Canadian Dairy Commission | Commission canadienne du lait

CANADIAN DAIRY COMMISSION

Annual Report 17-18

Canada

Mandate of the Canadian Dairy Commission

Under the *Canadian Dairy Commission Act*, the CDC's legislated objectives are:

- to provide efficient producers of milk and cream with the opportunity to obtain a fair return for their labour and investment; and
- to provide consumers of dairy products with a continuous and adequate supply of dairy products of high quality.

Mission statement

To provide leadership to enhance the vitality of the Canadian dairy industry for the benefit of Canadians.

Values

Excellence | Integrity | Leadership | Respect

Commission staff is available to serve you, in either official language, from 8 a.m. to 4:30 p.m. Eastern time, Monday to Friday (statutory holidays excluded).

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Catalogue No.: A88-2018

ISSN: 0382-3229

Design and production:
Element Design and Communications

Printing: Gilmore Printing Services Inc., printed in Canada

Table of Content

Message from the Chairman

I am pleased to present the Canadian Dairy Commission's (CDC) Annual Report for the 2017-2018 dairy year. The dairy industry has had many successes and challenges in the past year, both domestically and on the world stage, all of which were handled with professionalism and dedication from CDC staff and in co-operation with industry partners. From rising demand for dairy products to the widespread support for supply management, it is clear that the dairy industry is important to Canadians. The CDC is proud of its accomplishments and contributions to this industry over the last year. It is in a sound financial position and has achieved most of its objectives.

After its Scholarship Program ended on July 31, 2017, the CDC conducted inclusive consultations with dairy industry and academia partners to explore options to expand its financial support beyond graduate scholarships. A new comprehensive program, the Workplace Development Initiative (WDI) was launched in April 2018. It includes additional elements such as post-secondary curricula and continuous training. This new initiative provides funding to the Canadian dairy industry for the development and training of skilled employees in dairy production and manufacturing to improve productivity and competitiveness. The initiative also promotes graduate studies in dairy and animal science to support research and help introduce new products, technologies, and markets to the dairy industry. In addition, it includes a Career Promotion Program to attract people into this industry.

The CDC continues to encourage the Canadian dairy industry to grow the market, innovate and adapt to new market realities. The CDC offers programs and services for the benefit of the industry. With programs such as Milk Access for Growth, which promotes investments in milk processing facilities by guaranteeing milk supply; the Matching Investment Fund, which provides non-repayable contributions for innovative projects and products that increase the use of dairy ingredients; and the Dairy Innovation Program, which provides milk to processors manufacturing

innovative dairy products, the CDC has funded and facilitated projects that have introduced many new products using Canadian milk or dairy ingredients.

The CDC's commitment to supporting the industry is ongoing. In the fall of 2016, it conducted a survey of dairy industry stakeholders to obtain their opinion of the CDC's level of success in accomplishing its role and responsibilities; identify changes in the industry over the next decade that will have an impact on the sector and the work of the CDC; assist the CDC in identifying areas for improvement; and gather stakeholder insights and observations to help inform the CDC's strategic and business planning. The level of participation was high. The survey was followed by a facilitated session on the priorities that the CDC would need to address over the coming years. The CDC then developed an action plan to address the issues raised. The CDC is proud of the actions it has taken so far, and the results of the survey will be re-examined to determine what other areas of improvement should now be addressed. The CDC will continue to implement the action plan over the coming year to ensure that the organization remains an important and vital institution in the Canadian dairy sector and continues to play a key role in ensuring the supply management system runs smoothly.

In May 2018, Mr. Serge Riendeau joined the CDC Board as the new Chief Executive Officer (CEO). Mr. Riendeau is a dairy farmer from Coaticook, Quebec and is a leading figure in the Canadian dairy industry, having occupied a position on the board of Agropur Cooperative for 26 years and having been its president for 15 years. We are pleased to welcome Mr. Riendeau to the CDC. His skills, experience, and knowledge of the industry will be a great contribution to the CDC and to the dairy industry.

I would like to take this opportunity to recognize outgoing CEO, Mr. Jacques Laforge. Mr. Laforge is well known for his leadership and vision. Throughout his career, Mr. Laforge has shown a strong dedication to his fellow farmers and to processors. During his time at the CDC, Mr. Laforge was devoted to his role on the Board and to his responsibilities to the industry and to staff. He contributed countless innovative ideas, generously shared his deep understanding of this industry, and promoted a culture of excellence among staff. On behalf of the Board and the employees, I would like to thank Mr. Laforge for his many contributions to the CDC and to the Canadian dairy industry.

As CDC Chairman, I would like to offer my sincere gratitude to industry stakeholders, provincial governments, the Minister's Office and our colleagues at Agriculture and Agri-Food Canada and the other Agriculture and Agri-Food Portfolio organizations for their constant co-operation and support. I also applaud the invaluable contributions of the CDC employees who run our operations with efficiency and passion, and who demonstrate on a daily basis their dedication to this dynamic industry.

Alistair Johnston

Message from the CEO

The Canadian Dairy Commission (CDC) is proud to partner with the Canadian dairy industry, an industry characterized by dedication, collaboration, and a desire to continuously improve. Each link of the value chain aims to ensure that Canadians have access to a continuous and adequate supply of high quality, nutritious dairy products. Having joined the CDC in May 2018, I am proud to be part of an organization that supports such a vibrant sector. What follows are highlights of the 2017-2018 dairy year.

