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Between the Producer and Retailer: A Review of Wholesale Trade for 2005

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Between the Producer and Retailer: A Review of Wholesale Trade for 2005

**Jean Lebreux,
Distributive Trades Division**

Summary

In 2005, Canada's wholesale trade industry recorded its best performance of the past six years, with much of the impetus coming from the four westernmost provinces.

Wholesalers, who are a key link between manufacturers and the marketplace, sold merchandise worth more than \$470 billion last year, up 5.4% from 2004. However, when adjusted for inflation, the gain was 7.8%, indicating that last year's increase in value was the result of higher volumes.

During the past three years, wholesale companies in western Canada have experienced the strongest growth.

Sales among wholesalers in Manitoba, Saskatchewan, Alberta and British Columbia have risen at an average annual rate of 9.1%. This was nearly double the rate of average growth rate for the nation as a whole, and three times the gain in the other regions of Canada combined.

In 2005, wholesalers in these four provinces together accounted for 60% of the total increase in wholesale sales nationally.

The companies most responsible for last year's gain were those in the machinery and electronic equipment sector, which includes products such heavy industrial equipment as well as computers and office and professional equipment. This sector represented barely 20% of all wholesale sales last year, but it accounted for over 31% of the year-over-year growth.

Several key factors had an impact on the wholesale trade industry in 2005. They included notably lower prices on certain products resulting in part from the stronger Canadian dollar against the American greenback; increased investment by business; the re-opening of the American border on July 18 to trade of live cattle under 30 months of age; the decline in residential housing starts in Canada; and China's growing role in the world economy.

The wholesale trade industry makes a substantial contribution to the Canadian economy. On average, it employed more than 739,000 Canadians in 2005, and it accounted for over 6.4% of Canada's economic output as measured by gross domestic product.

This report examines the performance of wholesale industries nationally and regionally last year, as well as the key factors influencing that performance. (Unless otherwise specified, all data are in current dollars; that is, they have not been adjusted for inflation.)

Wholesalers: Key link in the economy

Most Canadians have no difficulty conjuring up the image of a retailer — whether it is a big box store, a corner store owner or a specialty boutique. Consumers encounter such businesses every day. But who are wholesalers?

Wholesalers are a key link between manufacturers and the marketplace. They anticipate customer needs and demands, buy merchandise, carry inventory, assemble shipments, deliver merchandise, extend credit, provide knowledge on various aspects of marketing products in Canada and abroad, and provide consultation services.

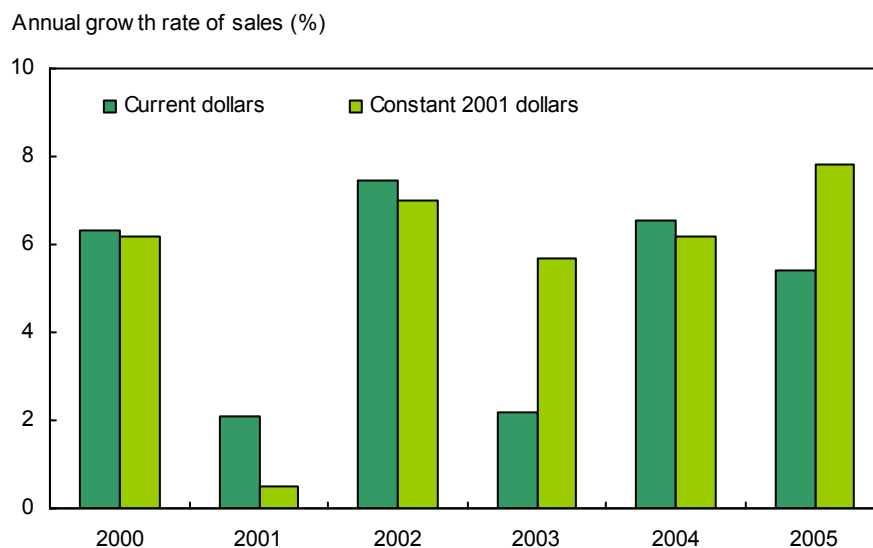
They work in every field from pharmaceuticals to motor vehicles, from building materials to personal goods.

