

**Positioning for Sustainable Growth: A Case Study of SMEs in
Canada's Consumer Products Industry**

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Introduction

This paper aims to analyze the differences in the strategies pursued by successful and unsuccessful organizations. We were drawn to this subject by an instinct that weak strategic alignment between firms and their respective industry contexts creates the foundation for firms to commit a range of other errors. This belief has been validated in post-mortem analyses of the accounting scandals of the earlier part of this decade.¹

While there is no shortage of this type of analysis in relation to large organizations over long time horizons, there is a dearth of research into the specific opportunities and challenges associated with the strategic choices of smaller firms. Accordingly, we have opted to focus our investigation on small and medium-sized enterprises (SMEs) in an effort to address this gap. Moreover, we believe this is an important subject given the role such enterprises play in economic development, specifically, creating new employment, developing and launching new products and cultivating new markets. Our overarching objective is to provide insights that will assist business leaders in making value-creating decisions.

For our purposes, “success” will be defined as creating the strategic preconditions for sustainable growth. While this might appear to be a somewhat vague objective, it is also an important one for many entrepreneurs. In a nutshell, they seek to build businesses that will outlast them. This is a notable contrast to the objectives of other business stakeholders: private equity firms strive to generate annual returns in excess of 20%+ on their investments over an average five-year time horizon; professional managers are largely focused on securing performance targets to drive incentive compensation; institutional investors want stocks that will outperform their benchmark.

In contrast, laying a foundation for sustainable growth implies a focus on careful business model and market participation choices that culminate in a vision of a larger, more profitable firm. Importantly, while the investment objectives cited above can drive strategic choices that are not aligned with sustainable growth, all theoretical valuation models rest on this principal through the concept of discounted future cashflows. In short, the ability to position a firm for sustained growth will always maximize the value of an enterprise.

While ideally one would seek to derive strategic principles that can be generalized across all industries, realistically, we determined that certain industries would have unique preconditions for growth. For example, firms operating in the natural resource sector are driven to a much greater extent by global commodity prices than other firms. Similarly, high tech firms rely to an inordinate extent on technological advancements. Accordingly, we chose to focus on the Consumer Products sector of the Canadian economy because it involves a relatively balanced consideration of all of the classic management disciplines: innovation and product development, marketing and branding, operational excellence, and supply chain management. The focus on our home market was driven in large measure by familiarity with the data sources and the availability of personal insights from managers with experience operating in this environment.

After struggling with various size thresholds, we opted to define our universe as publicly-traded firms whose sales were less than \$250 million in 2000². This choice aligned reasonably well with the definitions of SMEs we encountered in the literature, including Carson et al³, who suggested

¹ Robert M. Grant and Massimo Visconti, Reputation and Transparency: Lessons from a Painful Period in Public Disclosure, Long Range Planning, Volume 39, Issue 4, August 2006, Pages 361-383.

² Some firms were constituents of the sector in 2000, while others have entered the index subsequently.

³ Carson, D.J., Cromie, S., McGowan, P., and Hill, J., Marketing and Entrepreneurship in SMEs: An Innovative Approach, Prentice-Hall, London, 1995.

that such firms have little impact on their surroundings and have limited power to modify environmental forces to their advantage. In other words, they accept industry price/value tradeoffs, their supply does not significantly impact the overall market, and they are in most respects the weaker negotiant in value chain relationships. We chose, rather arbitrarily, to analyze the strategic choices made by these firms during the period from 2000 through 2005.

This scope resulted in a universe of over forty companies, spanning everything from home security and gaming, to food processing, broadcasting and building products. This was an impractical sample given the time allotted for this project, so we opted to focus on the two largest and most homogeneous sub sectors: food and alcohol beverages, which provided a sample of fifteen publicly-traded firms. We added one private firm to the sample due to its particular fit and our unique access to its senior management as a source of information. The list of companies with high level size data is included in Appendix 1.

Approach

We commenced this study with a review of existing literature that addresses the unique challenges and opportunities faced by SMEs. We provide a summary of the highlights from this literature.

The literature provides a reasonably consistent view of the objectives and priorities of SMEs through various surveys. There appears to be a near-universal focus on the following factors:

- attention to the needs of customers
- an external or market-focused orientation
- innovation
- quality
- talented employees.

We take these observations as given and focus on the following three things in our analysis of the companies in our sample:

- evaluating the strategies that are articulated by the sample companies in the context of how well they are likely to achieve these priorities
- identifying the differences between them that provide insights into potential future performance
- identifying signals for the intangible linkages between the factors that are instrumental to future success (ie. Integrative thinking)

The sample was analyzed as follows:

1. Prepared an analysis of the industry backdrop against which each firm was participating.
2. Compiled high level financial snapshots for each company over the five year horizon being examined (included in Appendix 2)
3. Reviewed key securities filings over the period to develop a chronology of the firm's key strategic choices leading up to and during the time horizon under consideration (the resulting detailed company summaries are included in Appendix 3)
4. Conducted interviews with senior managers at E.D. Smith Income Fund, Smucker Foods of Canada (a competitor to E.D. Smith), Give & Go Prepared Foods, Kensington Capital Partners (a private equity firm invested in Give & Go), Coolbrands and Moosehead Brewery. The insights from these meetings are incorporated in the Industry Backdrop and Company Summaries.

While this approach yielded interesting insights about the key success factors underpinning the performance of the firms in our sample, it does have some noteworthy limitations. First, the

analysis is confined to a discussion of firms' strategic choices as expressed through publicly-reported actions it has undertaken. The fact that these are public companies removes the possibility of understanding whether the underlying intent differed from reported events. Second, this approach of looking at strategic choices and their eventual financial outcomes makes it impossible to identify to what extent execution capabilities impacted the resulting performance.

Literature Review

At a high level, the research largely confirms the key success factors that are known to be important to larger firms, namely attention to the needs of customers, an external or market-focused orientation, innovation, quality and talented employees. Peeling back the onion, however, important questions remain unanswered with respect to how SMEs can compete in this context.

There are two primary schools of thought with respect to the role of strategic design in business performance: industry vs. resource-based. The industrial view advocated by McGahan⁴, posits that performance is dictated primarily by industry structure, because firms must conform to the dominant industry model. In contrast, the core of the resource-based view is that firms differ in fundamental ways as each has its own bundle of resources and capabilities.⁵

Clifford et al⁶ found that high growth companies exist even in declining industries, and hence, deny the conventional wisdom that growth can be achieved only in attractive sectors. Similarly, the strategic choice school of thought argues that strategies adopted by entrepreneurs are the dominant influence on a firm's growth. There is extensive literature to support the assertion that the entrepreneurial orientation of the owner or manager has been found to have a sustainable positive relationship with performance and competitiveness. However, there is also significant research evidencing the vulnerabilities of firm performance in the face of the limited knowledge and experience implied by such a “one-man show”.

We discovered a number of studies that examine the self-reported capabilities and priorities of rapidly growing firms.

O'Regan et al⁷ take the approach of contrasting high growth (defined as revenue growth of over 30% for three consecutive years) with other firms based on self-reported capabilities. Interestingly, high growth firms graded themselves substantially lower on about half the attributes, and rarely better than lower growth firms did. We wondered after reading this whether high growth firms are more modest in their assessment of their capabilities, indicating a higher performance standard that is reflected in their performance. In the alternative, rather than being the cause of high growth, it could also be the result, as rapid growth is destabilizing and can make it feel like the business is out of control.

Tonge et al⁸ surveyed 31 firms regarding the strategies they pursued on seven key areas that were identified from existing literature, seeking to differentiate between companies whose growth ranged from 20-30% and those whose growth was 40-50%. The key attributes were as follows: Ability to attract and retain quality staff, quality product/service, flexibility, early entry into growth markets, diversification, niche marketing, frequent innovation. They found the following:

- both groups of companies were focused on the same leadership features of direction, selection of key personnel and vision. Similarly, they both exhibited a strong focus on

⁴ A. McGahan, *How Industries Evolve*, Harvard Business School Press, 2004.

⁵ N. O'Regan, A. Ghobadian, D. Galleary, *In Search of the Drivers of High Growth in Manufacturing SMEs*, *Technovation*, 26, pp. 30-41, 2006.

⁶ D.K. Clifford and R.E. Cavanagh, *The Winning Performance – How America's High Growth Midsize Companies Succeed.*, Sidgewick and Jackson, London, 1985.

⁷ N. O'Regan, A. Ghobadian, D. Galleary, *In Search of the Drivers of High Growth in Manufacturing SMEs*, *Technovation*, 26, pp. 30-41, 2006.

⁸ R. Tonge, P.C. Larsen, M. Ito, *Strategic Leadership in Super-Growth Companies – A Re-appraisal*, *Long Range Planning*, Vol. 31, No. 6, pp. 838-847, 1998.

- customer-related activities such as adding new customers, understanding customer needs and increasing sales to existing customers.
- Supergrowth firms were more concerned with their competitive position than high growth ones, and stressed financial targets as a strategy
 - High growth companies were looking for a more balanced focus for the future between financial results, long-term performance capabilities and enhancing customer relationships
 - The supergrowth companies were a lot younger than the high growth ones, and there is evidence of convergence between them as the supergrowth firms mature.

While we found little to dispute these observed differences between supergrowth and high growth firms, we believe that it would be more meaningful to combine high growth and supergrowth firms into a single group, and contrast them with firms that are not growing at all.

The game theory approach articulated by Lee et al⁹ offered a particularly interesting view. Giving consideration to the resource constraints of small firms and the payoffs to larger players from various courses of action, they posit that it is more costly for the bigger firm to compete aggressively against the SME's entry when the SME follows the free-rider strategy, than when it follows the niching strategy.

They dispute the traditional explanations for why large firms avoid certain market segments (namely anti-trust considerations, fear of self-cannibalisation, or low perceived potential of the niche) because these essentially imply that the bigger firm is locked into inefficient practices and hence, is not able to adapt to the demands of the market niche. Rather, they propose that the bigger firms analyze the payoffs under various entry/accommodation/aggressive competition scenarios and make a rational decision to deliberately ignore the niches filled by the SMEs and to accommodate the entry of SMEs into their markets. Such a decision is taken because, direct competition with the SMEs depresses prices not only in the market niches, but also in all other market segments which are currently supplied with substitutable products by the bigger firms. The loss in margins, and hence profits, to the bigger firms in these other segments can be sufficiently large such that they prefer to adopt a "live and let live" attitude towards the SMEs which choose to supply the market niches.

Accordingly, they recommend that SMEs supply products that are substitutable to that of their bigger rivals' instead of totally differentiated ones. The more substitutable the SMEs' products are to those of their bigger rivals, the greater their losses due to depressed margins to the bigger firms if they choose to compete aggressively in the niches supplied by the SMEs. Although accommodation can cause the bigger rivals to lose some market share, it may still be less costly than aggressively fighting the entry by the SMEs and thus, they choose to accommodate. In the limit of substitutability, the SMEs can supply identical products to that of the bigger rivals and hence, free-ride on the latter's market development and promotions efforts.

An important caveat to the free-rider strategy is that the bigger firms will take the costly action of fighting SMEs if they think they can drive them from the market. Accordingly, signalling staying power is important, and Lee et al advocate the formation of strategic alliances to give credibility to the SMEs position.

⁹ Khai S. Lee, Guan H. Lim, Soo J. Tan, Dealing with Resource Disadvantage: Generic Strategies for SMEs, *Small Business Economics* 12: 299-311, 1999.