DAIRY INDUSTRY TRENDS

Production

In 2017-2018, the number of dairy farms in Canada decreased by 329, a 2.9% reduction over 2016[1]. This rate is lower than for United States or European dairy farms[2]. This global trend is expected to continue. As a result, the remaining farms produce more milk and generate more revenue per farm.

Despite this reduction in the number of farms, thanks to the productivity and efficiency of producers, milk production increased to 380 million kg of butterfat over the course of the 2017-2018 dairy year. This represents an increase of 6.1%, and helped respond to a rapid growth in demand for dairy products.

Processing

In 2017, Canada's dairy processing sector contributed $14.3 billion and approximately 23,400 jobs to Canada's economy.

1 Despite having fewer farms, Canada produces 21% more milk than 5 years ago to respond to domestic demand.

2 US dairy farms declined 3.9% between 2015 and 2017, 5.1% for the EU and 4.6% for Australia (International Dairy Federation). In Canada, the overall number of farms has decreased by 6% between 2011 and 2016, the years of the last two Census of Agriculture.

Consumption

Over the last year, Canadian consumers reduced their per capita consumption of fluid milk and frozen yogurt but increased their consumption of cream, cheeses and ice cream[3]. Manufacturers have responded to these trends. Canada now produces over 1,050 cheeses, most of which are made with cow milk. Innovation programs administered by the CDC have certainly been a factor in the development of some of these new products. For example, since the beginning of the Dairy Innovation Program[4] in 1989, over 380 projects to create new cheeses, yogurt products and other dairy products used close to 126 million litres of milk. The Matching Investment Fund, launched in 2009, has financed 25 innovation projects that have received a total of over $992,000. Cheese, skim milk powder, and fluid milk are the main ingredients involved in these projects for the development or reformulation of dairy desserts, cheese-

3 Source: www.dairyinfo.gc.ca

4 Previously known as the Domestic Dairy Product Innovation Program which was replaced by the Dairy Innovation Program on August 1, 2013. Program parameters are essentially the same.

based and nutraceutical[5] products, and dairy-based confectionery products.

In 2017-2018, retail sales of dairy products were strong for most categories. Demand for butter and cream remained strong with a respective 3.4% and 4.8% rate of increase at the retail level. In addition, growth in cheese consumption has persisted, particularly for cheddar, everyday cheeses like Mozzarella, Feta, and Havarti, and fine cheeses such as Brie and Camembert.

The trend related to a steady increase in demand for higher butterfat dairy products continued. This required a 3.7% year over year increase in quota to serve the Canadian market. Repeated quota increases along with a 5% growth allowance boosted milk production which enabled CDC and private butter inventories to rebuild and reach sufficient levels. As production caught up with demand, the CDC and the provincial marketing boards put measures in place to adjust growth in production to Canadian requirements.

Market Development

Over the course of the year, the CDC continued to encourage investments in processing that would either add value to the solids non fat or increase demand for Canadian milk. The Milk Access for Growth program, which guarantees a sufficient supply of milk to encourage new investments in the dairy sector to grow the overall Canadian demand for milk and milk products, received two applications which were accepted.

Trade

Canada and the European Union (EU) reached an agreement in August 2014 towards the Comprehensive Economic and Trade Agreement (CETA). CETA went into provisional application on September 21, 2017. This agreement gradually increases the EU access to the Canadian cheese market by 17,700 tonnes. In comparison, Canadian cheese production in 2017 was 497,288 tonnes. The CDC will take these additional imports into account when calculating production quota.

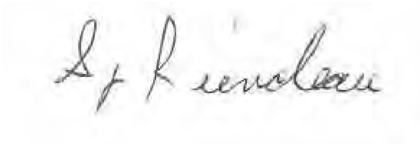
5 Nutraceutical refers to natural foods thought to have a beneficial effect on human health. The classic example is yogurt with probiotics. Some specific milk proteins could also have benefits but more research is needed.

WORKPLACE TRENDS

The CDC continues to follow and contribute to Blueprint 2020 initiatives and implement relevant Government of Canada policies. Following the tradition established by my predecessor, I continue to meet with all staff at least four times a year to discuss changes in the workplace and industry orientation. Directors meet with their staff at least twice a year to discuss priorities and to give staff an opportunity to present concerns and ask questions. Employees also have the chance to contribute to the CDC's strategic planning during the CDC's yearly strategic planning exercise.

In 2018, as part of an ongoing workplace assessment exercise, the CDC conducted its fifth annual employee satisfaction survey. The objective of the survey is to provide a snapshot of a number of themes and issues relevant to the CDC. The response rate this year was 87%, similar to what it was in 2017. The overall satisfaction rate was 98% in 2018, up from 94% in 2017. This demonstrates that the overall health of the organization is increasingly positive. Over the next year, the CDC will address, through an action plan, any organizational concerns identified by the survey.

In closing, I would like to thank all the dedicated CDC employees for their professionalism in running our operations with efficiency and integrity. It is an honour to be part of an organization that is committed to the advancement and betterment of the Canadian dairy industry.



