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Canada

Dairy and Products Annual

2015

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Report Highlights:
In 2016, milk, cheese, butter and skim milk powder production is expected to stay close to 2015 expected levels due to steady demand and the need to rebuild stocks. Imports of these products will remain close to average levels due to the import controls in place. The need to gain efficiencies through lowering production costs will keep imports of U.S. origin milk protein substances strong. Concessions on dairy have been granted through the TPP agreement equivalent to 3.25 percent of the domestic milk production and are expected to provide new urgency to addressing the growing SNF structural surplus.

DAIRY AND PRODUCTS ANNUAL – CANADA

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SNAPSHOT OF CANADIAN DAIRY INDUSTRY

The Canadian dairy sector functions under a supply management system, based on planned domestic production, administered pricing and dairy product import controls.

- In 2015, the first seven month of data show total cash farm receipts at the same level as in 2014 for the same time period(source: Statistics Canada, table 003-0008) In calendar year 2014, total net cash farm receipts from milk and cream sold off farms reached C$6.07 billion. This is a 3 percent increase over 2013 levels.

- For 2015, the first 6 months of data shows sales of milk and dairy products 2 percent below year 2013 levels for the same time period. In 2014, manufactured shipments (sales) of milk and dairy products reached C$16.4 billion. This is a 5 percent increase over 2013 levels. In 2014, manufactured shipments (sales of milk and dairy products represented 18.8 percent of Canada's total food and beverage sector (Source: Statistics Canada, table 304-0015).

- The dairy industry ranks third in terms of value in the Canadian agricultural sector following grains and red meat (http://www.dairyinfo.gc.ca/index_e.php?s1=cdi-ilc).

- Improved feed rations, disease control and genetic advancements have increased the amount of milk produced per cow resulting in fewer dairy cows needed to meet Canada's domestic requirements. For example, since the year 2000, the Canadian dairy herd has fallen to 953,200 head in 2015, which represents a 13.6 percent decrease. (Source: Canadian Dairy Information Center)

- The number of dairy farms has decreased nearly 40 percent since the year 2000. The number of dairy farms has dropped to 11,683 in 2015 from 19,962 in 2000. (Source: Canadian Dairy Information Center)

- Consequently, farming units have grown in size and have become more efficient in operation. The number of dairy cows per farms has risen from an average of 57 dairy

cows per farm in the year 2000 to an average of 80 dairy cows per farm in 2015. This represents an increase of over 40 percent. (Source: Canadian Dairy Information Center)

- The provinces of Quebec and Ontario are the provinces were dairy production is most concentrated. Quebec accounted for 37 percent of the dairy cows in 2015, followed by Ontario with 33 percent. The province of Alberta had the next largest number of dairy cows and accounted for 8 percent of the total number of dairy cows. (Source: Canadian Dairy Information Center)

- The typical Canadian dairy farm is quite specialized, with most of its revenue coming from milk production and the sale of dairy cattle. It is a family-owned operation. The farm owners are in their mid-forties and have built up considerable equity in their operation. The typical family farm is accustomed to using advanced technology in practices such as artificial insemination, breed selection and labor-saving milking systems. Computerization of feeding and herd management systems, and equipment innovations are also rapidly changing the way things are done on the farm. The industry has experienced a 36 percent decline in the number of dairy farms over the past decade. However, individual farming units have grown in size and have become more efficient in operation.

- The dairy processing sector is relatively concentrated. The latest statistics show that the three largest processors in the country (Saputo, Agropur and Parmalat) process approximately 75 percent of the milk produced in Canada. The fluid milk market represents almost 40 percent of milk utilization, while the market for manufactured dairy products such as butter, cheese, yogurt and ice cream accounts for more than 60 percent of utilization. (Source: Canadian Dairy Commission)

PRODUCTION, CONSUMPTION, TRADE AND STOCKS FOR MILK, CHEESE, BUTTER AND NON-FAT DRY MILK

MILK:

Dairy, Milk, Fluid	2014		2015		2016	
Market Begin Year	Jan 2014		Jan 2015		Jan 2016	
Canada	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Cows In Milk	955	955	955	955	0	955
Cows Milk Production	8409	8437	8535	8682	0	8685
Other Milk Production	0	0	0	0	0	0
Total Production	8409	8437	8535	8682	0	8685
Other Imports	48	56	48	49	0	50
Total Imports	48	56	48	48	0	48
Total Supply	**8457**	**8493**	**8583**	**8730**	**0**	**8733**
Other Exports	4	4	4	4	0	4
Total Exports	4	4	4	0	0	0
Fluid Use Dom. Consum.	2946	2946	2946	2945	0	2945
Factory Use Consum.	5107	5143	5244	5396	0	5398
Feed Use Dom. Consum.	400	400	389	389	0	390
Total Dom. Consumption	8453	8489	8579	8730	0	8733
Total Distribution	8457	8493	8583	8730	0	8733
(1000 HEAD) ,(1000 MT)						

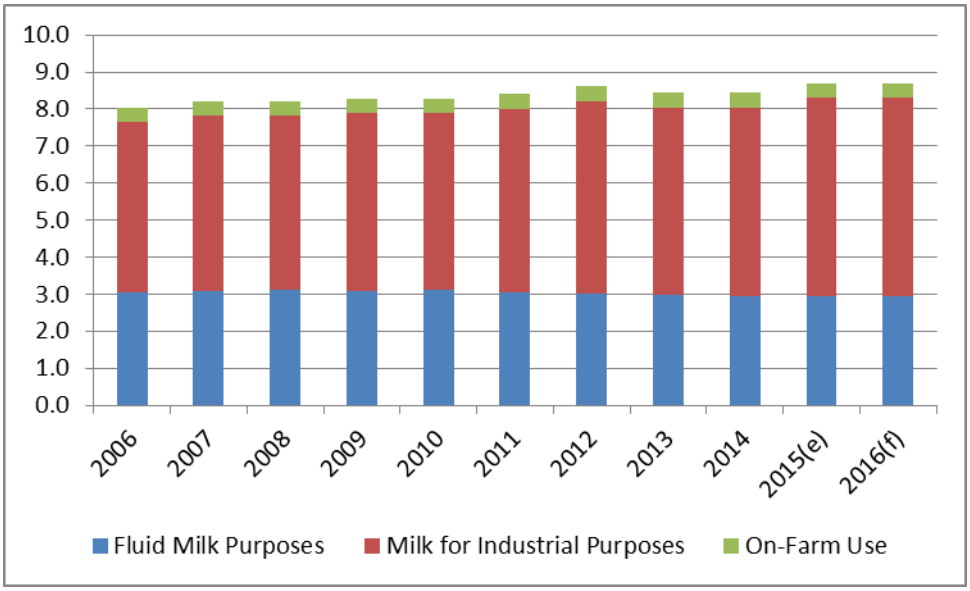
Production:

In Canada, provincial milk marketing boards maintain responsibility for setting production limits of its own fluid milk, pricing formulas, quota policies and other regulations. Industrial milk production levels are allocated using a national management tool called the Market Sharing Quota (MSQ). Quota is allocated on a butterfat basis. It is set by the Canadian Milk Supply Management Committee (CMSMC), which applies the terms of the National Milk Marketing Plan (a federal-provincial agreement) to establish each province's share of the MSQ. The provinces are then responsible for distributing shares of the quota to producers according to provincial policies and in accordance with pooling agreements.

More on the system can be found at the following URL address: http://www.cdc-ccl.gc.ca/CDC/index-eng.php?id=3806

Milk production in Canada supplies two markets. The fluid milk market includes creams and flavored milks. The industrial milk market is milk used to make products such as butter, cheese, yogurt, ice cream and milk powders. In 2014, the fluid milk market accounted for 35 percent of total milk produced in Canada, and the industrial milk market 60 percent. On farm use is estimated to account for approximately 4 to 5 percent of total milk produced.

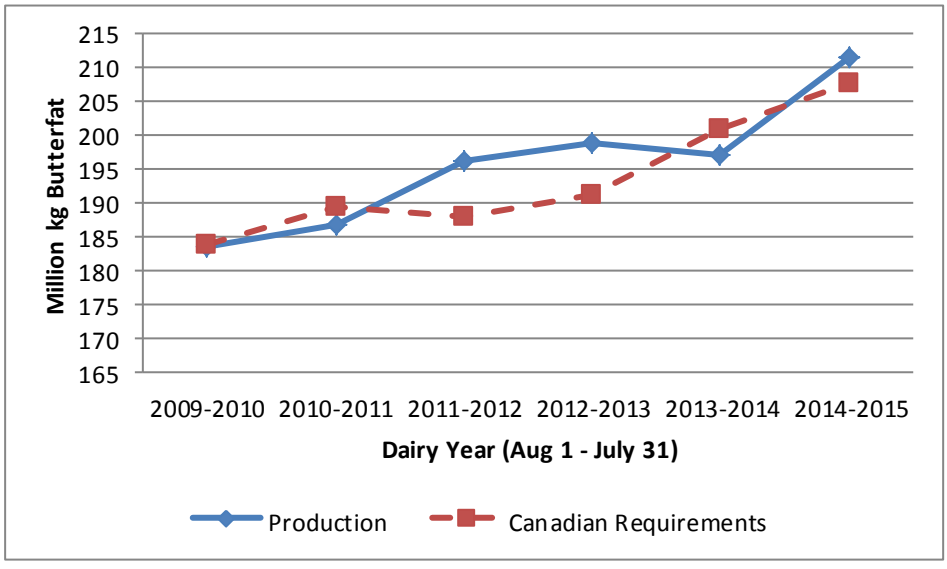
Figure 1: Milk Production in Canada, 2006-2016(f), in million metric tons



Source: Statistics Canada, Milk production and utilization, http://www5.statcan.gc.ca/cansim/pick-choisir?lang=eng&p2=33&id=0030011

The Canadian Milk Supply Management Committee (CMSMC) sets the MSQ based on the recommendations of the Canadian Dairy Commission (CDC). The CDC monitors the trends in Canadian dairy requirements (demand) and makes recommendations on the necessary adjustments to reflect changes in demand for milk for industrial dairy products. ***Figure 2***, below illustrates the changes in Canadian dairy requirements and milk production for industrial purposes over time by dairy year.

Figure 2: Canadian Dairy Requirements and Production for Industrial Milk Market



Source: Canadian Dairy Commission; Market Bulletins
http://www.cdc-ccl.gc.ca/CDC/index-eng.php?link=112

For several years, milk production in butterfat equivalent had been trailing below the dairy industry requirements. However, at the end of dairy year 2014-2015(August 1, 2014 – July 31, 2015), milk production in butterfat equivalent had caught up with industry requirements. This increase in production has been driven by an increased demand for butterfat by the dairy processing industry.

Due to the supply management system in place, significant changes in milk production from year to year due to changing international market conditions do not occur. In 2016, milk production is forecast to reach 8.685 million metric tons (MMT) in order to meet the demand for butterfat by the dairy processing industry. Based on 7 months of production data of milk produced for the fluid milk market and for the industrial milk market, the 2015 milk production (including on farm feed use) is estimated to reach 8.682 million metric tons (MMT). This represents a 3 percent increase over year 2014 levels of 8.437 MMT.

Trade:

The fluid milk access level is set at 64.5 thousand metric tons (TMT); however there is no commercial quota available for fluid milk, as it is assumed to be filled through cross border shopping. Milk imports enter Canada under personal use exemptions (General Import Permit No. 1 - Dairy Products for Personal Use) or through the imports for re-export program (IREP) and therefore are limited.