Davig, et al¹⁰ surveyed 75 manufacturing firms in the Midwestern U.S. to determine the performance benefits of implementing a balanced scorecard approach to strategic planning. They made the interesting discovery that there was no statistically significant difference in the performance of SMEs that claimed to have implemented a balanced scorecard and those that had not. They hypothesized that while certain firms were collecting non-financial supplementary data to measure customer perspectives, employee learning and business processes, these firms failed to use the data to analyze linkages between the factors and make appropriate improvements.

Innovation is an area that is also widely discussed in the literature. In a series of articles, Rothwell held that, although fundamental or radical invention ordinarily took place within either large firms or large public laboratories, small firms were disproportionately responsible for near-to-market developments and initial market diffusion. In fulfilling this role, small firms enjoyed unique advantages: lack of bureaucracy; efficient, often informal, internal communications systems; and flexibility and adaptability through nearness to markets. By contrast, small firms faced constraints associated with: lack of technically qualified labour; poor use of external information and expertise; difficulty in attracting/securing finance and relating inability to spread risk; unsuitability of original management beyond initial prescription; and, high cost of regulatory compliance. In essence, the advantages enjoyed by small firms are fundamentally behavioural, whilst constraints relate to resource.

In Freel¹¹, a random sample of 238 SMEs in the West Midlands of England were surveyed about their innovation and general organisational characteristics. Innovators were distinguished from non-innovators based on their rate of innovation, namely the relative benchmark of the number of new products introduced as a proportion of the firm's product base. They found that innovators were significantly more likely to have collaborated with business partners and universities. No other statistically significant differences were found between innovative classifications. Co-operation with suppliers or subcontractors was the most common form of arrangement, with 24.8 per cent of firms participating in a project of this nature.

A particular strategic choice that the literature indicates is a strong driver of performance is the behaviour of exporting. Studies indicate that exporters are likely to be more competitive than non-exporters. Hence, it is assumed that attributes related to exporters are closer to those of "best practice".¹² An export strategy is perceived as a vehicle for growth and enhanced profitability for SMEs. Firms may export to avoid stagnating because of limitations inherent in the local market. Limitations may include saturation, intensified competition, or a perceived lack of opportunities. Decisions to export may relate to a firm's size, competitive advantage, managerial characteristics, the amount of strategic opportunities abroad, outlook for domestic sales, and perceived ability to acquire information, to mention a few factors. Firms may also wish to acquire new skills and knowledge by exporting. The perception of this learning opportunity may increase a firm's tolerance of the lag in sales and profits that may occur in the early exporting stages.

¹⁰ William Davig, Norb Elbert, Steve Brown, Implementing a Strategic Planning Model for Small Manufacturing Firms: An Adaptation of the Balanced Scorecard, SAM Advanced Management Journal, pp. 18-24, 1984.

¹¹ Mark S Freel, **Barriers to product innovation in small manufacturing firms**, International Small Business Journal, Volume 18, Issue 2, pp. 60-80. 2000.

¹² Exporting Firms' Strategic Choices: The Case of Egyptian SMEs in the Food Industry

Industry Backdrop

Our sample covers two broad segments within the Consumer Products industry: alcoholic beverages (including both beer and wine) and food processing. The key features of these markets are described in the following section.

Food Manufacturing Industry

As a result of plentiful food supply, high concentration and intense competition in the food retailing sector, Canadian food prices are among the lowest in the world. These dynamics underpin an operating environment for food manufacturers that has long since been characterized by a high degree of rivalry.

More recently, competitive advances from discount and club formats (WalMart and Costco) have put traditional grocers on the defensive, and in an effort to retain market share, supermarket chains have undergone significant consolidation. They have utilized their growing scale with the following actions:

- They have leveraged their retail brands to develop robust private label programs in an effort to differentiate their assortment and reap higher margins. While private label penetration varies among grocery categories, it has approached 25% of retail volumes in recent years.
- An increasing proportion of the costs associated with private label product development are being pushed upstream to manufacturers¹³, who are effectively being used as pawns in retailers' category management efforts.
- While not a new phenomenon, retailers continue to squeeze suppliers for greater promotional allowances both in terms of one-time slotting fees as well as better ongoing incentives
- Initiated a trend toward consolidation of the mix of grocery and mass products, and as a result, a consolidation of suppliers. The top ranked branded manufacturers benefit from this expanding market place, but also face increased pressure to keep costs down, as retailers demand aggressive pricing to enhance their ability to compete

The U.S. retail market is more fragmented and regional in nature, and as such, there is generally a better balance in negotiations between suppliers and retailers.

Private label penetration south of the border is about half of the level it is in Canada, so the competition between national and store brands is less intense. This dynamic has provided opportunities for Canadian manufacturers to leverage their experience in supporting private label development in that market. Store brands also tend to serve a slightly different function in the U.S. While in Canada the focus is on achieving a differentiated assortment, south of the border, private labels tend to occupy the position of a value alternative. This results in U.S. consumers being able to purchase private label food and beverage products at an average discount of approximately 23% to comparable national brands¹⁴.

The Alcohol Beverage Industry

One feature that differentiates the Canadian alcohol beverage market from its food counterpart is the high degree of government participation in the distribution and retail elements of the value chain. This participation has taken various forms, ranging from interprovincial trade barriers, tax subsidies and retail monopolies. Generally speaking, however, these government controls have

¹³ An industry participant indicated in our interviews that Loblaw's product development team has been pared from 80 people down to six in recent years.

¹⁴ E.D. Smith IPO Prospectus,

fostered a protectionist environment that has been characterized by a relatively low degree of rivalry.

This low degree of rivalry is manifested in the proliferation of brands, each with a tiny share. While the average large grocery store might carry three brands of ketchup, Ontario consumers are able to choose from over 100 different brands of beer, and even more varieties of wine. As a small fraction of these brands comprise the lion's share of sales volumes, a rationalization of SKUs seems inevitable if competition ever comes to alcohol beverage retailing.

Because provincial governments have historically had a high degree of involvement in regulating the distribution of alcohol beverages, distribution is primarily a regional business. Accordingly, the nature and extent of rivalry and value sharing across the value chain varies materially across jurisdictions. This variability has tended to increase the operating risks associated with entering new jurisdictions, effectively serving as a barrier to entry. In each of the provinces of Canada (excepting Newfoundland, Quebec and Alberta) manufacturers primarily distribute their products through provincial government-operated outlets or independent licensed retail outlets. In the other provinces and in the U.S., manufacturers create their own distribution networks, and as a result, industry rivalry is more intense due to the presence of competition at multiple stages of the value chain¹⁵. Moreover, these wholesalers have experienced consolidation in recent years, which has in turn driven optimization of their supplier relationships that has placed small manufacturers at increasing risk. Accordingly, the U.S. market for alcoholic beverages has been particularly challenging as manufacturers have been squeezed by both their peers and downstream partners.

Trade issues at the inter-provincial and international levels have had a significant impact on the Canadian alcohol beverage industry. Historically, provincial regulations generally required Canadian manufacturers to operate a facility in a particular province in order to obtain favourable pricing and distribution access in such province. This requirement severely limited manufacturers' ability to distribute their products inter-provincially. This, and similar trade barriers restricting imports were removed in 1995, sparking a wave of industry consolidation that continues today.

The Canadian alcohol beverage industry has experienced destabilization as a result of trade liberalization - the General Agreement on Tariffs and Trade ("GATT") between Canada and the European Community and the Free Trade Agreement ("FTA") between Canada and the United States, mandated the phasing out of retail mark-up differentials on domestic versus United States and European products over the period ending in January, 1998.

Concentration in the Canadian beer industry is extremely high, with leaders Molson and Labatt controlling some 87% of the market. Sleeman was the nation's third-largest producer with 5% share when it was acquired in mid-2006. Labatt and Molson (both acquired by foreign firms in recent years) produce products that are marketed to appeal to a broad range of consumers. In order to maintain competitive prices and higher volumes, and to capitalize on the economies of scale that are inherent in mass production, these beers are produced in larger breweries. Historically, these brewers competed primarily based upon advertising; however, price-based and promotional competition has been an increasing feature of the market as it attempts to defend itself against incursions from the value segment. Premium brands are priced at a 10-25% premium to the mainstream brands, while value brands are priced at a 15-30% discount to the mainstream.

¹⁵ Distribution costs for Canadian manufacturers selling in the U.S. are augmented further by the participation of a national importer.

The dynamics of the Ontario market are somewhat different insofar as the mainstream producers' collective share has declined to 80% with the rapid growth of value and premium brands; these currently occupy roughly 33% and 15% of the market, respectively. Niche providers Lakeport and Brick have gained significant market share in recent years with a strong focus on value brands. This growth has been assisted by significant government subsidies for microbreweries in the form of reduced taxes. Importantly, government regulation imposes a minimum legal price for beer, so manufacturers are prevented from destructive pricing.¹⁶

Industry reports indicate that approximately 57% of the average retail price of beer consists of bottle deposits, taxes and service fees (which are paid to the distributor). That proportion is 69% for beer sold in the value segment.¹⁷ The cost of producing beer (including all taxes and fees that are passed along to the consumer) is fairly uniform throughout the country. For the brewer, the balance of costs is allocated among packaging, raw materials, labour, plant operations and other costs.

Packaging is an important element of beer industry competitive dynamics. Beer is a product that consumers select primarily for the lifestyle attributes with which brands are imbued. In a nutshell, it is a "badge" product, and packaging forms a significant part of each brand's badge. The majority of Canadian brewers utilize a common, refillable 341 ml bottle commonly known as the industry standard bottle (ISB). The ISB is characterized by amber glass and a twist off cap. Brewers' use of the ISB results in environmental benefits and significantly reduced purchasing, distribution, warehousing and sorting costs. The corollary of using the ISB is a barrier to entry in the form of surcharges for the use of non-standard bottles. This industry structure developed for the benefit of the dominant players Molson and Labatt, who own the monopoly distributor, The Beer Store (TBS). In 2002, TBS attempted to deny Brick Brewing access to the industry standard bottle if it continued to use the "stubby" bottle for some of its brands. The resulting lawsuit between Brick and TBS has yet to be resolved, but the situation provides evidence of the potential perils of what is generally a reasonably benign industry structure.

Apart from Molson Coors, Labatt and Sleeman, the balance of the Canadian beer market tends to be served predominately by regional brewers. The relatively high cost of transportation and distribution has been a primary driver in the development of the regional focus of the majority of Canada's brewers. Apart from dominant players Molson Coors and Labatt, Sleeman is the only player that has successfully extended its brands into multiple regions from a single market.

The Canadian wine industry is much more fragmented than the beer market. When it was acquired by a foreign player in 2005, market leader Vincor had only a 21% share, and its closest competitor was roughly half that size. Like the beer market, however, it has been in the midst of significant consolidation that promises to increase concentration levels and competitive intensity.

The wine industry is subject to significant fluctuations in raw material supplies and prices. The global production of wine-grapes has been steadily increasing over the last two decades, driving a sustained surplus of wine production that has annually exceeded global consumption by

¹⁶ In Ontario, each brewer listed with TBS receives weekly price change notifications from TBS. This pricing transparency permits brewers to respond to their competitors' pricing strategies with minimal lag-time.