Serge Riendeau

The Canadian Dairy Commission

The Canadian Dairy Commission (CDC) is a Crown corporation created in 1966 by the *Canadian Dairy Commission Act*. The CDC reports to Parliament through the Minister of Agriculture and Agri-Food to whom it serves as an advisor on matters related to the dairy industry. The CDC plays a central facilitating role for the dairy industry. In addition to operating elements of the milk supply management system, managing milk price setting for producers, and ensuring milk production meets demand, the CDC administers several programs on behalf of the industry and encourages the industry to grow the market and innovate. Activities such as audits, pooling calculations, exports, imports, and setting quota are also part of the CDC's role and are progressing as per the CDC Strategic Plan.

The CDC is part of the Agriculture and Agri-Food Portfolio along with Agriculture and Agri-Food Canada, the Canadian Grain Commission, Farm Credit Canada, the Farm Products Council of Canada, and the Canada Agricultural Review Tribunal. The CDC also works in partnership with the Canadian Food Inspection Agency.

The federal government funds about half of the CDC's administrative costs. Other costs, including marketing activities, are funded by dairy producers, the CDC's commercial operations, and the marketplace. The CDC borrows money from the Consolidated Revenue Fund and from a line of credit to finance the programs it administers on behalf of the dairy industry.

Since supply management was first applied to the dairy sector, the CDC has been in charge of two critical parts of the system: managing milk price setting and recommending milk production quota. Through its many roles and central facilitating function in the dairy industry, the CDC ensures that Canadian dairy farmers have the opportunity to obtain a fair return for their labour and investment.

The CDC monitors national production and demand and recommends the necessary adjustments to the national production target for milk. It ensures that milk production in Canada matches demand from Canadian consumers. It is important to avoid any shortage of dairy products and just as important to avoid production surpluses that are costly to handle, store and market.

To achieve its mandate, the CDC works with provincial governments and dairy industry stakeholders such as dairy producers, processors, further processors and consumers. On behalf of the dairy industry, it administers the revenue and market pooling agreements and develops, implements, and administers major programs such as the Special Milk Class Permit Program, the Dairy Innovation Program, the Dairy Marketing Program, the Dairy Export Program and the Milk Access for Growth[6].

The CDC chairs the Canadian Milk Supply Management Committee (CMSMC)[7] and in this capacity, apprises the committee on matters that require resolution and, when necessary, proposes various solutions, alternatives or recommendations to enhance orderly and efficient marketing with an eye to avoiding deficit or surplus milk production. The CDC performs a similar role for the Eastern Canadian Milk Pool (P5) and the Western Milk Pool (WMP)[8].

6 A description of CDC's programs is presented in the section of this report entitled *Activities and Programs*.

7 The CMSMC is the main national decision-making body of the dairy industry.

8 See p.18 for more information on these pools.

CDC AT A GLANCE

Created in 1966

72 employees (as of July 31, 2018)

Location: Ottawa

Web site: www.cdc-ccl.gc.ca

Administrative budget 2017-2018 (dairy year): $9.15 million

Dairy year: August 1 to July 31

Mission

To provide leadership to enhance the vitality of the Canadian dairy industry for the benefit of Canadians.

Values

Excellence, integrity, leadership and respect

THE CANADIAN DAIRY INDUSTRY

At the Farm

In 2017, 10,951 dairy farms were shipping milk in Canada. The average farm had 86 cows and an average annual production of 34,703 kg of butterfat[9], a production higher than that of 2016. Quebec and Ontario had the greatest percentage of dairy farms at 82%, followed by 12% in the Western provinces, and 6% in the Atlantic Provinces. Dairy farms generated $6.6 billion in total farm cash receipts.

Milk Processing

In 2017, the dairy processing industry generated $14.3 billion worth of products shipped from 478 processing plants (279 of which were federally registered) accounting for 12.7% of all processing sales in the food and beverage industry. As a key contributor to the Canadian economy in 2017, dairy production ranked second behind meats in terms of the value of its manufactured shipments. The dairy processing sector employed approximately 23,400 workers.

Milk Markets

Provincial marketing boards and agencies purchase milk from producers and sell it to processors for the manufacture of dairy products. The milk sold to processors in Canada is classified according to its end use based on the Harmonized Milk Classification System[10]. The price paid for milk by processors varies according to the milk class.

In the 2017-2018 dairy year, the fluid milk sales accounted for approximately 26% of total sales or 100 million kg of butterfat. The industrial milk market accounted for the remaining 74% of total sales or 279 million kg of butterfat.