Milk imports in 2016 are forecast to remain at levels similar to 2015 due to similar market conditions. Milk imports are estimated to fall to 49 TMT in 2015, based on 7 months of available trade data. This 12.5 percent decrease is attributed to a strengthening U.S. dollar compared to the Canadian dollar. It should be noted that trade numbers on milk coming into Canada as part of cross border shopping are not reliable as it is not tracked very closely. Commercial milk imports come into Canada either through the Import for Re-Export Program (IREP) or a duty draw-back program both which require that the milk be re-exported in some form within a certain time limit. In 2014, IREP trade accounted for 25 percent of milk imports, while Statistics Canada reports 75 percent of the trade as coming in over access, which would suggest through the duty deferral program.

Cream, unlike fluid milk, has a small commercial quota, which is determined on a dairy year (August-July) basis rather than an annual calendar year (CY) basis. The cream access level is 394 metric tons. Cream imports continue to increase due to the increased usage of IREP and duty drawback programs. In 2016, cream imports are forecast stay at 2 TMT, the level estimated for 2015. In 2014, cream imports were 1 TMT. Cream imports have been increasing over time as the imports for re-export and duty deferral programs gain in popularity.

Despite a weaker Canadian dollar expected for the foreseeable future, the volume of milk purchased through cross border shopping is not expected to change due to ingrained shopping

habits as well as the attractiveness of US milk prices compared to Canadian prices. Due to market proximity and the perishable nature of fluid milk and cream, the United States is the primary source for imports of milk and cream into Canada.

Milk exports from Canada are very small, in part due to export subsidy limitations, but for the most part due to the structure of the supply management system and provincial regulations which limits the ability of milk producers to transport the milk across the border. Milk exports in 2016 are forecast to remain at 4 TMT, the same levels expected for 2015.

Consumption:

The Canadian dairy sector functions under a supply management system, based on planned *domestic* production, administered pricing and dairy product import controls. As a result, milk production levels have stayed relatively stable over time. Stable production levels are also due to the fact that there are not significant changes in GDP or population growth to drive an increase in demand for dairy products. Statistics released in July, 2015 showed Canada's population growth rate slowing to 0.9 percent, down from 1.1 percent a year ago. The slowdown is largely due to a decrease in international migration. The overall population growth rate has shown little variation in 30 years, ranging between 0.8 percent and 1.2 percent. The statistics also reveal that much of this growth occurs through immigration, which does not necessarily translate into increased demand for dairy products. In addition, the popularity of milk substitutes from other product groups (almond milk, soy milk, margarines etc.) has meant increased competition.

BUTTER:

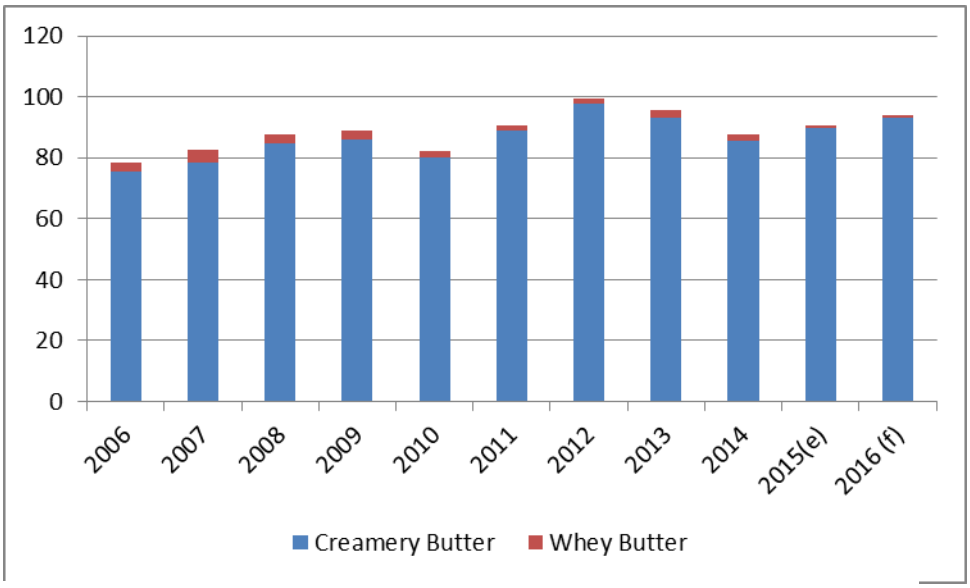
Dairy, Butter	2014		2015		2016	
Market Begin Year	Jan 2014		Jan 2015		Jan 2016	
Canada	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Beginning Stocks	11	11	5	9	0	9
Production	85	88	90	91	0	93
Other Imports	11	10	15	11	0	11
Total Imports	11	10	15	11	0	11
Total Supply	**107**	**109**	**110**	**111**	**0**	**113**
Other Exports	2	2	2	2	0	2
Total Exports	2	2	2	2	0	2
Domestic Consumption	100	98	101	100	0	100
Total Use	102	100	103	102	0	102
Ending Stocks	5	9	7	9	0	11
Total Distribution	**107**	**109**	**110**	**111**	**0**	**113**
(1000 MT)						

Production:

Post forecasts a production increase in 2016 to continue to meet the steady demand for butterfat and re-build butter stock levels. Based on 7 months of production data combined with the fact that the Canadian Dairy Commission continued to increase its estimate for butterfat

requirements by the processing industry, Post estimates for butter production to reach 91 TMT in 2015. This represents a 4 percent increase over 2014 production levels of 88 TMT.

Figure 3: Butter Production in Canada, 2006-2016(f), in thousand metric tons



Source: Statistic Canada, Table 003-0009, Production of Selected Butter Products

Trade:

Total butter imports are comprised of three HS codes: 0405.10.00 for butter, 0405.90.00 for fats and oils derived from milk, and HS 0405.20.00 (zero TRQ access) for dairy spreads, which contain butter. Similar to cream imports, the butter import access level is determined based on the dairy year, rather than the calendar year. The access quota is set at 3,274 MT and applies only to the butter and fats and oils from milk. Nearly two thirds of the TRQ is allocated to New Zealand (2,000 MT).