Sales by wholesalers rose 7.8% in 2005 after adjusting for inflation, the largest jump in the past six years. The main beneficiaries of this growth were wholesalers working in the machinery and electronic equipment sector.

Some of this constant-price increase can be attributed to the strength of the Canadian dollar. It continued to solidify in 2005, maintaining an average annual exchange rate of US\$0.825 compared to US\$0.768 in 2004.¹

This translates into lower prices for imports, with Canadian businesses substituting less expensive foreign products for goods made in Canada. Wholesalers were one of the key beneficiaries of this substitution, as about 40% of imported merchandise passes through their hands. The machinery and electronic equipment sector, which is a major player in the import sector, accounted for nearly one-third of the growth in wholesalers' sales last year.

Wholesalers' growth in sales strongest since 2000 (constant prices)



Source: Statistics Canada, Monthly Wholesale Trade Survey.

1. The average annual exchange rate is obtained directly from the Bank of Canada, <http://www.banqueducanada.ca/en/rates/exchange.html>, (accessed April 18, 2006).

Growth in sales slows slightly (current dollars)

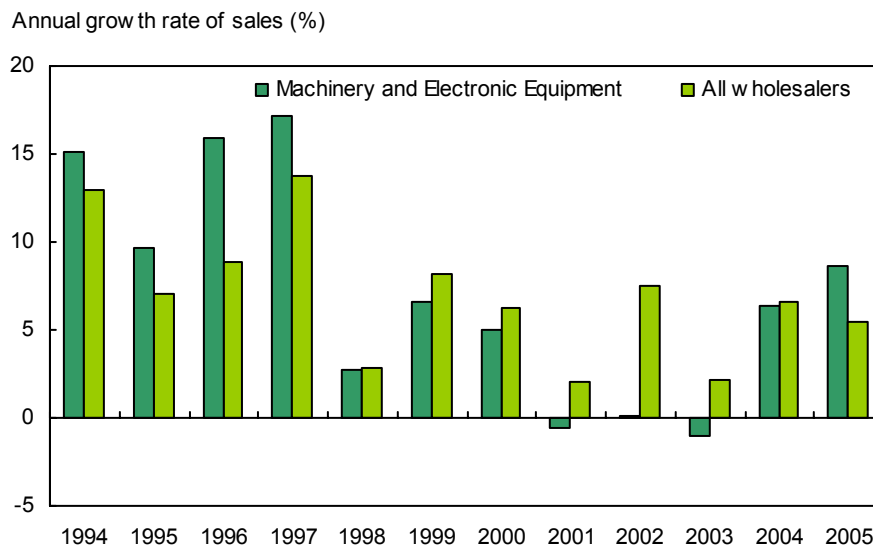
In current dollars, that is, not adjusted for inflation, sales by wholesalers were strong in 2005 but short of previous year's performance. Wholesalers sold \$470 billion in merchandise, a 5.4% gain from 2004. This growth rate was slower than the 6.5% increase the year before.

The rate of growth in sales accelerated in all major trade sectors, except three that explain the slowdown. Consequently, the building materials sector, the motor vehicle, parts and accessories sector and the "other" products sector (which encompasses commodities such as fertilizers, field crop seeds, chemical products and other farm supplies) cancelled out the acceleration of the growth of the other sectors.

Huge investment in machinery and electronics for second year in a row

For a second consecutive year, businesses made huge investments in machinery and electronic equipment. Wholesale sales in this sector exceeded \$95.5 billion, up 8.6% from 2004, well above the national average of 5.4%. This sector represented barely one-fifth of all wholesale sales last year, but it accounted for nearly one-third of the year-over-year growth.

Strongest gain in machinery and electronic equipment sector since 1997



Source: Statistics Canada, Monthly Wholesale Trade Survey.

As they did in 2004, all groups within this sector contributed to the growth. Sales of machinery and equipment climbed 16.2%, a seventh consecutive annual gain. Wholesalers of office and professional equipment posted their second increase in a row in 2005 (+5.7%), along with the computers and other electronic equipment group (+0.3%).

A number of factors contributed to this recent period of robust growth, which began at the end of 2003. First, it should be noted that low interest rates made equipment purchases less onerous.