9 Milk production in Canada is expressed in kg of butterfat.

10 Harmonized Milk Classification System (http://www.cdc-ccl.gc.ca/CDC/index-eng.php?id=3811)

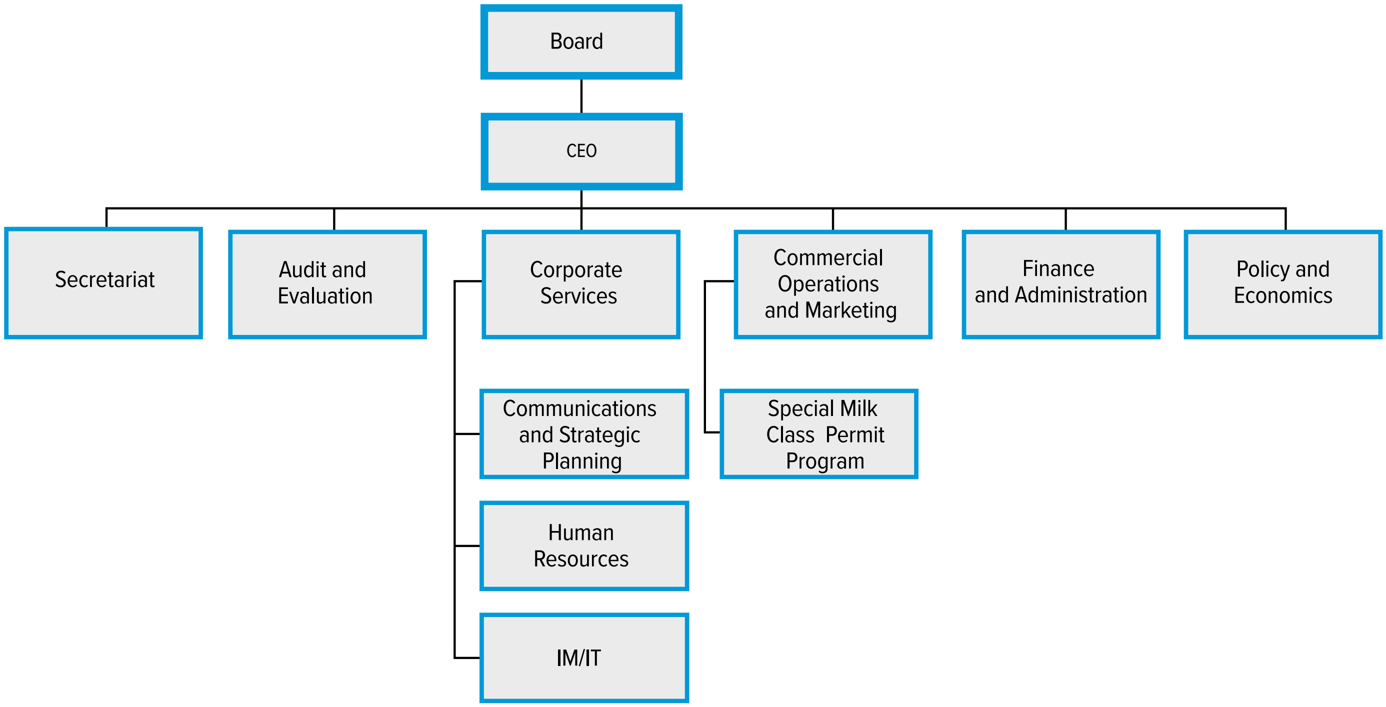
Governance

The Canadian Dairy Commission (CDC) is governed by the *Canadian Dairy Commission Act*, the *Financial Administration Act*, and the *Public Service Labour Relations Act*. It is also governed by the following regulations:

- the Dairy Products Marketing Regulations
- the EEC Aged Cheddar Cheese Export Regulations.

It reports to Parliament through the Minister of Agriculture and Agri-Food.

Structure of the Canadian Dairy Commission



GOVERNING BOARD

The governing board of the CDC is made up of a chairperson, a commissioner, and a chief executive officer (CEO). The CDC Board members are appointed by the Governor in Council and fulfill their mandates on a part-time basis. Members of the Board have a lengthy and varied experience in the dairy industry and together, they bring a balanced approach to decision-making.

The governing board is responsible for the overall stewardship of the organization. It approves the CDC's corporate plan, annual report, strategic plan, budget and financial statements. It develops policies for the CDC, and ensures that the principal business risks are identified and that appropriate systems to manage these risks are in place. It also receives and addresses the annual audit and the special examination reports of the Office of the Auditor General.

BOARD MEMBERS

Chairman (appointed on May 28, 2015, for a four-year term effective August 1, 2015)

Alistair Johnston

Mr. Johnston arrived in Canada in 1988 and joined the Northern Alberta Dairy Pool as Director, Operations, subsequently holding leadership roles within Dairyworld Foods and the Vanderpol Food Group. For the past several years he has provided technical and strategic assistance to dairy and food manufacturing enterprises domestically and internationally. He has extensive board experience with the BC Chicken Marketing Board and BC Investment Agriculture Foundation, BC and Alberta Dairy Associations, and the BC Food Processors Association.

Commissioner (appointed on January 3, 2017, for a three-year term)

Jennifer Hayes

Ms. Hayes is a dairy and beef farmer on Quebec's Gaspé Peninsula. She is the third generation to farm at Pine Crest Farms in Shigawake, which she co-owns with her father and uncle. Her farm is the most eastern dairy farm on the mainland in Quebec. Ms. Hayes has extensive governance experience as an active member of the UPA (*Union des producteurs agricoles*). In addition to her position as a regional elected board member for Les Producteurs de lait de la Gaspésie-Les-Îles, Ms. Hayes was regional vice president for the beef producers association, and an executive member of the provincial cull cattle and bob calf marketing committee.

Jennifer Hayes, Commissioner
Alistair Johnston, Chairman
Serge Riendeau, Chief Executive Officer

Chief Executive Officer (appointed May 14, 2018, for a three-year term))

Serge Riendeau

Mr. Riendeau is a leading figure of the Canadian dairy industry. He has occupied a position on the board of the Agropur co-operative for 26 years and was its president for 15 years. In 2017, Mr. Riendeau retired and left his position as president of the cooperative. His management experience is rich and varied. From 1991 to 1997, Mr. Riendeau was involved in municipal politics as a counselor and mayor of the town of Barnston in Quebec. Mr. Riendeau is co-owner of Riendeau and Gendron Farm along with his wife and his son, who is the main shareholder. The farm has a production quota of 250kg/day and 1,000 acres of land.