¹⁷ Lakeport IPO Prospectus, June 2005, p. 24.

approximately 20%. The vast majority of this surplus has been in lower quality grapes that are grown in the European Union and are unsuitable for the production of the premium wines. At lower quality levels, this has resulted in lower bulk wine prices, which have reduced the cost of popular priced wines. At higher quality levels, certain producers have sought to clear their oversupply by blending the surplus ultra-premium wine with super-premium wines to improve flavour and overall quality or by reducing prices to clear inventory. This increased supply of premium wine has placed some margin pressure on the premium segment. Finally, the raw material price volatility experienced by Canadian manufacturers is heightened by the fact that regulators require specified amounts of grapes to be procured from local sources, which can be significantly disrupted due to weather conditions in any given year.

Beyond these unique attributes, the food and alcohol beverage industries have several attributes in common:

They are mature, multi-billion dollar markets – The retail value of beer and wine sold in Canada is roughly \$11 billion annually¹⁸ and while selected segments have experienced growth, in aggregate the market is essentially flat. The food market is much more difficult to define given the range of product categories and channels through which they are distributed. Nevertheless, using annual grocery chain sales of roughly \$60 billion as a proxy, it is fair to say that the manufactured food component is a similar order of magnitude size as the alcohol beverage market. Given an already vast array of products and limited population growth, expansion opportunities are similarly modest.

Products are developed for mass market consumption by the same end consumer – All of the companies in our sample are in a continuous battle for the hearts and minds of consumers. This is a challenge because while consumers can exhibit very stable behaviours and brand loyalty in some categories, in others, their tastes can be quite fickle. A macro trend toward healthier lifestyles has been adding increasing volatility to numerous categories as low fat (ice cream), low sugar (fruit spreads) and low carb (beer) trends come and go.

Consumer markets have become increasingly bifurcated - Mainstream mid-market brands have become commoditized, and as a result, lost share to both value (eg. private label) and highly differentiated premium products (eg. Haagen-Dazs ice cream, Jones Soda). This trend has been mirrored in the beer industry; as the aggregate market has stagnated, the premium and value categories have been growing at rates in excess of 15% p.a.

The competitive landscape has consolidated and is increasingly characterized by the presence of one or two industry giants which dominate the market – Both the food manufacturing and alcoholic beverage markets have undergone significant consolidation whereby multinational consumer firms have acquired vast portfolios of brands from companies operating in a small number of categories. These portfolios are typically comprised of a mix of very profitable category leading brands along with other secondary or regional brands. Manufacturers typically take a portfolio approach to managing the brands that they steward, waging periodic share wars in an effort to increase sales volume and profit margin. This consolidation has brought an increasing degree of globalization to the market for consumer packaged goods, whereby regional and national firms (SMEs) compete against multinational behemoths like Unilever, Nestle, Kraft and the like.

¹⁸ The \$11bn market is roughly 70% beer and 30% wine.

End markets are accessed through an increasingly consolidated network of retail distributors – There is significant concentration in the distribution networks available to the companies in our sample. The Canadian supermarket retail channel is dominated by four firms (Loblaws, Sobeys, Safeway and Metro-Richelieu) which serve some [80%] of the domestic market. Similarly, distribution of alcoholic beverages is done either through government-controlled boards, as in most of Canada, or regional wholesalers as in the U.S. In all cases, there are a limited number of distribution options available to manufacturers.

They are exposed to significant regulation governing the composition, manufacture and distribution of their products – Food and beverage manufacturers are regulated by federal, provincial and local laws and regulations regarding such matters as licensing requirements, trade and pricing practices, permitted and required labeling, advertising, promotion and marketing practices, relationships with distributors and related matters.

Analysis

The companies in our sample fall into three performance categories over the five-year time horizon we examined. These are colour-coded in our summary in Appendix 1:

- High growth in sales and operating profit (Brick, Lakeport, Vincor, Jones, Give & Go)
- Modest growth in sales and operating profit (Sleeman, Magnotta, Peller, Lassonde, E.D. Smith, Dover, Sun-Rype)
- Declining sales and operating profit (MRRM, Sepp's, Beaumont Select)

Coolbrands is an outlier among the sample, having experienced significant revenue growth but a significant drop in operating profit in 2005.

Looking at the more successful companies in the sample, a handful of common traits are apparent:

Focus

With the exception of Brick, all of the high growth companies demonstrate a high degree of focus in their market participation choices. Lakeport focused on distinct segments within a specific market that had been identified as having a different set of customer needs than the mainstream. Vincor and Give & Go displayed a similar focus on the emerging needs of their respective customers on a broader geographic scale. Jones did the same in a North American context, but in an extremely narrow product niche.

Focus is important because it amounts to diminished competition. However, it also reduces operational risk because you only need to be really good at a limited array of things. Both of these factors are important to leveling the playing field for SMEs. The inability to play in two distinctly different categories was a key element in Sleeman's ultimate failure, and likely explains Lakeport's outperformance relative to Brick in the value category.

The challenge with focus, of course, is that it limits the size of the potential opportunity. While Lakeport has experienced tremendous success in the Ontario value-priced beer market, it is already running up against the confines of this segment. In order to grow further, it will have to take the risk of either entering new segments in the same geographic market or attempt to replicate its strategy in another market. The challenge with the former is that its capabilities are focused on the value segment. The latter assumes that another player has not already copied Lakeport's strategy in their home market.

The corollary of the strong focus exhibited by the successful companies is the tendency of the unsuccessful firms to attempt too broad of a scope. Sepp's provides a dramatic illustration of this characteristic; it operates in two distinctly different food categories, prepared foods and bakery, markets both branded and private label products as well as performing co-packing services for other manufacturers, and does all of this from plants in three different provinces and sells its products to customers on three continents. A \$1 billion business might be able to sustain the geographically dispersed operations management, quality control, distribution network, sales and product development expertise necessary to succeed with this operational scope; however, it is implausible for a \$22 million company to do so.

Innovation

While it took different forms among the most successful companies, innovation played a key role in each:

- Jones has demonstrated an ability to create a new brand in an innovative way; its stated business model is in effect an attempt to formalize the process for doing this by

- consistently and intimately engaging its customers in a creative rather than high cost fashion.
- Lakeport took a unique approach by focusing exclusively on the value beer category. This provided an authenticity to its messaging that was compelling to consumers in a way that hybrid producers' was not. This proved critical in a "badge" business like beer, where consumers make brand choices as a reflection of their personality more so than in other categories.
 - Brick innovated by changing the value equivalence line in the mainstream beer industry. While Sleeman used innovative packaging to differentiate its premium beers and Lakeport injected new life into the value beer category by cutting prices to the legal limit, Brick combined the two in its Red Cap brand by offering premium packaging in a product that was priced slightly below the mainstream. This was a critical threat to the mainstream breweries because while value-priced beer offered a lower value product at a lower price, Red Cap gave customers a reason to expect greater value at a lower price.
 - Vincor invested in developing the global market for "new world" wines, most notably Canadian ice wines. This allowed it to benefit to a greater extent from the maturation of the Canadian wine industry than other players.

Organic Growth

While the success stories did participate in industry consolidation to varying degrees, organic growth figured prominently in all of their financial profiles. Organic growth is important because it reflects a firm's ability to both be in touch with its customers' needs and also to execute a business model that can consistently deliver the solution. A business model characterized exclusively by growth through acquisition implies the absence of a strategy. Coolbrands' consolidation of frozen yogurt shops and E.D. Smith's recent difficulties are illustrative of this fundamental challenge.

Category Leadership

Among the moderately successful companies, category leadership emerges as a key factor. We observed, however, that definitions of the category and the market vary widely. For example, to date, the value beer category has been defined regionally. Accordingly, the scale and brand benefits of leadership are presently accruing to Lakeport for its current position in the Ontario market. However, Sleeman succeeded in taking the premium beer market to a national scale, eroding the benefits that previously may have accrued to regional leaders in this category.

We perceive a similar transition approaching for the natural fruit juice market, where to date, Sun-Rype and Lassonde have split the national market between east and west. However, Lassonde's acquisition in 2004 of Ontario-based Alfresh and Sun-Rype's concurrent organic entry of that market foretell a shift toward a nationally defined category in which the benefits of leadership do not accrue to either firm.

Such changes in the definition of category markets are critical for SMEs, particularly when opportunities emerge for industry giants to enter. Certain categories have traditionally been dominated by SMEs, like E.D. Smith in the Ontario jam market, which was later shared with U.S.-based Smucker when it entered the market in the 1990s. There has been relatively peaceful co-existence between these two mid-sized players. E.D. Smith's recent announcement that it is undertaking a review of its "strategic options" represents a significant risk to Smuckers. In the event that the company was sold to an industry giant like Kraft, the balance of power in the category would shift materially as a result of Kraft's huge portfolio of brands and significantly greater clout with distributors.

Coolbrands' experience provides an interesting counterpoint to the category leadership question. While it has not typically been a category leader in the frozen novelty market, the faddish nature of its brands have an important role to play in improving retailer assortments. Like Jones, it leverages flexible manufacturing to be able to bring creative new products to market quickly. Moreover, many of the companies with whose brands Coolbrands partners value its independence, because they compete with ice cream industry giants Nestle and Unilever in other categories.

Serving Multiple Stakeholders

The business models pursued by the most successful companies are also differentiated by their ability to add value to multiple stakeholders in the value chain. For example:

- Give & Go's strategy of providing thaw and serve products in miniature sizes meets the objectives of retailers to provide a differentiated assortment at a lower cost than in-store bakeries, and health conscious consumers for ultra-fresh products in smaller portions.
- Jones Soda's strategy of creating an engaging authentic brand fulfilled young consumers' desire for a fashionable item through which they could express their individuality, and distributors' need for a higher margin alternative to CSDs.
- Coolbrands' strategic focus on rapid time-to-market and flexible manufacturing, combined with its independence meet the needs of both retailers looking for unique assortments and other food brands looking to create new license revenue streams.

Branding vs. Private Label

In the companies we studied, the decision of focusing on branded products versus building scale in private label was typically informed by the manufacturer's perception of their primary customer. In the case of Give & Go, their focus is on helping retailers with "fakery", giving consumers the benefits of fresh-baked goods in store without the cost. Accordingly, maintaining their Two-Bite Brownie and other brands is awarded secondary importance. In contrast, for Jones and Coolbrands, their primary interest is driving consumer interest in their unique brands and using that to pull retailers to list their products.

A more sustainable axis along which to evaluate this decision is the differentiation within the category. In commodity categories like flour and syrup it seems somewhat naïve to espouse brand religion. However, in highly differentiated categories like ice cream novelties, the high potential margins make a strong argument for defending brand assets against incursions from retailers.

Outstanding Questions

Given the short time horizon over which we analyzed the subject companies, one question that remains unanswered is what SME business models are best equipped to withstand the ongoing trend toward global consolidation. One theory is that firms that originate in the Canadian market are fundamentally impaired in this objective because of this market's small size. Vincor's experience would seem to validate this hypothesis. It leveraged a dominant position in the Canadian market to expand into other new world wine regions, but because other players had advanced a similar strategy further in the much larger U.S. market, it became clear that Vincor would be unable to compete on a global scale.

Conclusions

Summarizing the foregoing analysis leads us to a set of generalizable principles for successful strategic planning for SMEs in the consumer products sector:

Given ever-changing consumer tastes, technologies and competitive threats, no strategic position can ever be permanent. Given that SMEs tend to be more prevalent in smaller or less

mature industries, the time horizons on their strategies are particularly short. Based on the performance trends among the companies in our sample, the average life span of a strategic position is probably only three to four years.