Last year's private and public investment certainly helped wholesalers in this sector. The Capital and Repair Expenditure Survey showed that for 2005, investments in plants and equipment reached a new high of over \$ 191 billion, an increase of 7.6%.² Higher prices for raw materials, due largely to a sharp increase in world demand, also accelerated many investments, especially in western Canada.

According to Statistics Canada's publication about private and public investment intentions for 2006, investment in equipment should remain strong this year, given the excellent outlook in the energy and public service sectors.³

A growing proportion of goods sold come from China, which generally offers lower cost products. This is especially true in the case of computers and computer accessories, as well as telecommunications equipment. In 2005, import prices on office machinery and equipment fell 17%. The decline for other types of telecommunications equipment and supplies was around 7.6%.⁴ A substantial share of imported machinery and equipment passes through wholesalers.

Building materials: Decline in its growth rate

Wholesalers in the building materials sector recorded sales of more than \$66 billion last year, up 8.5% from 2004. However, this rate of growth was less than half the increase of 20.0% during the previous year. Nevertheless, sales rose in all groups in this industry last year.

2. For more details on results of this survey, see "Private and Public Investment in Canada, Intentions 2006", Statistics Canada, March 2006, Catalogue No. 61-205-XWE.

3. Ibid.

4. Statistics Canada, CANSIM Table 228-0037.

Sharp slowdown in the growth rate in building materials sector

Annual growth rate of sales (%)



Source: Statistics Canada, Monthly Wholesale Trade Survey.

Sales in the first group, lumber, hit nearly \$13 billion, up just 2.5%, a fraction of the growth rate of 23.8% in 2004.

Part of this slowdown was due to lumber prices, which fell by about 5.0%. Overcapacity in North America combined with fiercer world competition also contributed to the downward trend. These results also reflect a change in the housing markets in the United States and Canada.

American builders are turning somewhat from building single-family homes, which demand a high quantity of lumber, to multi-family homes. According to the Canada Mortgage and Housing Corporation, the number of housing starts in Canada fell 3.4% in 2005.

The second group, metal products, which are important in construction, experienced an even sharper slowdown in growth than the lumber group. Wholesalers of metal products sold nearly \$14 billion in goods, up only 7.1% compared with a 33.3% gain in 2004. Prices began to level out in 2005 with China's entry into steel production.

According to the International Iron and Steel Institute, world production for the first 11 months of 2005 rose by slightly more than 1.0 billion tons, the equivalent of a 6.1% increase over the same period in the previous year. At the same time, China's production climbed by over 25.0%. If not for China's increase, world production would have fallen by 1.0%. The levelling out of prices was offset in part by strong demand arising from numerous investments in non-residential building in western Canada.

In the third group, building materials, wholesalers continued to post strong results, with sales of more than \$39 billion. This was an 11.2% increase, a slight slowdown compared with a 14.7% gain the year before. This group has seen virtually uninterrupted growth since the fall of 2003. A strong performance by renovation and construction markets in Canada has been driving this group.

The regions: Growth shifting toward the western provinces

Growth in wholesale sales has shifted to Canada's westernmost provinces during the past three years.

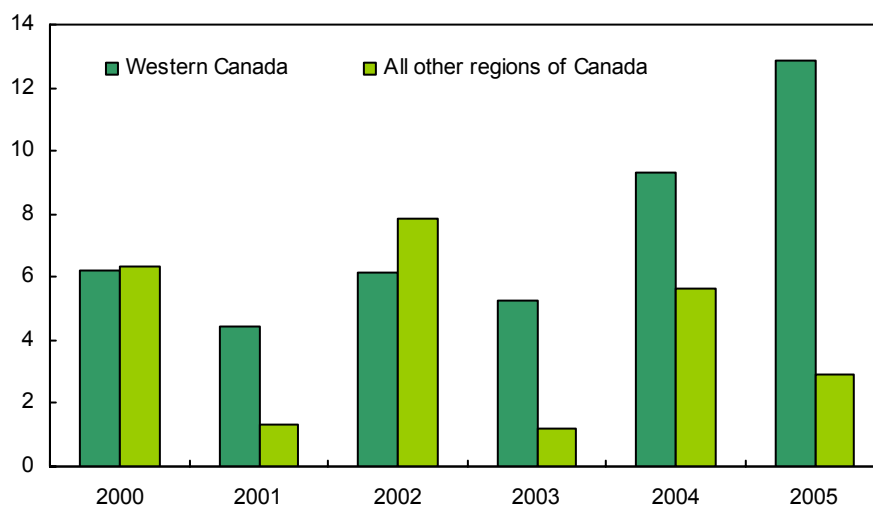
Sales among wholesalers in Manitoba, Saskatchewan, Alberta and British Columbia have risen at an annual average rate of 9.1%. This was nearly double the average growth rate of 4.7% for the nation as a whole, and almost three times the gain of 3.2% in all the other regions of the country combined.