BOARD COMMITTEES

Audit Committee

The Audit Committee ensures proper accountability over CDC operations as required by the *Financial Administration Act*. It reviews and approves the annual audit plan of the Auditor General and actively solicits the Office of the Auditor General's expertise regarding the corporation's accounting principles and financial reporting. The committee meets quarterly to review the financial statements and receive internal audit and program evaluation reports.

Members

- Commissioner (chair)
- Chairperson
- Chief Executive Officer

Senior Management Team

The Senior Management Team (SMT) meets approximately every two weeks to discuss the daily operations of the CDC and to make the required decisions. It is supported by four advisory committees that develop plans and priorities, and advise management on human resources, internal audits and program evaluation, security, and occupational health and safety.

The SMT creates and amends CDC policies and reviews the administrative budget before it is presented to the Board. It also addresses issues relating to human resources, audit, evaluation, and governance, and acts as a sounding board for the CEO on industry-related matters and on recommendations to be presented to the Board.

Members

As of July 31, 2018, in addition to the CEO, the following people make up the SMT.

- Senior Director, Commercial Operations and Marketing
- Director, Audit and Evaluation
- Director, Corporate Services
- Director, Finance and Administration
- Director, Policy and Economics
- Corporate Secretary

MANAGEMENT COMMITTEES

Human Resources Advisory Committee

The Human Resources Advisory Committee's mandate is to provide advice to the SMT on human resources priorities and initiatives. It meets twice a year or at the request of the chairperson.

Members

- Director, Corporate Services (chair)
- Manager, Human Resources Programs
- Advisor, Human Resources (secretary)
- A representative of employees in each service
- A representative of managers

Internal Audit and Program Evaluation Advisory Committee

This committee develops internal audit and program evaluation plans for the review of CDC's systems, programs, policies, and practices. It is also responsible for monitoring the progress of internal audits and program evaluations as per the approved plans and of the resulting management actions. It meets at least three times per year and at the request of the chair.

Members

- Chief Executive Officer (chair)
- Senior Director, Commercial Operations and Marketing
- Director, Audit and Evaluation
- Director, Corporate Services
- Director, Finance and Administration
- Director, Policy and Economics
- Manager, Audit
- Senior Financial Officer

Occupational Safety and Health Committee

The Occupational Safety and Health Committee (OSH) serves as an advisory body to the SMT for all matters relating to the health and safety of CDC employees as mandated by the Canada Labour Code and associated regulations.

Members

- 1 employee representative (co-chair)
- 1 employer representative (co-chair)
- 1 secretary
- 1 employee representative
- Champion of Mental Health (*ex-officio*)

Risk and Security Committee

The Risk and Security Committee's mandate is to assist the SMT in meeting the security requirements of the Government of Canada related to the CDC's employees, information and assets, as well as in identifying and monitoring corporate risks and controls.

Members

- Departmental Security Officer
- Director, Corporate Services
- Senior Financial Officer

GOVERNANCE AT THE CDC

In the fall of 2017, the Board approved the Annual Report and Financial Statements of the CDC for the 2016-2017 dairy year. In April 2018, the Board also approved the CDC's Corporate Plan for the period starting in 2018-2019 and ending in 2022-2023. The Corporate Plan contains all the major directions of the corporation as well as its forecasted budgets and borrowing plan. It was approved by Treasury Board on May 31, 2018. To ensure that the CDC's borrowing capacity was in line with rising milk production the CDC prepared amended Corporate Plans for 2017-2018 to 2021-2022 and 2018-2019 to 2022-2023 in June 2018. These were approved by Treasury Board on June 26, 2018.

The CDC updated its Corporate Risk Profile in January 2018. The profile defines each risk, describes the existing measures for managing the risk and the group responsible for implementing these strategies, and it is taken into account when performing the environmental analysis during the strategic planning process. The Audit Committee approves the measures contained in the Corporate Risk Profile and these measures are monitored by the Internal Audit and Program Evaluation Advisory Committee on a regular basis.

The Audit and Evaluation division completed the second phase of an internal audit on Core Controls which was approved by the Audit Committee. Recommendations and management actions were also approved as part of this process. This audit mainly assessed the CDC's effective and efficient management of its resources, both financial and non-financial. This internal audit has been a priority among various government departments with the Office of the Comptroller General placing a great importance on the prudent stewardship of public resources.

The CDC held its annual public meeting in January 2018 in Ottawa. This meeting is open to the public but is generally attended by about 50 representatives of the dairy industry. It gives the CDC the opportunity to report on its financial statements and strategic objectives for the past and current dairy years and to answer any questions from participants.

Chantal Laframboise, Director, Finance and Administration; **Danie Cousineau,** Corporate Secretary; **Christine Boutin,** Senior Director, Commercial Operations and Marketing; **Hossein Behzadi,** Director, Audit and Evaluation; **Benoit Basillais,** Director, Policy and Economics; **Chantal Paul,** Director, Corporate Services

Activities and Programs

The Canadian Dairy Commission (CDC) monitors demand and adjusts the supply of milk, ensures a fair return to producers, encourages market development, provides auditing services, and supports the industry by providing many technical and administrative services and administering various programs.