Accordingly, strategic planning efforts that assume the continuation of status quo conditions beyond this time horizon are fundamentally flawed. Importantly, while managers should reasonably be able to envision what their industry structure will look like three years in the future, the real challenge for strategic planning is to identify where the industry will be moving toward in the future, and how the firm needs to be positioned to capture the resulting opportunities.

It is necessary to identify opportunities early. Clearly, this involves taking risks that you will call the trend wrong; however, the consequences of being late to the game are severe: key customers have already established relationships, suppliers' capacity is pledged to competitors and acquisition opportunities have disappeared. This appears to have happened in the case of Peller after Vincor moved aggressively to consolidate the Canadian wine industry.

It also appears that first mover advantage could be more important in highly vertically integrated industries. While Sleeman's move to consolidate the craft brewing sector thwarted opportunities for Brick to grow in the same segment, Vincor's strategy of owning the entire value chain for producing VQA wines gives new meaning to the concept of barriers to entry. With its dominant share of the retail market and near-equivalent share of vineyards, other players' ability to catch up grew increasingly limited.

Moreover, these companies show that demonstrating a commitment to an emerging trend can help ensure its continuance. Value-priced beers had existed with a nominal share of the Ontario market for some time before Lakeport came on the scene and applied some focus to the segment. By designing their post-CCAA business model and capital improvements to target this segment of the market they were able to drive higher growth in this niche than anyone expected. The same thing is true of Jones.

SMEs should actually be advantaged in identifying emerging trends because they are less committed to legacy behaviours than more mature firms. Moreover, because SMEs tend to outsource more and employ staff with more generalist skillsets given their lack of critical mass, they should be better positioned to embrace emerging trends than established firms.

Sustainable business models must reflect integrative thinking - A strategy that rests on a differentiated brand but lacks the manufacturing flexibility to respond to timely changes in product design is one that is destined to failure. Similarly, categories in which products have become commoditized can only be supported by strategies that drive toward scale economies in production and minimized investments in brand support. While large firms are better able to sustain strategic inconsistencies due to subsidies from other parts of their business, the requirement for strategic consistency is paramount for SMEs because it helps them get the greatest leverage of limited resources.

Based on this logic, a hybrid branded and private label strategy would appear to be similarly inconsistent, especially within a single category or channel. After all, the source of a brand's value is its differentiation relative to other products. Differentiation relies on continuous innovation, the cost of which is not supported by private label or co-pack margins. This is particularly true in the U.S. where private label is strongly positioned as a value alternative.

The importance of integrative thinking also applies to ownership structure – This point is illustrated most notably by the poor alignment between the income trust structure and the operational risks and financing requirements of growth firms. The tendency among income trusts to pay out the bulk of their operating cashflow each year to unitholders severely limits their options in the event that operating results vary. This is evidenced by recent events at E.D. Smith in which a variance of roughly 0.5% of sales is forcing the trust's Board to formally re-evaluate its future as an independent public company.

The foregoing analysis would appear to dispute the industrial positioning school of thought on competitive advantage as all of the “successful” firms in our sample grew at rates that significantly exceeded their respective industries. Interestingly, it appears that subtleties made all the difference. Certainly, none of the firms articulated strategies that dispute the conventional wisdom that emphasizes innovation, customer needs, quality or competitiveness. However, it appears that to a certain extent, these elements are table stakes. The most successful companies were those that challenged the industry model by identifying customer segments that were not being well-served by it. This allowed them gain share from industry leaders and ultimately to grow at rate in excess of their respective markets. Moreover, it appears that the actions of innovative SMEs can be a catalyst for changes in the dominant model, as evidenced by players like Sleeman, Brick and Lakeport thriving during a period when industry leaders Labatt and Molson were faltering. In a nutshell, these firms succeeded by developing strategies that leveraged their behavioural strengths, whilst minimizing the challenges associated with their resource limitations.

Appendix 3 – Company Summaries

Sleeman Breweries (acquired by Sapporo in October 2006)

Sources: AIF for FY ended December 31, 2005

Sleeman produces, sells, markets and distributes a variety of specialty-brewed beers for the on-premise and take-home markets across Canada. While its roots date back to 1834, Sleeman's identity as a national premium brewing company began in May 1996 when it began a major consolidation of Canadian brewing industry with the purchase of the Okanagan Brewing and Malting. When it was acquired by Japanese brewer Sapporo in October 2006, the company was the country's third largest brewery, with a 5% share of the 19 million hectoliter Canadian market. Its brewing facilities in Guelph, Ontario have been expanded several times since 1988 and still produce most of the company's product. It has also retained Okanagan's operations in Vernon, British Columbia.

In January 1996, the Company acquired a minority interest in TBS, the primary distributor of beer products in the Province of Ontario. This interest allows the Company to participate directly in future policies and decisions affecting beer distribution practices in Ontario, along with its majority owners, Molson and Labatt.

The acquisition of Okanagan was followed in 1998 with the purchases of a series of other premium brewers: The Upper Canada Brewing Company Limited (Ontario), Shaftebury Brewing Company Ltd. (B.C.), Joseph Warner Brewery (Alberta) as well as small regional breweries in Quebec and the Maritimes to derive a national footprint. These cash acquisitions were financed with debt, and the operations were consolidated with Sleeman's existing breweries in Ontario and B.C.

Seeing the seeds of an insurgence of the value price category, in 1999 Sleeman signed a long-term licensing agreement with Pabst Brewing Company granting it the Canadian rights to the entire Stroh family of value brands¹⁹ (Old Milwaukee, Rainier, Colt 45 and Stroh's). It also acquired the assets of Stroh Brewery Alberta, which carried on the business of importing, marketing, promoting, distributing and selling fermented malt products. Initially, brewing for the Stroh brands continued to be carried out in the United States, but as a result of Pabst's early termination of its production contract in 2001, approximately 85% of the Stroh volumes are now brewed in Sleeman's Guelph facility.

The Stroh's transaction added another \$40m of debt to the company's balance sheet, in addition to the \$35 incurred in relation to its earlier purchases, bringing its debt/CF ratio up to 6.0 times. Moreover, it represents a departure from the company's heritage in the premium beer segment.

Beginning in 2000, Sleeman undertook several strategic transactions which allowed it to enter the fast growing import beer category in Canada. By 2005 it had signed sales and marketing agreements with a large number of the world's most popular brands, including Samuel Adams, Scottish & Newcastle, Beck's, SAB, Strongbow, Grolsch, Sapporo, Guinness, Kilkeny, Harp and Smithwicks and Sol. These moves rested on a strong strategic foundation by deepening the company's participation in the premium category and allowing it to earn commission revenue by leveraging its existing distribution capabilities

¹⁹ In March 2001, Sleeman exercised its option to purchase the Canadian rights to the licensed brands.

Sleeman made its first foray into the United States in early 2001, targeting the New England and the upper Midwest markets with limited success. However, its \$40m acquisition of Unibroue, Quebec's largest microbrewery, in 2004 provided the company with access to a 40-state distribution network in the U.S. that allowed it to win a more substantial share for its Sleeman and Upper Canada brands. However, the presence of competition in both the distribution and retailing segments of the U.S. value chain make it a much less profitable market, and never contributed materially to the company's profitability.

In September 2002, Sleeman signed an agreement with Japan-based Sapporo to provide contract production for Sapporo's products sold in the United States, and the contract was later expanded to include reselling in Canada and worldwide production of Sapporo's distinctive 650 millilitre Silver Can.

While Sleeman's volumes were split roughly 60/40 between premium and value brands, the ability to price its premium products at a premium to those charged by the large domestic brewers was an important component of its marketing strategy. It allowed the Company to recapture the higher costs of ingredients and processing that are involved in producing its various premium brands, as well as allowing the Company to differentiate the packaging of its premium products from that of mass-produced brands. Its premium brands were generally priced 10% to 25% higher than the large domestic brewers mainstream brands. In contrast, its Stroh brands were being generally priced 15% to 25% below the large domestic brewers' mainstream brands. This pricing strategy allowed the Company to grow the Stroh business at the expense of other value brand competitors and at the expense of the mainstream, domestic brands without cannibalizing the premium priced Sleeman brands.

This strategy worked well during the late 1990s when the premium beer category was experiencing strong growth. Then, in the early 2000s Lakeport, Brick and Big Rock began to leverage significant microbrewery subsidies to price their value brands at the legal minimum. These moves spurred rapid growth of the value category at the expense of the mid-market. The mid-market retaliated with more aggressive promotional activity that ultimately widened the price spread between mid-market and premium products and hurt Sleeman's premium brands. Competition also intensified in the premium segment as Molson and Labatt increased their focus on that category, heightened by Molson's purchase of Creemore in 2005. Moreover, because Sleeman's premium heritage brought with it a cost structure that was uncompetitive in the value category, it was unable to match this move, and it also lost share in the value category. These difficulties were no doubt exacerbated by the loss of its President & COO in 2002 and his subsequent move to become the CEO of Brick Brewing in 2004.

Looking critically, Sleeman really didn't do anything innovative to support the maintenance and growth of its premium franchise. Its products were marketed through the same variety of mediums, including media advertising (in the form of print, television, outdoor and radio media directed at the take home consumer market which emphasizes the Sleeman brand name and its high quality attributes), sponsorship of local events (including sporting, community and charitable events) through a special events group organized for this purpose and point of sales displays (such as tap handles, coasters, banners, posters and consumer items such as T-shirts), all of which are designed to enhance the Company's reputation and visibility.

Despite investing in additional marketing and promotional activities in an effort to defend its business against this heightened competitive intensity Sleeman continued to lose market share in 2005. Moreover, the expense of supporting its wide array of acquired brands across a growing number of formats became increasingly uneconomic in the face of this share erosion. With

growing working capital costs and a debt/CF ratio that reached 7.9 times at the end of 2004, Sleeman ultimately put itself up for sale in May 2006.

Brick Brewing

Sources: AIF and Proxy Circular for FY ended January 31, 2006

Founded in 1984, Brick Brewing produces, markets, sells and distributes a portfolio of premium (Brick and Waterloo), mid-market (Red Cap, Formosa and Red Baron) and value (Laker) beer brands in the Ontario market. The Company also exports selected brands to Alberta and New York through reciprocal agreements with Big Rock and High Falls Brewing, respectively. In addition, the Company is the only major brewer involved in the private label segment, producing, selling, marketing and distributing various beer products under the licensed PC trademark on behalf of Loblaws Inc. which are available in Ontario and Quebec.

In 2002 the Company relaunched Red Cap in the classic “stubby” bottle. This historic brand in the retro “stubby” bottle was very well received by the market and sales grew substantially. The success of this initiative helped the Company grow its current business in Ontario and confirmed that it could increase sales if it used a variety of packaging for its products and not exclusively the industry standard bottle. The renewed interest in Red Cap led to the introduction of the brand in Alberta and British Columbia. Importantly, the use of a non-standard bottle is a unique product feature in the mid-market segment, as the incremental costs associated with distributing such a product is typically reserved for premium brands. In fact, while Red Cap is currently classified as a mainstream brand, it was in the premium category when it was originally launched.

In 2003, the Company embarked on a strategy to aggressively compete in the rapidly-growing value priced beer category in Ontario with its Laker family of brands, acquired from Molson in 1997. The Company lowered the price of selected Laker brands to the “Social Reference Price”, the minimum price allowed by the Government of Ontario. As a result, Laker volumes increased dramatically and this trend has continued through fiscal 2006, despite intense competition at this price level from other brewers.

