

Make Informed Decisions

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Olymel Re-Alignment

On October 22, Olymel announced that it decided to reduce the volume of its live hog purchases by 25,000 per week starting March 2022. The notification went on to say the following:

This decision is made necessary with the current market conditions. In addition, faced with a labor shortage that is hitting hard in Quebec, Olymel must achieve a better balance between available labor and the company's ability to produce a larger share of added value products in order to reduce losses incurred in recent months.

In order to improve our profitability and achieve our goal of reducing live hog purchases, Olymel management has also taken the decision to modify the vocation of Olymel's pig slaughtering and cutting plant in Princeville, in the Center of Quebec, and to cease its slaughtering activities there starting March 2022. All the activities of this plant will then be divided between the cutting, boning and packaging of pork products...

...15,000 hogs from Quebec are affected, while approximately 10,000 hogs from Ontario will also be affected by this decision starting in March 2022. Despite this decision, Olymel will continue to assume its responsibilities with regards to addressing the current backlog of live hogs.

Princeville Changes Role

There are many issues and ramifications associated with this move as outlined in the company release shown above. I will get to those at a later date. First it is best to try to understand what is being done.

Regarding Princeville, I expect from Olymel's perspective the key driver is what they stated in the first paragraph above. The company needs to be able to add value to their pork production to a certain base level. To do that, given labor shortages, they need to reduce their slaughter numbers. That is a stark reality check about labor availability. That puts the small 2,700 head per day Princeville plant into focus. I think the company assessed that the hog slaughter may not be too important at Princeville, but the labor is critical.

There are many experienced and skilled workers at Princeville. Olymel wants to keep those staff. Princeville workers will finalize value adding to production that cannot be done at other Olymel packing plants.

The decision was to use the skill and available labor at Princeville to help close the loop on value added. It is widely known in the Canadian industry that without value added, bone-in product revenue is generating very depressed returns for Canadian packers. It is not sustainable. That is particularly the case given the loss of China and with prospects there being so uncertain.

Quebec Regulated Price Makes It Worse

This lack of value-added revenue is extra problematic in Quebec given the regulated price that packers are forced to pay. As noted in this last report, October 18, the Canadian cutout value is far short of the U.S. cutout. Nevertheless, due to the regulated pricing scheme, Quebec packers are forced to pay for hogs based on the U.S. cutout. I expect that makes a very bad situation on the revenue side doubly untenable given the inflated regulated hog cost. Packers in Quebec are paying a value-added hog cost without the value-added pork revenue.

Of course, the labor woes generated by COVID made this situation even worse. The problem and precariousness of the labor supply were evident long prior to 2020. Prior to COVID labor issues, however, the Chinese market was looking good. Value adding was not a big part of that trade so there was a false sense of a workable condition. That situation, of course, was very fragile given the nature of China as a trading partner.

Now given the Chinese bans on Canadian plants, that false sense of a workable arrangement is widely and harshly exposed. That is not a workable business model. Olymel, and probably all Canadian packers, would have had to double back and re-think its plans. The only way to survive for many, if not all packers, is to value add.

25,000 Reduction

The Princeville plant has been harvesting about 9,000 a week recently. Olymel, however, is going to reduce its slaughter by about 25,000 a week. The 25,000 reduction would logically be a way to balance the available value adding capability with the volume of hogs. This reduction would probably allow the minimum amount of value added that is needed to make it work from a revenue perspective. It was likely an arithmetic outcome when combining human resources with operations.

The breakdown of the 25,000 head decrease is comprised of 15,000 from Quebec and 10,000 from Ontario. That breakdown would have considered several factors, including Olymel's cooperative shareholder suppliers, long term supply agreements in Ontario, as well as the company's commitment to Quebec.

I expect that the first hogs that would have been reduced would have been the numbers that Olymel inherited when Breton cut back on commodity production. When Breton went 100% to its niche market production, it had surplus commodity hog supplies. Those 6-8,000 hogs went to Olymel at that time.

Counter to Packer Instinct

There are several ramifications and nuances related to this decision. They will be explored later. The key point to consider for now is that this decision demonstrates how serious the labor problem is for this industry. A packer cutting kills is counter to every instinct and impulse in the industry. It is the last choice in an industry that is all about market share and operational efficiency. The company in Quebec will go from harvesting about 140,000 a week (when Vallee Jonction is fully back) to 115,000 a week. Some plants will be running at 50-60% capacity. That is completely counter to every packer's operational culture and focus.



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November 2021

A version of this paper first appeared in the November 1 edition of Canadian Pork Market Report. If you would like a free two-month trial, please send me an email, kevin@kevingrier.com