SUPPLY MANAGEMENT

Determining and Adjusting Quota

The CDC monitors trends in total demand[11] and milk production (supply) monthly. This allows it to adjust the national production quota every month to reflect changes in the demand for milk products. The objective when establishing production quota is to minimize the possibility of shortages or surpluses in the domestic market. Any surplus that occurs is managed by adjusting the quota, by temporarily storing surpluses at the expense of producers or, as a last resort, by exporting dairy products within Canada's trade commitments.

From August 1, 2017, to July 31, 2018, total milk demand increased by 1.9% from the previous year, to reach 371.1 million kg of butterfat. During the same period, the total quota also increased by 3.7%. As a result of quota increases this year and last year, milk production increased by 6.1% to 380.03 million kg of butterfat. With milk production being very strong, butter stocks had increased by the end of dairy year 2017-2018.

Supplying Growth

On May 1, 2018 the CMSMC eliminated the temporary 3% growth allowance. This measure responded to strong production trends in the industry. The CMSMC is considering changes to the methodology used to adjust quota in order to respond more rapidly to variations in demand. Beyond continued robust domestic production, the market has been supplied with 3,274 tonnes of butter comprised of the tariff rate quota that the CDC imports in any normal year.

Removing Surplus

The CMSMC directs the CDC in the operation of the Surplus Removal Program. The program ensures that milk surplus to the domestic market is removed in the appropriate region and in a timely fashion. Returns from this program are shared among all Canadian producers through the Comprehensive Agreement on Pooling of Milk Revenues. The CDC exported a small quantity of butter (50 tonnes) under this program this year due to excess milk production.

CDC inventories of skim milk powder (SMP) for animal feed went from 38,190 tonnes to 12,706 tonnes. Sales of SMP to the animal feed sector will continue until the inventory is fully depleted. The CDC has signed firm contracts for almost all the powder remaining in stock.

11 The quantity of butterfat required to fulfill domestic demand and planned exports for dairy products.

Adjusting Supply

The Domestic Seasonality Programs allow the industry to cope with the seasonal demand for dairy products. The industry has mandated the CDC to operate these programs in co-operation with the private sector. Generally, the CDC buys and stores products when consumption is low and sells them to processors when consumption rises. As production increased throughout the year, the CDC was able to rebuild its butter stocks.

Summary of transactions under the Domestic Seasonality Programs

	Opening inventory	Purchases	Sales	Closing inventory
	tonnes			
Butter	16,210	38,754	29,893	25,071

Imports

Under the terms of the 1994 WTO Agreement on Agriculture, Canada has established tariff rate quotas (TRQ) for a number of dairy products. TRQs are the quantities of products that can enter Canada with little or no tariff. With the support of the industry, the CDC has acted as the receiver of butter imports under federal permit since 1995 and has directed this product to the food sector through butter manufacturers. The TRQ for butter is 3,274 tonnes. Of this, approximately two thirds (2,000 tonnes) is specifically allocated to New Zealand.

During the 2017-2018 dairy year, the CDC imported its full TRQ commitment of butter of 3,274 tonnes, including more than 2,000 tonnes from New Zealand. Since production was sufficient to meet demand for butter, Supplementary Import Permits were not required.

PRODUCER REVENUES

Pricing

As part of the supply management system, the price that producers get for their milk is regulated and varies depending on the end use of the milk. Price adjustments at the farm level for milk classes 1 to 4 are based on a combination of annual changes in the cost of production and the consumer price index. The cost of production is measured annually by the CDC and the consumer price index is obtained from Statistics Canada.

SMCPP – volume of milk sold (million kg butterfat) and average producer revenue ($/hl)*

Class		2013-2014	2014-2015	2015-2016	2016-2017	2017-2018
5(a) (cheese)	Volume	7.61	8.09	7.96	8.56	8.58
	Price	$48.24	$50.42	$44.18	$47.49	$44.00
5(b) (other ingredients)	Volume	17.50	16.05	11.82	13.79	19.16
	Price	$50.89	$46.88	$40.66	$43.26	$41.42
5(c) (confectionery)	Volume	6.37	5.86	5.31	6.37	2.91
	Price	$48.60	$33.35	$27.68	$37.94	$40.13
Total	**Volume**	**31.48**	**30.00**	**25.09**	**27.02**	**30.65**
	Price	**$48.99**	**$44.89**	**$38.99**	**$44.56**	**$43.00**

*Prices are calculated at 3.6 kg of butterfat per hectolitre, using the latest compositional standards for all dairy years.

The CDC support price for butter is also a factor in class pricing. The CDC held regular pricing consultations in November 2017. Despite a small reduction in the cost of producing milk in Canada, for the sake of the industry's stability, the CDC decided to maintain the support price of butter at $8.0062/kg.

Given the increase in the cost of production during the year, the CDC held special pricing consultations in July 2018. The CDC decided to increase the support price of butter from $8.0062 to $8.3901/kg, effective September 1, 2018. This support price adjustment is expected to increase overall producer revenue by approximately 4.1%, and raise class 1 to 4 butterfat and solids nonfat prices by an equivalent amount.