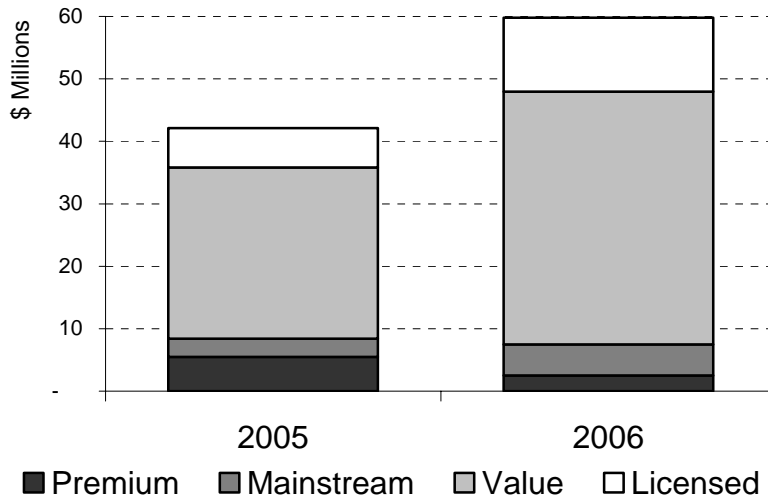
In mid-2004, the Company increased its focus on the value segment by entering into a multi-year agreement with Loblaws, whereby it was granted a license to use the PC trademark to produce, distribute and sell PC beer in Ontario and Quebec. This contract was important because it provided the Company with a sales base to develop its distribution for the first time in the province of Quebec.

In fiscal 2005 the Company successfully increased its sales volumes of beer by approximately 225% over fiscal 2004. The significant increase in volume of the Laker brands, combined with the launch of the PC brands and aggressive promotion of Red Cap, accounted for this increased sales volume. This brought a number of important benefits to the Company, including: greatly enhanced and more efficient product distribution in Ontario, due to increasing volumes to more retail outlets; improved purchasing power for raw materials; and, improved economies of scale providing production efficiencies. Operating income grew strongly as a result.

Brick has gained share by tightening industry pricing, placing its mainstream brands 5% to 15% below the large domestic brewers’ mainstream brands and at various times are aggressively price promoted to 25% below mainstream brand prices. Its Laker brands are currently being sold at prices approximately 25% to 30% below mainstream brands and approximately 10% below other value brands. This pricing strategy has allowed the Company to grow Laker brand sales at the expense of other value brand competitors and at the expense of competitors’ mainstream and domestic brands. While this strategy was intended to prevent cannibalization of Brick’s premium brands by increasing the price spread in relation to its mainstream brands, it has not succeeded; as

the table below indicates, sales of Brick's premium-priced brands continued to decline in the year ended January 2006.

Brick Brewing – Revenue by Product Segment



Brick has financed its recent growth through private placements of common shares in April and November of 2004. The former investment was supported by brewing industry executive Doug Berchtold who as a result became President & CEO of Brick, while founder James Brickman's role was scaled back to Executive Chair. Prior to joining Brick, Berchtold had President & Chief Operating Officer of Sleeman.

Lakeport Brewing

Sources: AIF for FY ended December 31, 2005

Lakeport is an Ontario-based, diversified brewer focused on producing quality beer for the value segment of the take-home market. Its primary product offerings are its nine proprietary beers. Lakeport brands compete primarily in the value segment as lower priced alternatives to the heavily marketed mainstream beer brands of other market participants. A small portion of Lakeport's profitability is derived from the production of private label brands and from co-packing contracts for blending and packaging alternative alcoholic and non-alcoholic beverages.

The company was founded in 1992 with the acquisition of a Hamilton brewery formerly owned by Amstel. In 1998, primarily as a result of underutilized capacity and undercapitalization, Lakeport sought protection under the *Companies' Creditors Arrangement Act*, from which it emerged in 1999 under new ownership. At that time a new management team was introduced, bringing with it a new focus on proprietary brands and the growing value segment of the market.

In fiscal 2001, Lakeport began extensive capital expenditure programs designed to upgrade its brewing, blending and packaging facilities in order to improve efficiencies and increase output. Between fiscal 2001 and fiscal 2005, the company invested approximately \$18 million upgrading its facilities. In addition, it began the process of recruiting key personnel in the areas of operations, finance, logistics, marketing and procurement. The IPO of an income trust was completed in June 2005.

While most brewers have brands positioned in the value segment, there are no competitors in the Ontario beer market that focus specifically on the value segment as a core strategy. This differentiator places Lakeport in an advantaged position because its competitors all risk cannibalizing sales of their higher margin mainstream and premium brands. Lakeport's uniqueness in the value category is evidenced by the fact that it competes against mostly imported brands (eg. Busch imported by Labatt and Milwaukee's Best brands imported by Molson Coors), and therefore, should enjoy a cost advantage. More recently, Brick's Laker and licensed PC brands have provided increased competition in the value segment, but largely as a follow-on to Lakeport's establishment of the category.

Between fiscal 2001 and fiscal 2005, Lakeport intensified its focus on its portfolio of value-priced proprietary beer products, rapidly increasing its share of the Ontario market from approximately 1.2% to approximately 5.4%. For the twelve months ended December 31, 2005, the Company's market share was approximately 10%. Lakeport Honey Lager, introduced in 2002, is presently one of the top 10 selling brands by volume in TBS locations, and Lakeport Pilsener is among the top 20 selling brands. As of December 31, 2005, Lakeport was the third largest brewer in Ontario based on over-the-counter sales of domestic beer at TBS.

Vincor International

Source: AIF for FY ended March 31, 2005.

With revenue of over \$650 million, Vincor was the eighth largest player in the \$190 billion global wine market before it was acquired by Constellation Brands in June 2006²⁰. Against the backdrop of a market that was generating real annual growth of 2-5%, Vincor emerged with an objective to participate in the global consolidation of the wine industry and become a top-five player.

Its strategy had two key elements: First, to leverage sales, marketing and distribution capabilities in key “new world” wine growing areas around the world to develop existing brands and expand their global reach. Second, to expand their portfolio of brands by acquiring wineries in key “new world” wine producing regions, and increase their value by applying their marketing machine. During its ten year history, the company acquired several well-known wine-makers and marketers around the world, establishing operations in several Canadian provinces as well as California, Australia and New Zealand and the UK. With the exception of its final purchase in the UK, this acquisition program was focused in regional clusters that allowed the company to build critical mass for a dedicated inside sales force and consolidated administrative functions.

Vincor also cited the expansion of the supply of premium grapes, particularly in Canada and capitalize on the reputation of Inniskillin to develop icewine into an international luxury product as strategic goals; however, these appeared to be somewhat tangential to the core brand management thrust. Moreover, while the strategy cites a focus on the premium segments of wine market, the brand portfolio also included a range of non-premium brands, which perhaps could have diluted its commitment to developing the premium segment.

Between 1996 and 2000, the company aggressively consolidated the Canadian wine industry developing leading positions in all major producing regions. These acquisitions proved the business model and resulted in significant synergies achieved in areas such as winery overheads, sales force consolidations, administrative efficiencies and other overhead reductions. In addition, the combined business has benefited from complementary product lines, which has resulted in leading brands in virtually all segments of the wine market in Canada. They supplemented this strong brand portfolio with a proprietary secondary distribution channel, a strategic advantage that reduced its dependence on provincially-owned liquor boards.

As a dominant player in the Canadian market with a 21% share by volume, Vincor rode the rising ride of Canadian winemakers on the global stage during the 1990s. It harnessed this momentum through a series of joint ventures with leading wineries around the world, and then parlayed this into a global consolidation strategy.

In 2000 it entered the U.S. market, with the acquisition of a vineyard and full service winery in the California, and followed with a second in Washington state market in 2001. Like the Canadian businesses, these two operations were consolidated to derive operating synergies. Finance, administration, management information systems, sales and marketing were all consolidated and integrated. In addition, wholesalers wherever possible were rationalized to combine the volumes of R.H. Phillips and Hogue in order to improve the business’ importance with its customers. Finally, brokers in key states were replaced by dedicated sales executives to improve our ability to service the various markets and also to reduce costs. 2002 through 2004 saw the model extended to include Australia and New Zealand.

²⁰ Bid was originally made in September, 2005, at a 55% premium to the then closing price.

Vincor's sales model was a key element of its strategy. Its sales and marketing team quickly gained critical mass by supporting the company's growing portfolio. Moreover, they leveraged their leading brands to achieve increased distribution and thus, market share, for acquired brands. It employed a similar sales model in the United States, Australia, and New Zealand, which sold its products to wine retailers, either directly or through wholesale distributors.

Throughout this period, Vincor's gross margins and operating profit and EPS grew consistently, and the stock's performance followed suit.

2004 marked a departure from the model, with the \$320 million acquisition of Western Wines in the UK. The purchase provided Vincor approximately an 8% in the UK as well as distribution reach Northern Europe. It also brought a portfolio of approximately 400 brands, including owned brands, agency brands and private label products; however, it was not backed by winery assets.

In the United Kingdom, we have a sales and marketing organization of 26. Its focus is to develop category management leadership in the off premise wine industry in the United Kingdom. The sales force operates through the head office organizations of its customers in the UK. The off-premise marketplace, where we compete, consists of a relatively small number of retail grocery chains. It is important, therefore, to offer these chains a full range of products, both in terms of brands and price points, in order to provide a full range of service to these customers.

Vincor participated in various segments of the value chain, producing and marketing wines in key "new world" wine regions. They were substantially vertically integrated, owning vineyards that produce roughly half of their grape requirements, with the balance fulfilled through a combination of long-term and annual supply arrangements. This business model appears to be aligned with their stated strategy to compete on the basis of providing value through a balance of quality, service, price, brand recognition, communication of product attributes, and distribution.

It is worth noting that Vincor's major acquisitions included long-term employment agreements with the former owners of these businesses, allowing it to maintain a significant level of management ownership as it has grown. To codify this, it introduced executive share ownership Guidelines for each tier of management, and expected these guidelines to be satisfied within five years.

Andrew Peller (formerly Andrés Wines)

Source: AIFs for FY ended March 31, 2006, 2005 and 2001.

Andrés Wines was incorporated in 1965, and as consumer tastes and demographics have changed, the company has grown from its historical position as Canada's leading supplier of value-priced table and sparkling wines (Hochtaler and Baby Duck) to become one of the leading suppliers of premium varietal wines. This transition began in the early 1990s when it established Peller Estates as a premium label and was augmented in 1994 when it acquired Hillebrand, then the largest producer of VQA and premium wines in Canada. The company's name was changed to Andrew Peller Limited in 2006, and today is the nation's second largest wine producer and marketer with a 12% share. Its premium brands include *Peller Estates*, *Hillebrand* and *Trius* and these are complemented by such popular priced wines as *Hochtaler* and *Domaine D'Or*, the two top-selling wine brands in Canada. The company's products are sold primarily through government liquor distribution systems and its 102 *Vineyards Estate Wines* retail stores in Ontario.

The company is committed to a strategy of growth that focuses on expanding its core business as a producer and marketer of quality wines and craft beer through the development of strong brands that continually meet the needs of its customers. This strategy is supported by sophisticated sales, marketing and promotional programs. It continues to seek out acquisition opportunities that support its strategic direction and meet its growth and investment return criteria.

