 2015-2016 objectives are to grow markets for Canadian dairy products, help the industry adapt to change; ensure a well-administered supply management system and a well-managed CDC.

Growing Markets

OBJECTIVES:

- Grow the demand for Canadian dairy products
- Ample milk is available at the right place at the right time

An Industry That Adapts

OBJECTIVES:

- Support the industry in addressing changing markets
- Help create new investments to increase use of SNF.

A Well-Managed Supply Management System

OBJECTIVES:

- Increase in producer revenues is due to market growth
- Milk components sold in various programs are used in eligible products
- Signals are sent to ensure sufficient milk supply for demand and butter stocks
- Improve the CDC tools to monitor compliance and administration of federal-provincial and international agreements
- WTO commitments are respected and met

A Well-Managed CDC

OBJECTIVE:

The CDC adapts to remain a high-performing organization

- the right workforce to achieve its objectives
- the right number of engaged employees with the right skill set in the right structure

The Way Forward

Continued collaborative discussion between producers and processors with the CDC and governments to resolve outstanding issues

- Market growth focused on SNF usage
- New investments to increase processing capacity especially for residual milk
- Trade agreements