Pooling of Markets and Producer Returns

In its role as a national industry facilitator, the CDC administers the three federal-provincial agreements that frame the sharing of revenues and markets among Canadian milk producers on behalf of the dairy industry.

Comprehensive Agreement on Pooling of Milk Revenues (P10 Agreement)

The Comprehensive Agreement on Pooling of Milk Revenues provides a means for the market returns from the sale of milk to processors under the Special Milk Class Permit Program (SMCPP) to be shared among the dairy producers of all ten provinces. Based on this agreement, the CDC administers the SMCPP on behalf of the industry.

Under the SMCPP, implemented in 1995, competitively priced milk is made available for use in processed products containing dairy ingredients. Further processors access these dairy ingredients by means of a Special Class permit issued by the CDC.

Further processors used the equivalent of 30.65 million kg of butterfat in the 2017-2018 dairy year, an increase of 13.4% over the previous year. The increase is mostly explained by additional sales of Canadian butter for further processing. The average revenue obtained by producers from these three classes amounted to $43.00/hl compared to $44.56/hl for the previous year. On July 31, 2018, there were 1,826 active program participants.

Regional Pooling Agreements

Agreement on the Eastern Canadian Milk Pooling (P5 Agreement)

The Agreement on the Eastern Canadian Milk Pooling provides a means for revenues from all milk sales, transportation costs, markets, and the responsibility for skim-off[12] to be pooled among dairy producers in Ontario, Quebec, New Brunswick, Nova Scotia and Prince Edward Island. The CDC chairs the meetings of the Supervisory Body of the pool, administers the pooling agreement, completes pooling calculations, and provides technical expertise and secretariat services to the P5.

Western Milk Pooling Agreement

Since 1997, Manitoba, Saskatchewan, Alberta and British Columbia form the Western Milk Pool (WMP) which shares revenues and markets for all

12 Excess butterfat from the fluid milk market

milk classes. The CDC chairs the WMP Coordinating Committee and administers the pooling agreement, performs the pooling calculations and provides technical expertise and secretariat services.

Activities of Regional Pools

During the 2017-2018 dairy year, P5 technical working groups addressed challenges related to the reconciliation of the P5 growth reserve. The growth reserve is used to encourage processing in certain classes. Beginning in the 2016-2017 dairy year, the CDC provided technical expertise to the P5 on a more effective way to balance the sum of milk required for this activity. The CDC also assisted signatories to the P5 agreement to complete a mandatory review, conducted every five years. The review was successful and no changes were made to the agreement.

Harmonization of policies and activities amongst P5 and WMP provinces continues to progress. In February 2018, the P5 and WMP adjusted milk components prices for all classes as per the result of the agreed national pricing formula (50% cost of production + 50% Consumer Price Index).

In the 2017-2018 dairy year, all provinces continued to work together to implement elements of the National Ingredient Strategy.

Milk deliveries (million kg of butterfat)

	P5	WMP
Fluid milk	75.37	36.10
Industrial milk	208.44	58.04
Total	**283.81**	**94.14**

MARKET DEVELOPMENT

Class 3(d)

Class 3(d) was created to encourage restaurants to use Mozzarella on fresh pizzas. In 2017-2018, 1,237 new restaurants joined the program for a total of 11,278 restaurants. Consequently, the total amount of Mozzarella used in the program for this dairy year amounted to 49 million kg compared to 48 million kg in 2016-2017.

Dairy Marketing Program

The CDC is committed to promoting growth and innovation in the manufacture and use of dairy products and components. The Dairy Marketing Program facilitates access to the technical support and expertise required to develop innovative dairy and food products and to bring them to market, partnering with universities and industry associations. Through the MILKingredients.ca Web site, dairy processors and further processors can apply for programs, and find up-to-date information on milk prices and dairy ingredients.

In 2017-2018, the CDC participated in the Restaurants Canada trade show to promote the Dairy Innovation Program, the Matching Investment Fund, the Special Milk Class Permit Program as well as other services the CDC offers to dairy processors and food manufacturers.

Dairy Innovation Program

The Dairy Innovation Program (DIP) encourages the manufacture of new and innovative products on the domestic market. It allows for the addition of specific volumes of milk to provincial quotas to ensure that the milk supply needed to produce innovative products is available to successful applicants.

During the 2017-2018 dairy year, dairy processing companies across Canada used 11.3 million litres of milk under the DIP compared to 12.6 million litres in 2016-2017. Quota previously allotted to the manufacture of products approved under Domestic Dairy Product Innovation Program (DDPIP) is allotted to the provinces upon expiry of DDPIP contracts. DDPIP was replaced with the DIP program in 2013.

This year, five applications were received under the DIP. As of July 31, 2018, one application was approved by the selection committee who met in April 2018. Three applications were rejected and one is still under review.

Matching Investment Fund

The Matching Investment Fund (MIF) is designed to help eligible companies and Food Technology Centres with product development initiatives that help stimulate demand for Canadian dairy products and ingredients. During the 2017-2018 dairy year, the MIF received seven applications, and as of July 31, 2018, three applications were approved. Approved projects include activities such as consultation services, recipe formulation, product testing, retrofitting of equipment and technology transfer.