In 1996, the Company acquired its initial position in what was then a rapidly-growing home winemaking market with the purchase of Niagara Vine Products, and rebranded it as Vineco International Products. A year later, it complemented this investment with the purchase of Brew King Limited, the largest manufacturer and distributor of wine kits and related accessories for home winemakers in Canada. It further extended this leadership position in 2003 with the purchase of Distrivin Ltée and Winexpert Inc, the exclusive distributors of Brew King products in eastern Canada, following which the company's stores were rebranded as Winexpert. This was followed in 2005 with the acquisition of Wine Not, a network of independently-owned franchise retailers operating wine-on-premise locations in Ontario. The acquisition was undertaken to increase the brand presence, distribution and market share of Winexpert in Ontario.

Later in 2005, the Company doubled its sales in the western Canadian market by acquiring British Columbia-based Cascadia Brands. Cascadia was one of Canada's largest producers of premium wine, craft beer, and spirits with a portfolio of brands that are well recognized throughout Western Canada; the spirits division was divested shortly thereafter.

Despite solid financial progress and excellent share price performance, Peller's dual focus on the premium wine and wine-on-premise markets does not appear to be a credible one. Further, there is no indication in the company's filings regarding the relative size or profitability of the wine kit and beer businesses. Regardless, it is difficult to see the synergy between this retail-focused value item and the company's stated focus on building premium wine brands.

Magnotta Winery Corporation

Source: AIF for FY ended January 31, 2006.

Magnotta Winery is an Ontario-based vineyard, wine-making and retail business. It commenced producing and selling wine late in 1990 and did an IPO in 1995 to finance the construction of a new flag-ship head-office, manufacturing and retail facility that was opened in May 1997. The Company entered the brewing and distilling businesses in 1996 and 1997, respectively, and currently generates 6% of its sales from these non-core lines.

In 2003, Magnotta changed its marketing focus to emphasize a “lifestyle” branding theme across all of its marketing and advertising efforts. Fiscal 2004 was a year of solidifying this branding position in the marketplace. The initiative has resulted in increased sales of the company’s higher end products. In fiscal 2006 and 2005, the Company allocated resources to penetrate many quality licensees/restaurants with its products. This investment has successfully resulted in Magnotta now being featured in many of Toronto’s premiere restaurants. This exposure is providing strong branding opportunities for the Company’s products.

Magnotta’s distribution strategy is unique in the Ontario marketplace. While roughly 90% of the wine sold in Ontario is distributed through the government-owned LCBO, Magnotta does not leverage this distribution channel due to a protracted litigation between itself and the LCBO that was settled during fiscal 2002. While the LCBO now offers some of Magnotta’s finest wines in its retail stores, Magnotta sells most of its products through proprietary retail outlets in its wineries (located in Vaughan, Mississauga, Scarborough, Brampton, North York, Beamsville, and Cambridge), and a direct-to-consumer product ordering e-commerce site launched in 2003. This internet site allows customers the convenience of ordering Magnotta products throughout the province of Ontario, for home delivery by Canada Post. Moreover, it neutralizes the distribution inefficiencies associated with being a small market participant. The Company is always looking for new markets for its product distribution. As a result, Magnotta has spent several years promoting its various products in other Canadian provinces and also outside of Canada.

The Company currently produces over 180 varieties of wine, including specialty wines such as icewine, aperitif wine and sparkling wines. Some of the varieties of wines are made from 100% Ontario grapes. The balance of the Company’s wines are the result of blending Ontario juices and wines (which the Company either grows from its vineyards, or purchases from Ontario growers) with wines and juices which the Company purchases from countries such as Argentina, Chile, Italy and the United States, to name a few. Regulations require that a specific percentage (based on crop yield) of juice used to produce wine in Ontario be grown locally.

Jones Soda²¹

Sources: SEC Form 10-KSB, for the years ended December 31, 2000, 2001 and September 11, 2006 presentation at ThinkEquity Partners Growth Conference (webcast).

Jones Soda manufactures premium products for the New Age beverage segment. Its strategy is to increase sales by expanding distribution of its internally developed brands in new and existing markets, stimulating consumer trial of its products and increasing consumer awareness of, and brand loyalty to, its unique brands and products. Key elements of this strategy include:

- creating strong distributor relationships and key accounts;
- stimulating strong consumer demand for its existing brands and products with primary emphasis in the United States and Canada;
- developing unique alternative beverage brands and products; and
- licensing its brand equity for the creation of other beverage or non-beverage products.

The Jones model relies on the virtuous cycle of innovation, pricing power, and value sharing with key stakeholders in the value chain. Simply put, Jones' strategy has been to offer high margins to distributors, leveraging the founder's previous experience as a regional beverage distributor. This was a welcome move in the CSD industry after years of the major manufacturers exploiting the fact that retailers are unable to compete without Coke and Pepsi products on the shelf by squeezing downstream operating margins to zero. Jones funds this value sharing by creating a premium product and a brand that captures the consumers' imagination and as a result, commands significant price premium over traditional carbonated beverages. This strategy upset the conventional balance of power in the CSD industry, and couldn't be matched by the dominant players because in the absence of innovation, their products would not support premium pricing.

The premise underlying Jones' business strategy is stated in their December 31, 2001 form 10-KSB:

“due to the limited life cycle of products in this category, it of the beverage industry, we believe that the ongoing process of creating new brands, products and product extensions will be an important factor in our long-term success... We believe that products in the New Age beverage category, much like certain fashion trends, tend to have a limited life cycle of approximately five to nine years. As part of our business strategy, we intend to launch new brands, products and/or product extensions at approximately eighteen to thirty month intervals.”

The need to maintain agility implied by this acknowledgement of the need to constantly innovate drives key elements of the company's business model, namely the use of:

- contract packers to prepare, bottle and package Jones Soda's internally developed products
- independent trucking companies to have product shipped from various contract packers to independent warehouses
- a network of independent distributors which sell and deliver products either to sub-distributors or directly to retail outlets
- creative but relatively low cost marketing and brand promotion techniques, including:
 - o developing unique brand names, slogans and trade dress

²¹ Jones Soda was listed on the TSX in 1999, the year in which we did our initial screen for companies to include in the sample. It has subsequently shifted to the NASDAQ and is only a reporting issuer in the U.S., but its story was too interesting not to include.

- provide each of our distributors with point-of-sale promotional materials and branded apparel items
- promoting interaction with customers through the use of such point-of-sale items as posters, stickers, table cards, shelf danglers, post cards, hats, pins, T-shirts, and our proprietary lighted display box
- through the labels on its bottles, invite consumers to access its website and to send in photographs to be featured on the *Jones Soda Co.* labels.

ED Smith Income Fund

Sources: Interviews with David Smith, CFO and executive at competitor, E.D. Smith 2006 AIF, IPO prospectus

Founded in 1882, E.D. Smith is a leading manufacturer of a diverse portfolio of private label and branded food products. Since the mid-1980s, the Company began to expand beyond its longstanding heritage in the fruit spread category (jams and pie fillings) and today its products include 1,450 SKUs spanning ten categories including ketchup, sauces (pasta sauces, salsa, barbecue, specialty sauces) salad dressings and syrups. The Company markets and distributes its products to the retail and foodservice markets in Canada and the U.S.

Branded products are marketed under the E.D. Smith name, but the Company's focus is increasingly on manufacturing and product development and less on marketing and branding. Accordingly, the bulk of E.D. Smith's sales are presently derived from the manufacture of private label products for Canadian and U.S. grocery retailers; it is the leading supplier of private label ketchup, jams, pie fillings, barbecue sauces, table syrups and pasta sauces in Canada.

The Company's research and development team develops and tests new product formulations and, in many cases, functions as the product development team for customers. It has been instrumental in creating such products as "Triple Fruit" jam products and "No Sugar Added" jams and syrups, private label products including Fresh Pack at Trader Joe's and branded products including Saucemaker branded sauces sold to foodservice distributors and operators. In addition, the Company plans to introduce new innovative branded products in categories in which it produces private label offerings, particularly where these products are complementary to the customer's private label offerings and seen as maximizing total category sales and profitability for the customer.

The company acquired its first material U.S. presence²² in 2005 through the acquisition of North Coast, a U.S. based manufacturer of pourable salad dressings, marinades, barbecue sauces and syrups, that was put up for sale after losing a co-packing customer who decided to self-manufacture. In addition to its private label offerings, North Coast brought branded products under the Garden Goodness brand, a value-oriented pourable salad dressing label, and the Den brand, a U.S. regional brand of pourable salad dressings, marinades and barbecue sauces. A year later, in August 2006, E.D. Smith acquired Seaforth Creamery, a key competitor to North Coast, for \$95 million. Seaforth was a leading manufacturer of pourable salad dressings, spoonable salad dressings and marinades in North America, with an exclusive focus on the private label market.

The business grew by 3.4% organically between 2001-2005, pursuing an objective of being #1 or #2 in each of the categories in which it participates. During this time, the company also invested in upgrading its facilities to support the flexibility to handle shorter production runs, allowing the Company to respond to diverse customer requirements while maintaining superior quality levels. Flexibility is imperative because product, package design and size of orders are variable in private label food products, and customers are increasingly seeking manufacturers that can produce a variety of food products, both on a large and small scale. The Company continues to enhance its operational efficiencies and focus on being a low cost producer as evidenced by the implementation of a cost reduction program at the Winona Facility in January 2003 called Project PEACH (Promoting Efficiency and Changing Habits), which is now entering its third year.

²² Prior to that acquisition, only 12% of the company's sales were generated in the U.S.

More recently, the company has augmented this strategy and significantly increased its size through several acquisitions. Its rationale has been that it needs to get bigger to survive as distributor customers continue to consolidate their supplier base among fewer, selected firms with the quality, quantity and variety of products that best meet consumer demand at the lowest cost.

Accordingly, it claims to be pursuing the following growth paths:

1. increase the share of wallet consumers spend on their category by introducing innovative new products
2. add new categories (eg. adding salad dressings, largely via acquisition)
3. increase leading share in existing categories by creating innovative new product extensions to win share from competitors
4. add new geographies/cross-sell products from acquired portfolios

Advance private label penetration of selected categories (eg. pourable salad dressings) because these have higher margins for distributors.

The portfolio of categories that has emerged to date appears to be somewhat reactive. For example, management states that the purchase of a syrup plant got them into dressings; then, subsequent acquisitions in the salad dressings category got them into the mayonnaise business. There is little apparent synergy amongst the current roster of ten categories; some are mature or declining (eg. jam, ketchup), while others offer opportunities for growth (eg. dressings, sauces). Moreover, given their stated strategy of expanding the penetration of private label dressings in the U.S, their acquired presence in value-branded dressings appears strategically inconsistent.

In December 2006 the company announced that it no longer expected to achieve its target payout ratio for the current year due to an increase in the market price of soybean oil, a key input for its private label dressings business, now a significant portion of the company's sales. Branded competitors have more flexibility to reconstitute their products or raise prices to offset the impact of such events; however, private label suppliers are typically followers.

The reduced payout ratio amounts to an adverse movement of roughly \$1m. This impact, which represents less than 0.5% of the company's sales, has been a catalyst for the resignation of the company's CEO and precipitated a formal review of its strategic options.

Coolbrands

Sources: Interview with Michael Serruya, AIF for FY ended August 31, 2005.

Coolbrands was founded in 1987 under the name Yogen Fruz by Michael and Aaron Serruya with a focus on building a chain of frozen yogurt franchises. The concept met with quick success and hundreds of locations were opened over the following several years. During the 1990s the concept was expanded as the company acquired a range of related store concepts, and by 1998 it had franchise operations amounting to nearly 5,000 stores in 82 countries under seven banners. Investors who purchased shares in mid-1995 were rewarded with a six-fold increase on their investment by mid-1998.