In 2005, wholesalers in these four provinces combined accounted for 60% of the total increase in wholesale sales nationally.

Robust demand for machinery and electronic equipment and for building materials was the main reason for the strong growth in the western provinces. This result was also fuelled by the economic and demographic boom currently sweeping the West, particularly Alberta.

Wholesale growth shifting westward

Annual growth rate of sales (%)



Source: Statistics Canada, Monthly Wholesale Trade Survey.

Prairies: Double-digit growth in all three provinces

All three Prairie provinces recorded double-digit growth rates in wholesale sales last year.

In booming oil-rich Alberta, the growth exceeded the national average for the third straight year. Alberta wholesalers sold nearly \$55 billion in merchandise in 2005, up 15.5%, somewhat higher than the growth rate of 12.8% in 2004. Alberta's sales represented nearly 12% of the total nationwide.

Four trade groups in Alberta posted strong growth in 2005: machinery and equipment, metal products, "other products", and motor vehicles. Sharp increases in oil prices in recent years accounted for much of the increase in sales by machinery wholesalers, as oil companies have accelerated their investments.

In Manitoba and Saskatchewan, sales surged after a relatively soft performance in 2004.

Manitoba wholesalers sold close to \$13 billion in merchandise in 2005, up 16.4% from 2004, the largest percentage increase among the provinces. However, their annual sales represented less than 3.0% of the national total for the year.

Similarly, wholesalers in Saskatchewan had about \$14 billion in sales, up 14.3%. These sales also accounted for less than 3.0% of the national total.

In Manitoba, all major sectors posted increases in 2005, except for the "other products" sector. Personal and household goods performed especially well as a result of positive economic conditions. The Agreement on Textile and Clothing, which imposed quotas on imports, expired on January 1, 2005 which allowed some wholesalers to acquire products at a lower cost. Even before the Agreement ended, over two-thirds (68%) of the clothing sold wholesale in Canada came from abroad. The machinery and electronic equipment sector experienced a growth rate above 10% in 2005, rebounding from a decline the year before.

For their part, wholesalers in Saskatchewan bounced back from lacklustre sales during the previous two years, as all sectors recorded growth. Sales in the farm products sector surged 27.1% with the re-opening of the US border on July 18, 2005 to Canadian cattle under 30 months of age. In December 2005, Japan also announced the opening of its borders to Canadian cattle 20 months and younger.

The "other products" sector in Saskatchewan continued to benefit from the world economic situation with a 17.6% increase, the third straight year of double-digit growth. This extended period of strong growth was due to specific components, such as seeds and fertilizers, as well as chemical farm products, which accounted for about one-quarter of the sector's sales. Foreign demand for such products, particularly from the Asian market, contributed largely to this sector's increase.

Sales in the "other products" sector have been generally on the rise since the fourth quarter of 2003, spurred on by higher prices for several components, notably chemical farm products and recycled metals. Prices for these goods are dictated by the world market, where China is playing an increasingly important role.

British Columbia: Above-average gains for past four years

The growth of wholesale sales in British Columbia has exceeded the Canadian average since 2002. In 2005, the province's wholesalers sold \$47 billion worth of merchandise, an 8.6% increase, compared with the national average of 5.4%.

While growth in 2004 was due largely to an outstanding performance among lumber wholesalers, last year the province's sales diversified. Four trade groups were primarily responsible for the growth: motor vehicles, building materials, metal products and machinery and equipment.

Sales of machinery and electronic equipment rose by 11.5% in 2005 on the heels of a 15.3% gain the previous year. This slowdown was attributable to the computers and office equipment group. However, growth in the machinery group accelerated from 12.6% to 15.7% in 2005.