More than half of the butter imports into Canada enter under the import for re-export program (IREP), the demand for which often fluctuates with the Canadian exchange rate. Imports of butter are forecast to remain relatively steady in 2016 due to increased domestic supplies. Year to date trade data suggests that butter imports will reach 11 TMT in 2014, a slight increase over 2014 import levels. This small increase is driven by the need for butterfat from the food processing industry.

Due to its proximity to the Canadian market and the popularity of the import for re-export program, United States butter imports (040510) account for between 25 percent and 59 percent of butter imports into Canada.

Canadian exports of butter are limited by its export subsidies commitments for butter of 3.5 TMT or C$11.025 million (which ever limit is hit first). Butter exports tend to be small due to the fact that the industry structures its production around meeting the domestic needs for

butterfat, resulting in little surplus to export. Exports of butter for 2016 are forecast to remain steady at 2 TMT, the same level estimate for 2015 levels.

Consumption:

Butter consumption has been growing slowly over time, and is forecast to remain steady at 100 TMT in 2016. Based on 7 months of consumption data, butter is estimated to reach 100 TMT in 2015, a 2 percent increase over 2014 levels of 98 TMT. Butter demand from the processing sector remains strong.

Stocks:

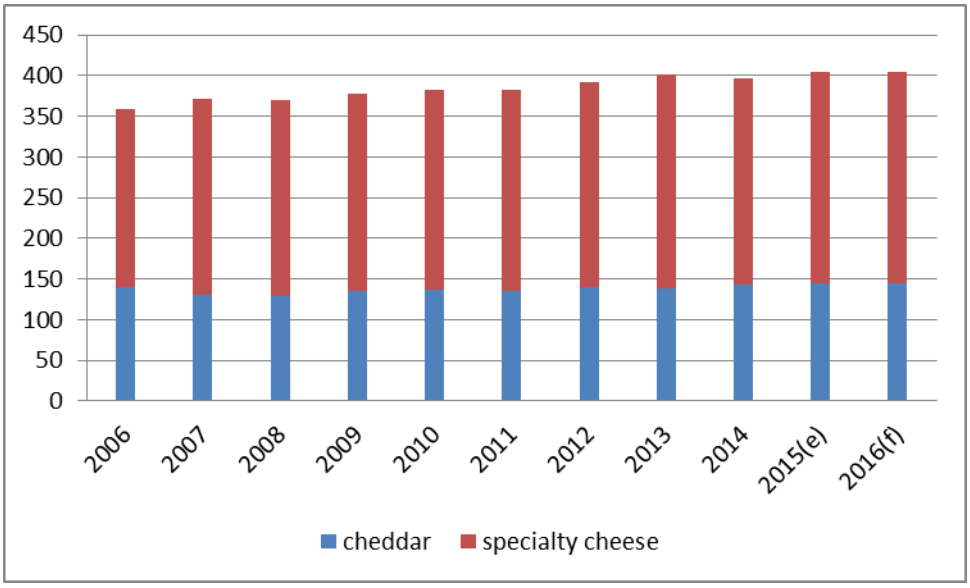
Increase in butter production will help rebuild stocks. Stocks are expected to be drawn down in 2015 due to domestic production not being high enough to off-set demand. A further increase in production forecast for 2016, combined with steady domestic consumption is forecast to result in an increase in stocks to 11 TMT.

CHEESE:

Production:

Cheese production has been slowly increasing over time in response to consumer demand. Most of this increase has been driven by an increase demand for specialty cheeses, and an increase in usage of cheddar cheese in further processed products (convenience foods). In 2016, cheese production is forecast to remain at 2015 estimate levels of 400 TMT. The one percent expected increase in 2015 over 2014 production numbers is in part being driven by cheese to be used in further processing as well as a need to build up stocks.

Figure 4: Cheese Production in Canada, 2006-2016(f), in thousand metric tons



Trade:

The commercial quota on cheese is 20,411,866 kilograms. Most cheese enters Canada either through the import quota system, which is filled every year, or through import for re-export programs which goes into further processed products which are then exported. The European Union has country-specific access to 66 percent of the global quota, the rest of the quota is non-EU cheese which is mostly filled by the United States. Due to the tariff quota system, imports remain relatively stable and are forecast to reach 25 TMT in 2016, the same levels expected for 2015. The popularity of import for re-export programs for cheese is unlikely to decrease despite the strong U.S. dollar in comparison with the Canadian dollar. Exports for Canadian cheese containing processed products will likely increase and off-set the negative impacts of the weaker Canadian dollar on IREP cheese imports.

Cheese exports are partially limited by export subsidy commitment levels of 9 TMT tons and outlays of C$16 million. In 2016, cheese exports are forecast to remain at levels similar to year 2015 levels of 9 TMT. Year 2015 cheese exports estimated are based on 7 months of trade data.

Consumption:

Cheese consumption in Canada has been growing slowly but steadily. In 2016, cheese consumption levels are forecast to at 2015 estimated levels of 416 TMT. This represents a nearly 3 percent increase over 2014 levels. There is increased consumer demand for specialty cheeses, as well as an increased usage of cheddar cheese in further processed products.

Stocks:

Cheese stocks in 2016 are forecast to be drawn down slightly, and remain level in 2015.

SKIM MILK POWDER:

Dairy, Milk, Nonfat Dry	2014		2015		2016	
Market Begin Year	Jan 2014		Jan 2015		Jan 2016	
Canada	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Beginning Stocks	25	25	24	34	0	42
Production	77	81	80	84	0	85
Other Imports	6	6	3	3	0	3
Total Imports	6	6	3	3	0	3
Total Supply	**108**	**112**	**107**	**121**	**0**	**130**
Other Exports	13	13	11	13	0	13
Total Exports	13	13	11	13	0	13
Human Dom. Consumption	70	64	71	65	0	69
Other Use, Losses	1	1	1	1	0	1
Total Dom. Consumption	71	65	72	66	0	70
Total Use	84	78	83	79	0	83
Ending Stocks	24	34	24	42	0	47
Total Distribution	**108**	**112**	**107**	**121**	**0**	**130**
(1000 MT)						

Production:

Skim milk powder production in 2016 is forecast to rise to 85 TMT in response to increased butter production. Skim milk powder production in 2015, based on 7 months of production data, is expected to reach 84 TMT. This represents a nearly 4 percent increase over 2014 levels. This increase is the result of an increase in butter production.