However, these gains were completely wiped out by the end of 1999 as competition in the frozen dessert retail market intensified, and the Company's banners found themselves increasingly competing not only with other frozen yogurt and ice cream chains but, in certain instances, also with each other. The acquisitions of ICBIY and Golden Swirl concepts acquired in 1996-97 proved inconsistent with market trends, and the company was forced to record a \$25m write-down on these assets in fiscal 2001.

The seeds of Coolbrands' current business model were sown in 1998 when it entered the market for pre-packaged novelties with the acquisition of Integrated Brands, which marketed, sold and distributed frozen desserts under the Tropicana®, Betty Crocker®, Yoplait® and other brand names pursuant to long-term exclusive license agreements. Integrated Brands sold its variety of pre-packaged frozen dessert products to distributors and various retail establishments including supermarkets, grocery stores, club stores, gourmet shops, delicatessens and convenience stores.

Integrated Brands' model was to purchase packaging and ingredients for its products directly from unaffiliated suppliers and then sell the packaging and ingredients to contract manufacturers. The manufacturers produced Integrated Brands' products under its quality control supervision, and then Integrated Brands purchased the finished products from the manufacturers at cost plus an agreed upon processing fee which includes a profit for the manufacturers. This strategy of managing the brand assets and outsourcing the commodity manufacturing was supported by a plentiful supply of contract manufacturers for ice cream novelties.

Yogen Fruz's brand management strategy was extended in October 2000 with the acquisition of Eskimo Pie Corporation in order to benefit from Eskimo Pie's strong brand names (which included Eskimo Pie, Welch's and Weight Watchers) and U.S. based manufacturing facilities. It paid US\$30m for the company's 1999 sales of US\$55m, and financed the purchase by incurring its first significant borrowings. Concurrent with this shift in the company's focus from retail franchising to brand licensing and development, the company's name was changed to Coolbrands.

Eskimo Pie extended the strengths of Integrated Brands, which included national brand recognition, quality products and the management of complex sales and distribution networks. Eskimo Pie's growth came primarily as a result of the development and introduction of Eskimo Pie brand frozen dessert products and the development and marketing of frozen dessert products under the licensing of other well-known national brands under sublicensing arrangements (eg. Weight Watchers). These rights allow Eskimo Pie to manage the product development, manufacture, distribution, marketing and sales of branded frozen novelties and ice cream products in exchange for royalty payments to the owners of the brand names. They used licensee manufacturers who provide a cost effective means to manufacture and distribute Eskimo Pie's products.

The Company provided marketing support for licensed brands manufactured and distributed by its licensees, but licensees were contractually required to contribute to trade promotion spending and to make quarterly royalty payments. The Company engaged in product/concept development, and advertising and sales promotion expense including trade promotion and introductory costs, price-off and feature price promotions, regional consumer promotion, couponing and other trial purchase generating programs and broker commissions.

Although the specific terms varied, Master License Agreements typically ranged in length from five to twenty years, and provided royalty payments to the licensor.

The licensing model provided the company with some significant successes over the next few years as it developed its existing brands and broadened its portfolio of licensing rights to include popular names like Godiva, Tropicana and Yoplait. The Weight Watchers brand grew into a \$100m franchise, and an Atkins low carb product developed by Coolbrands achieved a run rate of \$60m within less than a year. These products generated high gross profit margins and lower than normal promotion, marketing and advertising expenses due to the initial low level of competition in this niche category.

In an effort to leverage its growing scale and ensure manufacturing capacity in the face of reduced availability of co-packing suppliers, Coolbrands acquired 50.1% of Americana Foods in fiscal 2003. This gave it control of a large, flexible production facility in Texas. The business supplied a variety of soft serve mixes, packaged frozen novelties for Coolbrands as well as to national retailers, food companies and restaurant chains. The Company consolidated a significant proportion of its manufacturing at this strategic facility.

At this point the company's strategic focus went off the rails, and it embarked on a process of diversifying outside their core frozen novelties market and across the value chain, including:

- the acquisition of substantially the entire Haagen-Dazs Ice Cream distribution system in the United States from Nestlé, including distribution assets spanning ten states.
- The \$59m acquisition of a Breyer's brand fresh cup yogurt plant located in North Lawrence, New York from Kraft.

However, the popularity of Atkins faded as quickly as it had emerged, and the company lost the Weight Watchers license at the end of fiscal 2004 after failing to agree on renewal terms with the licensor.

These disappointments sparked a chain of adverse events which decimated Coolbrands' gross profit in fiscal 2005:

- The change in mix of frozen dessert products being sold in 2005 away from blockbuster super-premium products to more mainstream ones which, in addition to carrying lower margins, required larger slotting allowances and promotional support.
- The write down of obsolete and slow moving finished goods inventories, packaging, and ingredients resulting from a settlement of litigation with Weight Watchers International, a new labeling law which will become effective January 1, 2006, and a provision for slow moving Atkins inventories; and,
- The inability to cover fixed overhead costs in both our manufacturing and distribution operations due to the lack of production and sales.

Selling, general and administrative expenses for fiscal 2005 increased as a percentage of revenues to 13.6% as compared with 11.5% for fiscal 2004. This increase occurred primarily due to the decline revenues.

These events resulted in the company breaching its debt covenants, and ultimately facing a liquidity crunch in which its loans were called and founder Michael Serruya had to step in to personally guarantee the debt.

More recently, it has divested non-core activities, including the yogurt, DSD and franchise business and refocused on its core brand development and manufacturing capabilities. Part of this refocusing will include a consolidation of the company's management in a single location. Mr. Serruya attributes at least a part of the company's strategic challenges to the difficulty of ensuring managerial consistency and efficiency across a geographically dispersed team.

Despite this refocusing, it must still be acknowledged that Coolbrands' market remains intensely competitive, with its brands competing against those of Unilever (Klondike, Popsicle, Breyer's, Good Humor and Sealtest), Nestle (Haagen-Dazs, Skinny Cow, and Starbuck's) and Dreyer's. It faces further competition for discretionary food dollars from the pint market and from other frozen desserts.

Despite this intense competition, Serruya believes there remains an important role for an independent in this category, as Nestle and Unilever compete with some of its licensees in other categories (eg. General Mills). Retailers also value Coolbrands' ability to offer improved product assortments. Accordingly, Coolbrands cites speed to market as a key differentiator, underpinned by both a product development capability and its Americana manufacturing facility. This ability was evidenced by its ability to have the Atkins low carb product on store shelves a mere six weeks after the agreement was signed. This is an important differentiator in markets where consumer fads tend to dissipate even more quickly than they develop.

The loss of the anchor Weight Watchers license taught Serruya the strategic value of owning the development and manufacture of his own brands. Accordingly, Coolbrands follows the Nestle and Unilever models and does not do any co-packing for other brands. This also serves as a barrier to entry for potential competitors because in the absence of co-packing suppliers, they would be forced to invest in constructing a plant in order to launch a product. He is also committed to avoiding private label arrangements with his major retail customers. Moreover, given the significant expense involved in obtaining shelf space for new products, he has learned the benefits of a portfolio approach; specifically, leveraging the blockbuster Weight Watchers and Atkins products when they were hot to pull through and develop less popular brands.

Interestingly, the company's poor financial performance in fiscal 2005 appears to have been a catalyst for some long overdue improvements in its corporate governance practices:

- A resolution was passed to collapse the dual share structure effective May 2007 based on a 1-for-1 exchange
- four new independent directors were nominated to the board, giving it a majority of independent directors.

Give & Go Prepared Foods (private)

Sources: Interviews with Joel Flatt, President (October 25, 2006) and Humberto Aquino, Director, Kensington Capital (November 9, 2006).

Give & Go Prepared Foods is a Toronto-based manufacturer of branded and private label thaw and serve baked goods. It produces the well known Two-Bite Brownie, as well as a range of other miniature treats. The key to its success has been operating in a growing category that offers high margins for distributors, maintaining a unique and continually refreshed specialty product line, and a patented manufacturing process.

Give & Go was founded in 1990 by two entrepreneurs seeking to create a niche product for the finished baked goods market. They leveraged a patented manufacturing technology to develop a range of unique products for producing miniature baked goods which addressed consumers' growing preference for smaller serving sizes. They initially focused on producing branded products for the foodservice and convenience channels.

The trend toward in-store bakeries in supermarkets during the 1980s brought a much larger opportunity. By the 1990s, retailers were struggling with the spiraling cost of in-store bakeries, but competitive pressures demanded that they continue to offer an assortment of fresh goods. Give & Go was able to address this problem by shipping thaw and serve products that allowed retailers to offer consumers the freshness they had come to expect without the expense of an in-store bakery. This took them in the direction of no label and private label products because the retailer wanted a "fresh baked" store brand in order to maintain the feel of the in-store bakery. As a result, store-branded products carry higher margins in the bakery because unlike other parts of the store, private label products are not used as a value alternative to national brands.

The tremendous popularity of the Two-Bite Brownie when it was launched in 1997 was a turning point for the company, offering a platform on which to add other products and expand its listing base. By the late 1990s the company was supplying Loblaws across Canada and had grown into a \$50 million business.

By the early 2000s the founders had taken the business to the limit of their abilities and were ready to move on. Mr. Flatt, a marketing executive at Oshawa Foods was seeking to buy a bakery business in order to exploit the trend toward reducing the cost of in-store bakeries. He acquired the business in 2003 with the support of private equity investors.

The business has more than tripled in size since that time, but its growth has been supported by a range of investments that were direly needed when the business changed hands in 2003. The new owners acquired an adjacent piece of land, built a new plant, and made significant investments in information technology infrastructure. It also significantly enhanced its management team adding new operational, marketing and financial bench strength.

Again the firm identified a new need in the marketplace in the form of immature private label penetration in the U.S. relative to Canada. They invested in developing a sales force targeting key accounts south of the border, and now sell to WalMart and every other major retailer in North America.

Flatt's experience with Oshawa group made him keenly aware of the challenges faced by retailers, and he believes that Give & Go's ability to ease their customers' pain has been a key factor in its success. They entered a growing niche early, and as a result, quickly achieved a scale at which larger firms are unable to add any incremental value.

A key learning has been that operating a \$50 million business is very different than a \$150 million one, and that the transition from one to the other cannot be achieved without risk. Rapid growth has at times been destabilizing as the organization has struggled to develop, produce and deliver ever-greater volumes of high quality products in a timely fashion. As a result, he believes that success rests on managing growth in a balanced fashion; deferring capacity investments can preserve capital, but risks delivery failures. Similarly, building a sales force to attack a Greenfield market introduces financial risks, but also raises the challenge of meeting potentially significant increases in demand.

He believes that the business will encounter new challenges as it approaches its next step-change in capacity. For example, until now, Give & Go's ability to create a tight locus of activity on a single corporate campus has facilitated management's ability to maintain the control and oversight needed to ensure success. Its next major capacity expansion will likely need to be at a physical distance from its headquarters, introducing new risks and challenges.

These risks are heightened by the need to expand beyond the comfort zone of extensions on proven products. Give & Go's customers expect it to continually offer innovative new products. Importantly, as an established supplier they have the benefit of a collaborative product development process and a lead order to underwrite the capacity expansions needed to deliver it. Moreover, Flatt believes that by focusing on their category specialties and staying close to consumer trends Give & Go can deliver a better record of successful innovation. These behemoths invest tens of millions in innovation, and take upwards of one year to develop and launch new products whilst the vast majority of the resulting offerings fail. Flatt argues that this model is unsustainable, a fact that positions SMEs like Give & Go for market share gains in the future.