Sales in the lumber group rose only 3.3%, a fraction of the increase of 46.2% in 2004. A large portion of this group's sales is destined for the United States. However, in 2005, the value of lumber exports fell, owing to a plunge in lumber prices that more than offset higher volumes.

At the same time, production rose substantially following the mountain pine beetle infestation, which forced the province to increase cutting rights by 27% to allow for the harvesting of dead trees. Hurricanes that struck the United States brought some benefit to British Columbia wholesalers since construction starts in that country reached a record high in 2005.

Quebec: Growth just above the national average

Quebec wholesalers sold merchandise worth nearly \$91 billion in 2005, a 5.7% increase, slightly higher than the national average.

Most major sectors posted growth rates that were considerably lower than in 2004. The only exceptions were two sectors: food products, tobacco and alcohol; and the "other products" sector. The sectors recording large declines were the farm products sector and the machinery and electronic equipment sectors. In contrast, companies in the personal and household goods sector continued to benefit from certain favourable economic conditions.

Sales of personal and household goods climbed 8.0%, the second consecutive annual gain. All groups in this sector contributed to the growth. Sales of household goods recorded another significant increase of 14.2% in 2005 following a 23.9% surge in the previous year. There has been a general upward trend in household goods since mid-2003 resulting from the strong performance of the real property market. In 2005, the housing resale market grew by 3.5% and construction starts again topped 50,000.

For their part, wholesalers of pharmaceutical products enjoyed a 5.0% increase in sales in 2005. Although this group records increases year after year, growth rates have been slowing for some time. Average monthly growth, which was quite robust in 2003, began to slow in 2004, due in part to higher use of less costly generic drugs. This tends to have a deflationary impact on prescription drug sales. Indeed, when the province introduced mandatory medical drug insurance in 1997, sales for this group literally exploded with double-digit growth rates for five consecutive years. Since then, growth has slowed.

Sales for clothing wholesalers rose by 3.7%, only partially offsetting the 16.0% drop in 2004. That decline halted three straight years of growth.

Sales in the machinery and electronic equipment sector slowed considerably, rising only 1.3% in 2005, compared with a 9.9% increase in 2004. Companies in two of three groups in this sector registered lower sales. The computers and other electronic equipment group experienced a 6.1% decline, while sales in the office and professional equipment sector edged down 0.3%. For its part, the machinery group experienced a sharp deceleration in its growth rate; sales rose only 8.0% in 2005 compared with 22.9% the year before.

The other products sector was one of the few groups to post an improved growth rate in 2005. Sales in this sector climbed 15.4% in 2005 compared to 13.0% in 2004. Substantial increases in sales of chemical products and recycled metals accounted for part of this performance.

Ontario: Automotive sector puts brakes on growth

Companies in Ontario's huge wholesale trade industry experienced a growth rate of only 2.2% in sales last year, less than half the rate of growth of 5.5% in 2004. In total, they sold \$237 billion worth of goods last year, which represented one-half of the national total.

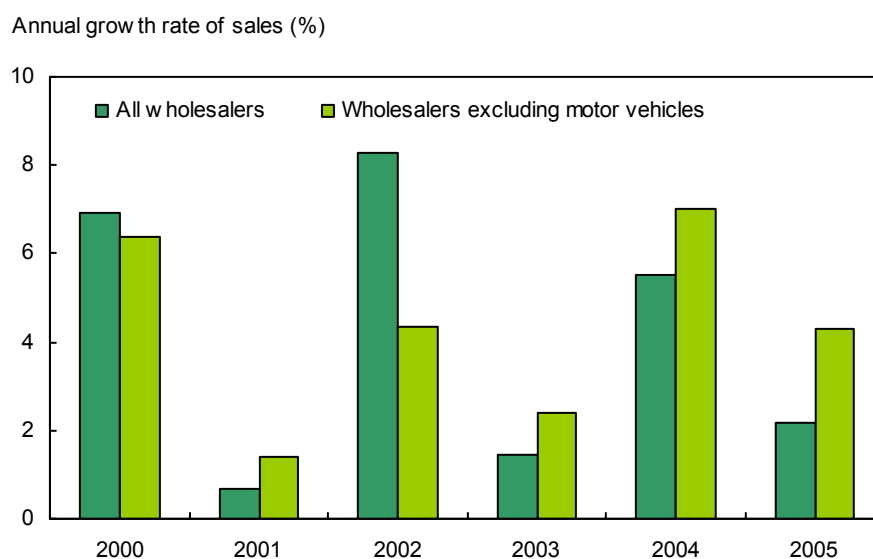
A poor performance in the automotive sector put the brakes on wholesale growth in the province. Excluding the motor vehicle sector, wholesale sales in Ontario grew by 4.3%.