Trade:

Skim milk powder comes into Canada under the import for re-export program and volumes vary between 3 and 5 TMT per year. Skim milk imports in 2016 are forecast to be 3 TMT which are average levels. Seven months of trade data for 2014 suggests that skim milk powder imports will be 3 TMT.

Skim milk powder exports are partially limited by annual export subsidy commitment levels of 45 TMT, and outlays of $31 million. The fact that there is a higher demand for butterfat that skim milk powder in Canada has led to a structural surplus which results in Canada trying to maximize skim milk powder exports while respecting its export subsidies commitments. The high domestic price for skim milk powder means that Canada hits the financial limit before it hits the volume limit. A weaker Canadian dollar in 2015 and 2016 will support increased exports. Post forecasts that skim milk powder exports in 2016 will be 13 TMT, the level estimated for 2015.

Consumption:

The use of skim milk powder in the Greek yogurt, has proven very popular with Canadian consumers and has helped maintain a steady demand for skim milk powder. Despite this demand, the domestic consumption of skim milk powder has been decreasing in recent years, in part due to available substitutes that come in duty-free. Some policy changes being considered include placing a cap on the amount of skim milk powder that the Canadian Dairy Commission will buy back from dairy processors. This may result in increased usage of domestic skim milk powder. Domestic consumption of the skim milk powder is forecast to reach 69 TMT, a 6 percent increase over year 2015 estimated consumption levels of 65 TMT.

Stocks:

In recent years, the availability of substitutes for domestic protein combined with an increase in butter production has led to increasing stocks. In 2016, stocks are forecast to increase to 47 TMT. Stocks in 2015 are expected to increase to 42 TMT.

TRADE

Import Controls:

Quantitative restrictions in ten categories of dairy products were converted to TRQs to support supply management of industrial milk under the Canadian Dairy Commission Act and as a result of the agreement at the World Trade Organization (WTO) in 1994. Canada undertook an Article XXVIII action in 2008 to create a new TRQ for milk protein substances in chapter 35. Due to the North American Free Trade Agreement, the TRQ cannot be applied against U.S. trade.

Information on the tariff utilization rates and quota holders for various dairy products can be found at the following URL address:
http://www.international.gc.ca/trade/eicb/agric/milk-en.asp

The legislation and regulations that underpin the import controls can be found at the following URL address:
http://laws.justice.gc.ca/en/E-19/index.html (Export and Import Permits Act)

The market access given to dairy products in Canada are presented in the table below.

Table 1: Market Access Given to Dairy Products:

Dairy Product Description	**Access in tons**	**Tariff Item Number (to 6-digit)**
Milk Protein Substitutes	10,000	3504.00.11, 3504.00.12
Fluid Milk[1]	0	0401.10, 0401.20
Cream, not concentrated, no sugar, (heavy cream)	394	0401.30
Skim Milk Powder	0	0402.10.10
Whole Milk Powder, whether or not Sweetened	0	0402.21, 0402.29
Concentrated and Evaporated milk	12	0402.91, 0402.99
Yogurt	332	0403.10
Powdered Buttermilk	908	0403.90
Liquid Buttermilk, Sour Cream	0	0403.90
Dry Whey	3,198	0404.10
Products consisting of natural milk Constituents	4,345	0404.90
Butter, fats and oil from milk	3,274	0405.10, 0405.90
Dairy Spreads	0	0405.20
Cheese	20,412	0406
Ice cream mixes	0	1806.20, 1806.90
Ice Cream and other edible ice	484	2105

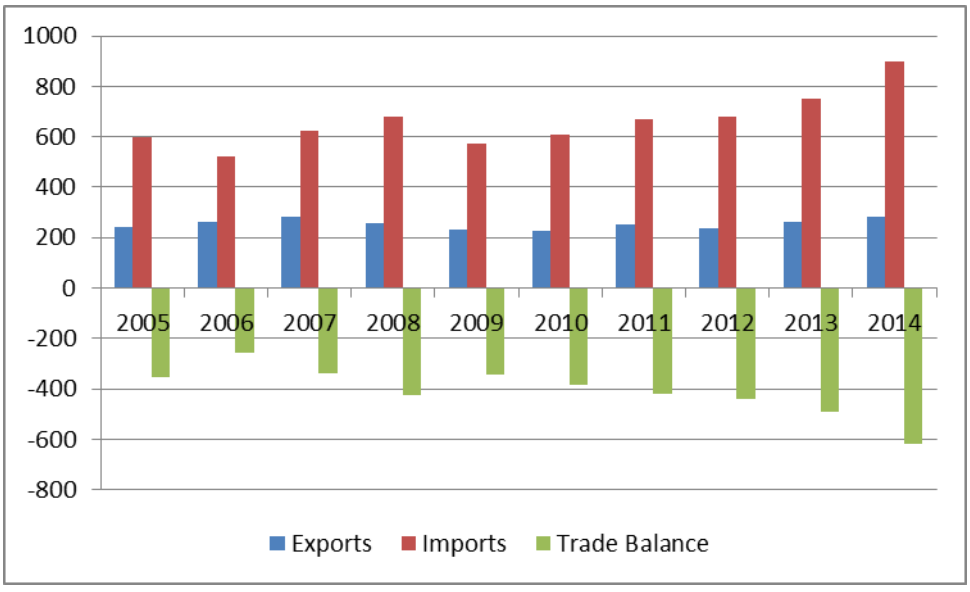
Milk cream and butter subs.	0	2106.90
Non-alcoholic beverages containing milk	0	2202.90
Complete feeds and feed supplements	0	2309.90

[1] There is no commercial TRQ for fluid milk. However access of 64,500 tons of fluid milk is allowed and considered filled by cross-border shopping.
** not applicable against countries with which Canada has a FTA

Export Limitations:

The 2002 ruling by the World Trade Organization (WTO) capped subsidized exports of dairy products from Canada. As a result, given the high domestic price for dairy products in Canada, exports opportunities for the Canadian dairy industry are limited and results in a negative trade balance. Export subsidies for butter, skim milk powder, cheese and "other milk products" are subject to caps of 3.5 TMT (C$11.0 million), 45 TMT (C$31.2 million), 9.1 TMT (C$16.2 million), and 30.3 TMT (C$22.5 million), respectively. The most recent notification by Canada for export subsidies was made in July of 2015 for marketing year 2013/2014 and reported subsidized exports totaling 17.024 TMT (C$31.036 million) for skim milk powder, 5.787 TMT (C$15.430 million) for cheese, and 6.637 TMT (C$18.063 million) for other milk products. Canada reported no subsidized exports of butter. For 2014, the Canadian dairy trade balance remained at a deficit of over C$619 million, a 26 percent decrease over the previous year's level.

Figure 5: Dairy Trade Balance for 2014 (in Million Canadian Dollars)



Source: Agriculture and Agri-Food Canada, Dairy Division

More information on Canada's commitments and notifications to the WTO can be found at the following URL address: http://www.wto.org/english/tratop_e/agric_e/ag_work_e.htm

POLICY

Trans Pacific Partnership Deal Reached, Includes Concessions on Dairy:

On October 5th 2015, the government of Canada issued a press release announcing that the members of the Trans Pacific Partnership had successfully concluded negotiations on a free trade agreement. The final agreement included market access concessions on dairy products. While the full details of the TPP agreement had not been released at the time of the report, the Canadian government has assessed the sum of access granted in the Canadian dairy industry to be equivalent to 3.25 percent of Canada's 2016 milk production. According to a press release issued by the Dairy Farmers of Ontario, this is equivalent to 250 million liters of domestic milk production. The Canadian government has stated that a significant majority of the additional milk and butter will be directed to value-added processing. The Canadian government has also stated that it negotiated tariff elimination for specialty and artisanal cheese exported to the United States.

It has also been reported through other countries' various press releases that Canada will eliminate its tariff on milk protein substances upon entry into force of the TPP. The United States already has duty-free access under this line (35.04.00.11 (within access), 35.04.00.12 (over access)) due to the NAFTA. The quota limit which is applied to countries with whom Canada does not have a free-trade agreement is 10 TMT. The TRQ on whey powder will be eliminated over a 10 year period. The Australian government reports that under TPP additional access will be granted for cheese, milk powders and butter.

The Canadian Department of Foreign Affairs, Trade and Development (DFAT-D) summary of the benefits of the agreement can be found at the following URL address:
http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/tpp-ptp/benefits-avantages/sectors-secteurs/01-AgriSector.aspx?lang=eng

The Australian government's summary of market access for goods in the TPP can be found at the following URL:
http://dfat.gov.au/trade/agreements/tpp/outcomes-documents/Pages/outcomes-goods-market-access.aspx

Market access for goods summary sheets are available from the New Zealand government from the following URL address:
http://tpp.mfat.govt.nz/assets/docs/TPP_factsheet_Goods-Market-Access.pdf

(a) Support Programs Promised

In parallel with this announcement, the Canadian government also announced that it would provide C$4.3 billion over 15 years in support to the supply management sector during the implementation of the TPP agreement and the Canada-EU trade Agreement (CETA) that has yet to be ratified.

Programs promised to be delivered to the supply management sector (which includes the poultry sector as well as dairy) include:

- C$2.4 billion will be made available through an Income Guarantee Program which is designed to provide supply-managed producers 100 percent protection for a full 10 years from the day TPP comes into force. Income support assistance will continue on a tapered basis for an additional five years, for a total of 15 years.

- C$1.5 billion will be made available through the Quota Value Guarantee Program. It is designed to protect producers against reduction in quota value when the quota is sold following the implementation of TPP. This demand-driven program, will be in place for 10 years.

- C$450 million will be made available through a Processor Modernization Program and will provide processors in the supply-managed value chain with support to further advance their competitiveness and growth.

- C$15 million in new funding will be provided to assist supply-managed groups in promoting and marketing their top quality products. The funding will be added to the AgriMarketing Program

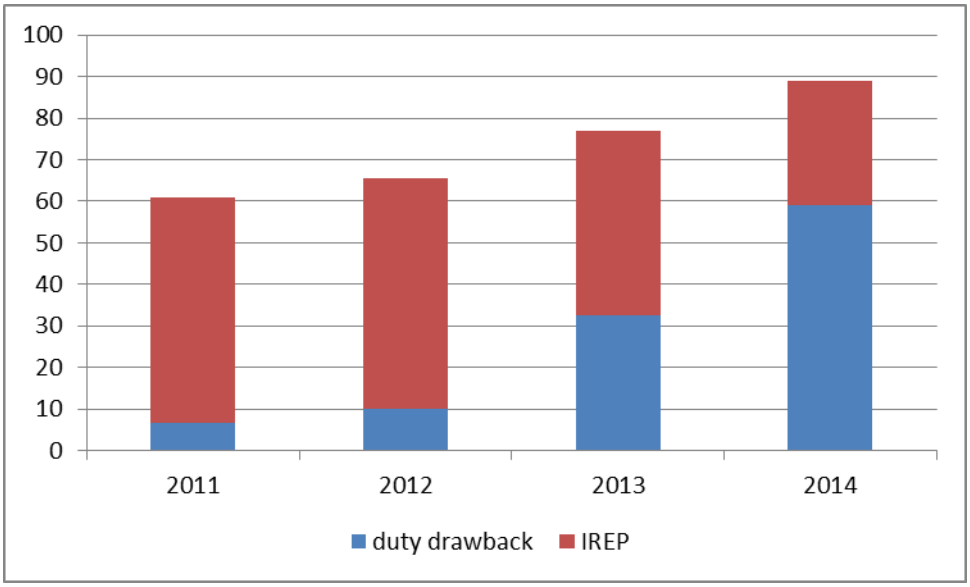
These programs were announced during an election campaign and it is unclear whether or not the current government is permitted to commit these funds to the supply managed sector. However, given the support for the supply management system from the opposing parties, it is unlikely that this promised support would be revoked should there be a change in government on October 19, 2015. One of the strongest lobby messages of the supply managed sectors in Canada has been the fact that they do not receive government subsidies. This will no longer be a viable lobby message once the TPP comes into force.