Give & Go's ownership structure has also played a key role in its development. In their pursuit for high returns, its investors were prepared to take the risk of investing in the growth and development of the business, and offered active but patient management. As a result, Flatt also attributes a significant amount of Give & Go's success to the sage advice of his Board, who brought a wealth of experience from similar businesses. However, as merchant bankers, their investment time horizon is finite, and at some point the desire for a liquidity event will invariably figure into the next stage of the firm's strategy.

For his own part, Humberto Aquino, a Director at Kensington Capital, he believes that firms controlled by private equity investors are uniquely positioned for success because management incentives are closely aligned with those of shareholders. He argues that public companies are doomed to failure simply because they offer too great of an opportunity for senior managers to get rich without delivering acceptable returns for shareholders. An interesting follow-up study would be to compare the performance of firms in which managers have a significant equity stake to those without, in order to determine what linkages exist between ownership-incentivized management and superior strategic positioning and financial performance.

Lassonde Industries

Sources: 2006 Annual Report and AIF

Lassonde develops, manufactures and markets fruit and vegetable products, sauces, and specialty products such as olive oil and wine. The company currently employs 900 people and maintains three subsidiaries: A.Lassonde Inc, Lassonde Specialties, and Arista Wines Ltd. The company operates primarily in Quebec, the Maritimes and increasingly, in Ontario. Some of its products are sold in New York State, New England, as well as exported to Texas, the Caribbean and Europe.

Lassonde was founded in 1918 by Aristide Lassonde, operating primarily as vegetable canning facility, gradually adding fruit products beginning in 1959. In an attempt to diversify its business, Lassonde acquired Vac-O-Nut, an importer, distributor and marketer of nut and dried fruit products and BHR Bakers Specialties Ltd in 1986. This was followed by international expansions to Thailand, China and Tunisia in the 1990s, but these markets have largely been exited.

Its current focus on the juice category was acquired with the purchase of several juice producers in eastern Canada over the years. In 2001, Lassonde signed a major agreement with Sunkist Growers Inc to produce and market the Sunkist brand primarily in Eastern Canada. In 2004 it solidified a growing position in the Ontario market with the purchase of Alfresh Beverages. Integrating this business was a key focus in 2005, and its operations are now carried out under the Lassonde name.

Lassonde's products are sold in the retail market under proprietary brands as well as private brands of food retailers and wholesalers. The company also has co-packing arrangements for juices and fruit drinks of other major brands.

The company's main competitors include Kraft/Del Monte, McCain, Coca Cola/Minute Maid, Ocean Spray, Procter and Gamble, Sun-Rype and Pepsi/Tropicana. Private brands also remain important, as well as the increasing presence of American brands and other smaller producers of short-life products.

Sun-Rype

Sources: 2006 AIF

Sun-Rype was incorporated in 1946 and operated as a fruit growers cooperative until 1993. At that time, the company completed a capital restructuring, distributing equity shares to the individual growers and formed BC Fruit Processing Ltd to manufacture a 100% pure juice from the apples that grow in the Okanagan Valley, whose warmer climate is ideal for the growth of fruit. The new juice was named 'Sun-Rype' and a suite of other apple products soon followed. Since then, the product line has expanded to include other 100% juices and fruit snacks. Its products are distributed in grocery, convenience and drug stores across Canada, although the beverages are sold primarily in Western Canada.

The Company leverages recent investments in processing and packaging technology at its sole manufacturing facility and headquarters in Kelowna, BC, in the heart of the Okanagan Valley. The Kelowna plant also houses research and development facilities, marketing and administrative support functions. Sun Rype's products are sold through dedicated key account sales reps in the West and for Corporate offices in Ontario, and brokers for the balance of central and eastern Canada. This structure is designed to fully leverage Sun-Rype's brand strengths and maximize each product line's full potential.

Within the western Canadian grocery marketplace, Sun-Rype's products are the brand leaders with 22.6% market share (by volume) in the Juice, Drinks and Nectars category of the ready-to-serve beverage market. Nationally, Sun-Rype's overall market share of the Fruit Snacks and Leathers category is 29.5% (by dollar volume). The company has launched a range of successful new fruit products in recent years, in order to continue to compete in the food and beverage market in Canada.

Historically, Sun-Rype's principal market has been in western Canada; however, its branded food sales have been growing in central and eastern Canada since 1997 and, in recent years, contract manufacturing sales have been growing in the United States. In late 2004 and early 2005, Sun-Rype started to distribute, for the first time, a limited selection of unique juice beverage products in the central and eastern Canadian market. Previously, only food products were distributed nationally. In September 2005, the Company announced it had signed a co-packing agreement to manufacture fruit-based snack bars for a large multi-national food and beverage company for distribution by them in the United States under their brand name. The term of the agreement is for three years and, similar to other third party manufacturing agreements, gives Sun-Rype the exclusive right to manufacture these products on behalf of the customer for a fee specified in the agreement. The agreement does not contain any volume guarantees and its significance to Sun-Rype will depend upon the volume of orders placed by the customer.

While private label products have recently entered the company's portfolio, 88% of sales are still derived from its own brands. Accordingly, the Company maintains its investment in the brand with ongoing consumer communication and advertising programs, allowing it to leverage the brand name into innovative new products and categories.

Sun-Rype prepares customer plans for its products and works with each retailer to maintain overall shelf management within a given product category. Sun-Rype also works with each retailer to develop co-operative advertising and product support plans, under which Sun-Rype provides financial support to retailers for promotional activities such as end-aisle displays and flyer advertisements.

Dover

Dover Industries produces food and paper products for households and the food service industry. Their product line includes flour, ice cream cones, plastic drinking straws, takeout containers and paper cups.

Dover Industries Ltd was created in 1940 with the coming together of three companies, S.J. Cherry and Sons, T.H. Taylor Co Ltd and Robinson Cone, making it Canada's first diversified company. The packaging business grew when, in 1956, the company purchased Filey Hall Paper Box Company Ltd and Howell Lithographic in 1960, eventually combining them into Howell Litho and Cartons. In 1981, Dover purchased paper cup and container manufacturer Bondware (a division of Continental Can), later moving its operations to Brampton, Ontario in 2001. In 2005, the group disposed of its packaging operations.

Dover opened a flour mill in Nova Scotia in 1968 and went on to purchase Halton Flour Milling in 2003.

The food products group operates flour mills and an ice cream cone plant in Ontario and Nova Scotia where there is also a mix plant. The mix plant supplies bakery flour and mixes to the baking industry in Ontario and Atlantic Canada, US border states, Iceland, Puerto Rico and the Caribbean.

Sepp's Gourmet Foods

Sepp's manufactures specialty foods for retail, wholesale, institutional and food service clients in North America and Mexico and certain areas of South America and Asia. They operate through two manufacturing divisions, bakery and savory. The company manufactures either under one of its own brands or the private label of a major retailers, as well as functioning as a co-packer for other manufacturers. Sepp's currently employs 145 people.

In the bakery division, there are two manufacturing locations: one in Burnaby and the other in Richmond Hill. The product line ranges from breakfast dishes (i.e. pancakes and waffles) to wraps and grilled sandwiches. Sepp's also produces goods accredited as AIB (American Institute of Baking), Kosher and Organic. New bakery products include fully cooks grilled cheese sandwiches and stuffed pancakes. Sepp's has maintained a history of developing unique, award-winning, specialty products.

The savory division is located in Innisfail, Alberta, with facilities CFIA/USDA approved and certified organic and HACCP (Hazard Analysis Critical Control Points). This product line includes pastries, hand-held entrees and appetizers. New products available are microwaveable breakfast rolls, mini quiches, and deep dish pizzas.

MRRM

MRRM is an established company, founded in the 1800s by Robert Reford, whose descendants remain active in the company today. MRRM is divided into two subsidiaries, Dainty Foods, which mills, bags, packages and cans several different varieties of rice, and Robert Reford shipping, a ship agency business. The food segment represents over 90% of the company's revenues. In 1946, the company made its initial public offering and is now traded on the TSX-Venture exchange, listed in the Tier-1 category.

Dainty Foods operates the only rice mill in Canada. It imports rice from the U.S., and mills, processes, and packages and cans rice and rice by-products at its AIB and HACCP certified Windsor, Ontario mill. Dainty participates in multiple portions of the value chain, selling products that range from flour that is used in the manufacturing processes of other food processors, to branded finished goods that are distributed to retailers and foodservice outlets.

Beaumont Select Corporations

Beaumont is a management and investment corporation with investments in the food processing and real estate industries and a portfolio of marketable securities.

The food processing division distributes specialty private label and branded products in the frozen food and bakery sectors to food wholesalers and retailers in North America. The food processing division is subdivided into two groups, the frozen food unit and the bakery unit. The frozen food unit focuses on perogies and panzarottis while the bakery unit includes cake, cookie and sandwich products.

The investment division manages a portfolio of securities, which has grown to \$16.8 million. The corporation also maintains a 40% investment in Somerset Properties.

The real estate division seeks out developed and undeveloped real estate opportunities. Currently, the corporation owns three buildings, one in Winnipeg and two in Calgary, all of which are leased to and used by the food processing division. The investment in Somerset also includes approximately 251 acres of land in Alberta as well as a 52% stake in Talisman Homes Ltd.

Appendix 1 - Company Universe

Company Name	Description	Revenue. 2005	Revenue. 2000	5yr Rev Growth	OP.2005	OP.2000	5 G
Brick Brewing Co. Limited	regional brewer of craft and value brands, with sales & marketing focus	62,277	20,805	25%	4,378	484	
Lakeport Brewing Income Fund	produces value-priced beer for the Ontario market	157,082	n/a	n/a	15,534	n/a	
Sleeman Breweries Ltd.	manufactures Sleeman beers and markets reputable global brands in Canada	206,674	141,466	8%	29,092	26,463	
Magnotta Winery Corporation	manufactures and direct distributes wines (also craft beer and spirits)	21,161	15,296	7%	5,693	4,748	
Andrés Wines/Andrew Peller	2nd largest producer, distributor and marketer of branded wines in Canada	167,634	133,638	5%	20,729	16,546	
Vincor	8th largest producer, distributor and marketer of branded wines in the world	653,915	268,196	20%	106,296	37,905	
Lassonde Industries Inc.	developer and manufacturer of fruit and vegetable juices and drinks	323,241	236,219	6%	37,671	26,029	
Dover Industries Limited	food products (flour) and paper cups manufacturer	148,828	134,661	2%	12,330	10,383	
CoolBrands International Inc.	produces and markets ice cream novelties under branded and private labels	385,070	97,488	32% -	33,770	8,600	
Sepp's Gourmet Foods Ltd.	Specialty branded and PL frozen foods for retail and foodservice	21,717	88,472	-24%	365	2,450	
MRRM Inc.	Mills and processes rice, the only rice mill in Canada	40,618	42,650	-1%	2,543	3,487	
Sun-Rype Products Ltd.	leverage B.C. fruit production in juices and fruit products	125,411	94,670	6%	14,023	10,671	
Beaumont Select Corporations Inc.	brands include: Mrs. Willman's Baking, Prestige	39,741	32,127	4%	1,423	3,088	
Jones Soda Co.	develops and markets premium sodas with a strong brand focus	33,511	19,016	12%	581 -	2,625	
E.D. Smith Income Fund	leading North American manufacturer and marketer of branded and PL food	194,811	140,600	7%	14,054	11,500	