Sales of Ontario wholesalers of automotive parts and products fell by 2.8% in 2005 due mainly to a 2.9% decline in motor vehicle sales. This was the third straight year of decline for this group.

In 2005, Ontario wholesalers accounted for about 79% of total Canadian sales in the motor vehicle sector. This sector represented over one-quarter of the activity of the province's wholesalers.

The Canadian market was the destination for over two-thirds of sales for Ontario wholesalers. The remaining sales were destined for export markets, mainly the United States. In contrast, sales of motor vehicle wholesalers in other provinces were almost exclusively dedicated to the Canadian market.

Automotive sector puts brakes on sales growth for wholesalers in Ontario



Source: Statistics Canada, Monthly Wholesale Trade Survey.

For the year as a whole, retail sales of new automobile vehicles in Canada rose 3.0% to 1,583 million units, the third best result ever recorded. It is important to note that in 2005 a number of manufacturers had to offer major discounts, notably in the form of the preferential usually rates given to only employees. Despite the increase of units sold, these discounts undermined the growth in sales in terms of value.

Motor vehicle parts wholesalers suffered a 2.0% decline in sales last year as well, a far cry from the spectacular 27% gain in 2004. Since this sector sells mainly to retailers and dealers, it is likely that the advance in used vehicle sales had a beneficial impact on this group. Prior to the strong showing

of the Canadian dollar, many used vehicles were sent to the United States. Subsequently, as vehicles became more expensive for the American market, companies had to sell more of them on the Canadian market.

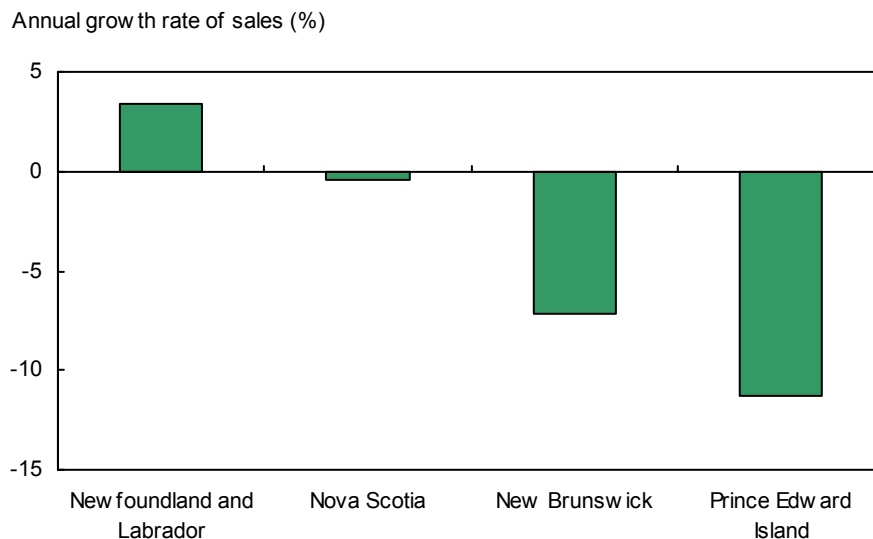
The building materials sector in Ontario also experienced slower growth in 2005. In 2004, this sector posted a growth rate of 21.7%, while in 2005 it slowed to only 7.8%. The slowdown may have been due to a 7.4% decline in housing starts in the province as well as the strong Canadian dollar, which had a negative impact on the export market.

The machinery and electronic equipment sector recorded a 6.0% gain in 2005 compared to 3.9% in 2004.