The program announcement can be found at the following URL address:
http://news.gc.ca/web/article-en.do?nid=1017899

(b) Tighter Border Controls Promised:

The Canadian government, through both the media release issued by Agriculture and Agri-Food Canada and in technical briefing call with stakeholders, has promised to intensify on-going circumvention measures that will enhance (Canada's) border controls. The press release made specific mention of the government's intention to exclude supply-managed products from the Government of Canada's Duties Relief Program which has been showing increasing usage by the Canadian dairy and food processing industry. By 2014, the total amount of dairy imports under TRQ entering through the Duties Relief Program had increased 9 times the levels experienced in 2011. This increase is largely due to the greater flexibility afforded through the program. Most imports are coming from the United States. ***Figure 6*** on the next page demonstrates the increased in dairy trade that has occurred under the programs that are conditional upon re-export.

Figure 6: Total Dairy Imports Under TRQ Entering Canada Under Programs that are Conditional on Re-Export, in MMT.

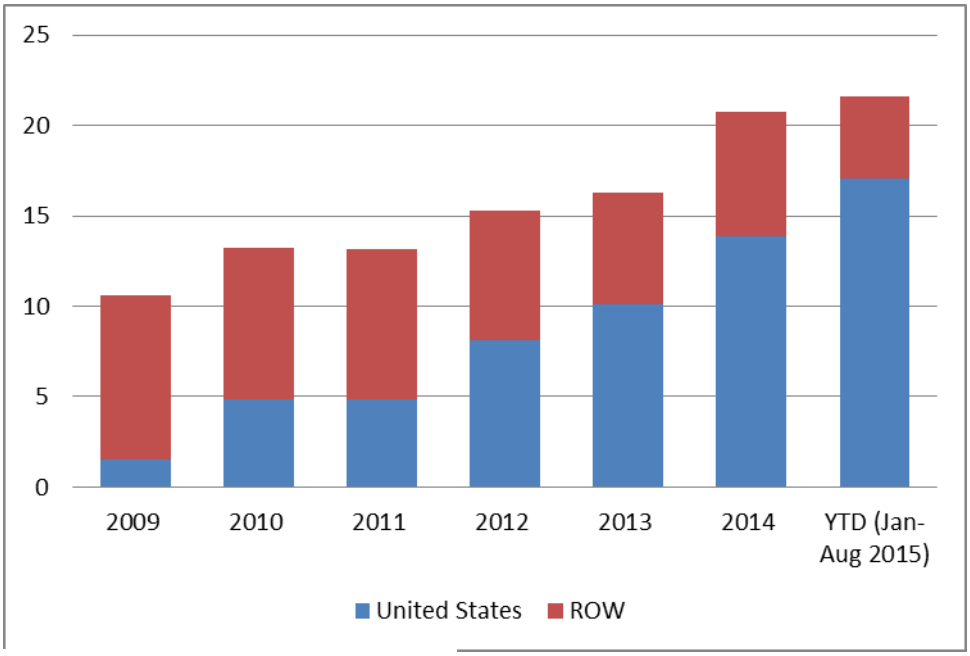


Source: Global Trade Atlas, Statistics Canada

Structural Surplus Growing:

The Canadian dairy industry continues to struggle with a structural surplus of solids non-fat (protein) due to the fact that the demand for butterfat significantly outstrips the demand for domestic protein. The system was designed to handle a structural surplus of 20 thousand metric tons but is now facing a structural surplus of close to 90 thousand metric tons. This surplus is in part due to imports of milk protein substances (35.04.00.11 and 35.04.00.12) which enter duty-free from the United States and which displace domestic protein resulting in income loss for Canadian milk producers. Trade under this line continues to grow year over year. The value of trade under 3504.00.11 and 3504.00.12 was US$ 172 million in 2014, with US trade valued at over US$ 100 million. In 2015, year to date trade (Jan-Aug) data shows the volume of imports (Jan-August) under 35.04.00.11 and 35.04.00.12 has already exceeded the levels reached at the end of 2014. US-origin imports account for 79 percent of the year to date trade. ***Figure 7*** on the next page shows the steadu increase in imports under these lines.

Figure 7: Imports of Milk Protein Substances under 3504.00.11 and 3504.00.12



Source: Global Trade Atlas, Statistics Canada

Now that the uncertainty around TPP has been eliminated, the focus of the industry is turning to how it will evolve in a post-TPP world. Of primary importance to dairy farmers is the loss of market share for protein and the growing structural surplus. At the provincial level, the Dairy Farmers of Ontario (DFO) announced on October 13th their intention to move forward unilaterally (in absence of a national strategy) on an ingredients strategy that would lower the price of milk protein to a competitive level (likely US or world price). According to the information posted on their website, DFO has made the request to the Farm Products Marketing Commission to create a non-contingent ingredients class with a target implementation date of February 1, 2016. The Farm Products Marketing Commission is the regulatory agency of Ontario that administers the legislation and regulation of the Farm Products Marketing Act and the Milk Act. DFO states that it is moving forward with support from the Ontario butter and powder processors, Gay Lea Foods and Parmalat. Should such a strategy move forward and be successful, it could have significant implications for demand of U.S.-origin milk protein substances.