Atlantic provinces: Sales fall in three of four provinces

Wholesalers in the Atlantic Provinces recorded a decline in activity for the second year in a row in 2005, as sales rose in only one province — Newfoundland and Labrador. However, this had only a small impact nationwide, as total sales in the Atlantic region as a whole accounted for barely 3.0% of the national total.

Newfoundland and Labrador: the only Atlantic province to increase sales in 2005



Source: Statistics Canada, Monthly Wholesale Trade Survey.

Sales rose 3.4% in Newfoundland and Labrador in 2005, halting two straight years of declines. Even though the province ranked second last in terms of wholesale trade activity, its sales hit a record high of \$2.6 billion, slightly higher than the previous record set in 2000. Last year's gain was widespread, as sales went up in six of the seven sectors.

A large portion of the growth can be attributed to the machinery and electronic equipment sector, as well as to "other" products.

In Prince Edward Island, wholesalers experienced a drop in their activity (-11.3%) for the first time since 1997. Sales fell in five of seven sectors. The food products, tobacco and alcohol sector, which accounted for 50% of wholesale activity in the province, recorded a 17.3% decline. This came on the heels of two years of strong gains: 16.0% in 2003 and 15.0% in 2004.

In Nova Scotia, wholesalers posted a drop in sales (-0.4%) for the second consecutive year in 2005. Only two sectors contributed to this slowdown. Activity in the food products, tobacco and alcohol sector fell 12.5%, due in part to weakness in seafood products. A decrease in some fish quotas and lower prices for some products may explain this result.⁵ The building materials sector posted a 1.4% decline, halting 11 years of uninterrupted gains.

In New Brunswick, sales by wholesalers fell 7.2% in 2005. Sharp declines in two sectors — food products, tobacco and alcohol, and machinery and electronic equipment — were behind this result. Together, these two sectors accounted for 43% of New Brunswick's wholesale activity.

5. For more information about provincial exports, see Internet site of Export Development Canada for the document "Global Export Forecast - January 2006 Update - Provincial Export Outlook", http://www.edc.ca/docs/ereports/gef/pdf/Provoutlook_e.pdf (accessed April 18, 2006).

Table 1. Wholesaler's sales by trade groups

Industry	Sales		Annual growth rate
	2004	2005	
	\$ thousands		%
Farm products	5,104,129	5,548,772	8.7
Food products	78,240,648	79,308,468	1.4
Alcohol and tobacco	7,743,289	7,557,960	-2.4
Apparel	8,682,795	10,072,718	16.0
Household and personal products	25,330,927	27,747,576	9.5
Pharmaceuticals	28,550,969	30,205,405	5.8
Motor vehicles	72,902,563	73,074,166	0.2
Motor vehicle parts and accessories	18,268,195	18,499,611	1.3
Building supplies	35,331,435	39,302,537	11.2
Metal products	12,663,929	13,566,165	7.1
Lumber and millwork	12,947,473	13,264,829	2.5
Machinery and equipment	38,925,393	45,240,054	16.2
Computer and other electronic equipment	28,507,642	28,606,314	0.3
Office and professional equipment	20,516,657	21,687,331	5.7
Other products	52,493,984	56,665,087	7.9
Total	446,210,028	470,346,992	5.4
Source: Statistics Canada, Monthly Wholesale Trade Survey, CANSIM Table 081-0007.			

Table 2. Wholesalers' sales by province and territories

	Sales		Annual growth rate
	2004	2005	
	\$ thousands		%
Newfoundland and Labrador	2,503,946	2,588,180	3.4
Prince Edward Island	591,699	524,808	-11.3
Nova Scotia	6,266,660	6,241,763	-0.4
New Brunswick	5,238,442	4,863,784	-7.2
Quebec	85,760,989	90,627,611	5.7
Ontario	231,961,116	237,004,415	2.2
Manitoba	10,904,613	12,696,681	16.4
Saskatchewan	11,935,143	13,644,694	14.3
Alberta	47,220,594	54,550,592	15.5
British Columbia	43,521,225	47,276,978	8.6
Yukon Territory	85,900	95,086	10.7
Northwest Territories	192,703	207,583	7.7
Nunavut	26,997	24,816	-8.1
Canada	446,210,028	470,346,992	5.4
Source: Statistics Canada, Monthly Wholesale Trade Survey, CANSIM Table 081-0007.			