Appendix 1

Dairy Items on Import Control List:
http://laws-lois.justice.gc.ca/eng/regulations/C.R.C.,_c._604/page-1.html#h-1

- **117.** Milk and cream, neither concentrated nor containing added sugar or other sweetening matter, of a fat content, by weight, not exceeding 6 per cent, that are classified under tariff item No. 0401.10.10, 0401.10.20, 0401.20.10 or 0401.20.20 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **117.1** Cream, neither concentrated nor containing added sugar or other sweetening matter, of a fat content, by weight, exceeding 6 per cent, that is classified under tariff item No. 0401.40.10, 0401.40.20, 0401.50.10 or 0401.50.20 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **118.** Milk and cream, containing added sugar or other sweetening matter, in powder, granules or other solid forms, of a fat content, by weight, not exceeding 1.5 per cent, classified under tariff item No. 0402.10.10 or 0402.10.20 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **119.** Milk and cream, in powder, granules or other solid forms, of a fat content, by weight, exceeding 1.5 per cent, not containing added sugar or other sweetening matter, classified under tariff item No. 0402.21.11, 0402.21.12, 0402.21.21, or 0402.21.22 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **120.** Milk and cream, in powder, granules or other solid forms, of a fat content, by weight, exceeding 1.5 per cent, containing added sugar or other sweetening matter, classified under tariff item No. 0402.29.11, 0402.29.12, 0402.29.21 or 0402.29.22 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **121.** Preparations (other than preparations classified under tariff item No. 2106.90.31 or 2106.90.32 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*) containing more than 15 per cent by weight of milk fat, but less than 50 per cent by weight of dairy content, and suitable for use as butter substitutes, not elsewhere specified or included, that are classified under tariff item No. 2106.90.33 or 2106.90.34 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **122.** Milk and cream, not in powder, granules or other solid forms, concentrated (whether or not containing added sugar or other sweetening matter) or not concentrated (containing added sugar or other sweetening matter), that are classified under tariff item No. 0402.91.10, 0402.91.20, 0402.99.10 or 0402.99.20 in the List of Tariff Provisions set out in the schedule to the*Customs Tariff*.

- **123.** Powdered buttermilk, whether or not containing added sugar or other sweetening matter or flavoured or containing added fruit, nuts or cocoa, that is

classified under tariff item No. 0403.90.11 or 0403.90.12 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **124.** Buttermilk (other than powdered buttermilk), curdled milk and cream, kephir and other fermented or acidified milk and cream, whether or not concentrated or containing added sugar or other sweetening matter or flavoured or containing added fruit, nuts or cocoa, that are classified under tariff item No. 0403.90.91 or 0403.90.92 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **125.** Products consisting of natural milk constituents, whether or not containing added sugar or other sweetening matter, not elsewhere specified or included, that are classified under tariff item No. 0404.90.10 or 0404.90.20 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **125.1** Powdered whey, whether or not containing added sugar or other sweetening matter, that is classified under tariff item No. 0404.10.21 or 0404.10.22 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **125.2** Milk protein substances with a milk protein content of 85 percent or more by weight, calculated on a dry matter basis, that do not originate in a NAFTA country, Chile, Costa Rica or Israel and that are the subject of two commitments signed by the Government of Canada on June 12, 2008, one with the European Communities and the other with the Government of Switzerland, relating to the modification, in Canada's schedule of concessions pursuant to the Agreement Establishing the World Trade Organization, to Canada's concession on tariff item No. 3504.00.00 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff* with regard to those substances.

- **126.** Mixes and doughs, for the preparation of bread, pastry, cakes, biscuits and other bakers' wares classified under heading No. 19.05 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*, containing more than 25 per cent by weight of butterfat and not put up for retail sale, that are classified under tariff item No. 1901.20.11, 1901.20.12, 1901.20.21 or 1901.20.22 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **127.** Milk, cream or butter substitutes containing 50 per cent or more by weight of dairy content, not elsewhere specified or included, that are classified under tariff item No. 2106.90.31 or 2106.90.32 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **128.** Food preparations of goods of heading Nos. 04.01 to 04.04 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff* (other than ice cream mixes or ice milk mixes), containing more than 10 per cent but less than 50 per cent on a dry weight basis of milk solids, not in retail packaging, that are classified under tariff item No. 1901.90.33 or 1901.90.34 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **128.1** Food preparations of goods of heading Nos. 04.01 to 04.04 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff* (other than ice cream mixes or ice milk mixes), containing 50 per cent or more on a dry weight basis of milk solids, not in retail packaging, that are classified under tariff item No. 1901.90.53 or 1901.90.54 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **129.** Food preparations, not elsewhere specified or included, containing 50 per cent or more by weight of dairy content, that are classified under tariff item No. 2106.90.93 or 2106.90.94 in the List of Tariff Provisions set out in the schedule to the*Customs Tariff*.

- **130.** Non-alcoholic beverages containing milk (other than chocolate milk) and containing 50 per cent or more by weight of dairy content and not put up for retail sale, that are classified under tariff item No. 2202.90.42 or 2202.90.43 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **131.** Complete feeds and feed supplements, including concentrates, containing 50 per cent or more by weight, in the dry state, of non-fat milk solids (other than preparations classified under tariff item No. 2309.10.00, 2309.90.10 or 2309.90.20 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*), not elsewhere specified or included, that are classified under tariff item No. 2309.90.31 or 2309.90.32 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **132.** Chocolate ice cream mix and ice milk mix that are classified under tariff item No. 1806.20.21, 1806.20.22, 1806.90.11 or 1806.90.12 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **133.** Ice cream mixes and ice milk mixes, being food preparations of goods of heading Nos. 04.01 to 04.04 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*, containing more than 10 per cent but less than 50 per cent on a dry weight basis of milk solids, that are classified under tariff item No. 1901.90.31 or 1901.90.32 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **133.1** Ice cream mixes and ice milk mixes, being food preparations of goods of heading Nos. 04.01 to 04.04 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*, containing 50 per cent or more on a dry weight basis of milk solids, that are classified under tariff item No. 1901.90.51 or 1901.90.52 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.

- **134.** Ice cream and other edible ice, whether or not containing cocoa, other than flavoured ice and ice sherbets, that are classified under tariff item No. 2105.00.91 or 2105.00.92 in the List of Tariff Provisions set out in the schedule to the *Customs Tariff*.