Exports

During the 2017-2018 dairy year, Canada did not export skim milk powder in Class 5(d). Due to higher than anticipated stock levels, Canada exported approximately 50 tonnes of butter. The CDC also issued Class 5(d) permits to Canadian exporters for 1,963 tonnes of cheese in addition to the cheese exported under the Dairy Export Program.

Dairy Export Program

The Dairy Export Program (DEP) aims to support the export of up to 3,000 tonnes of cheese per dairy year as well as the export of other dairy products. Applicants must be federally licenced plants or exporters and all exports are within Canada's trade commitments. In 2017-2018, 2,698 tonnes of cheese and 762,624 litres of milk were exported under the DEP.

Milk Access for Growth Program

The Milk Access for Growth (MAG) program guarantees a sufficient supply of milk to encourage new investments in the dairy sector to grow the overall Canadian demand for milk and milk products. These investments include expansion and/or establishment of plants by Canadian dairy processors, further processors of food or any other products, or Canadian or foreign investors seeking to establish a business in Canada. The program may be used for new as well as existing products (dairy or other products containing dairy ingredients), with the emphasis being placed on growth. In 2017-2018, the program received two applications, which were accepted. Agreements are being finalized.

Market Development Initiative

The CDC has been actively involved in providing assistance to investors (foreign and domestic) in order to promote the development of new markets. The goal is to arrive at private investments from Canadian or foreign enterprises to grow markets both in Canada and abroad.

AUDITING

The table on page 21 explains the various audit roles of the CDC.

Most external audits cover companies participating in the Special Milk Class Permit Program (SMCPP). Risk assessment is used to identify higher-risk companies among program participants. In conjunction with SMCPP audits, the CDC also audits companies participating in the Import for Re-export Program

Export limits and products exported

	Subsidy limit (million kg)	Quantity of products exported (million kg)	Subsidy limit (million $)	Subsidy value on exported products (million $)
Butter	**0.905**	0.05	11.025	0.1824
Cheese	**6.041**	4.661	16.228	9.753
Skim milk powder	**18.147**	0	31.149	0
Other dairy products	**14.189**	0.762	22.505	0.0356
Incorporated products	**n/a**	0	20.276	0

Type of audit	Auditee	Purpose of audit
Revenue Sharing	Provincial boards	Verify completeness of pooled revenues from all 10 provinces
Milk Utilization	Processors	Verify accuracy and completeness of milk components reported in utilization classes and related programs (i.e. School Milk Program, Dairy Innovation Program, etc.) in 6 provinces (NL, PE, NB, NS, MB, SK)
IREP	IREP Participants	Verify compliance with program requirements on behalf of Global Affairs Canada (GAC)
Milk Class 3(d)	Distributors and Restaurants using Mozzarella on fresh pizza	Verify compliance with class requirements
Class 4(m)	Class 4(m) participants	Verify compliance with class requirements
Special Milk Class Permit Program (Class 5(a), (b), (c))	Distributors and Further Processors	Verify compliance with program requirements
Class 7	Class 7 participants	Verify compliance with class requirements

(IREP) which is administered by Global Affairs Canada (GAC). Audit activities also included participants in the 4(m) program, which was in place for skim milk and liquid MPC until January 2017. During the 2017-2018 dairy year, a total of 88 audits were conducted of SMCPP, 4(m), and IREP participants, compared to 51 audits the previous year. The increase was mainly due to additional audit focus in the 4(m) program area.

Audits for Milk Class 3(d) (Mozzarella for fresh pizzas) were performed and covered selected independent pizzerias and distributors. During the 2017-2018 dairy year, a total of 63 pizzeria restaurants and distributors were audited, which was higher than the projected target. Targets were reduced based on audit results of prior years, as this was considered a low-risk area.

Audits of Class 7 activities are underway in collaboration with provincial auditors. A total of 30 joint audits were conducted during 2017-2018, which is lower than the projected target, mainly due to system updates required for the provinces. For joint audits performed, the CDC contributed valuable expertise with support for harmonization of audit practices, and overall audit results were positive in this regard. Class 7 audits are continuing into the 2018-2019 dairy year.

The CDC also performs the milk plant utilization audits in Manitoba, Newfoundland and Labrador, Nova Scotia, Prince Edward Island, New Brunswick, and Saskatchewan (29 plants in 6 provinces) on a cost-recovery basis. Utilization audits cover procedures specific to each class as well as other CDC and provincial programs (i.e. DIP, School Milk Program, etc.).

As of July 31, 2018, overall routine Special Class audit recoveries totalled $203,742. These funds were returned to producers. Total recoveries have decreased due to improved understanding of program requirements by long-term participants, as compared to previous years, as well as the increased focus on Utilization and Class 7 audits.

National Milk Utilization Audit Standards and Harmonization of Practices

In parallel with its auditing work, the CDC provides audit expertise and promotes the harmonization of procedures through the National Milk Audit Advisory Committee. This committee brings together CDC auditors, provincial auditors, as well as representatives from milk marketing boards and the dairy processing industry twice a year. Meetings were held in September and December of 2017.

The CDC continued to play a coordinating and training role relative to the implementation of CMSMC policy decisions having audit implications. It also monitors key industry changes and trends and shares information with auditors of other jurisdictions to continually improve audit outcomes for all provinces.

INDUSTRY SUPPORT

Canadian Milk Supply Management Committee

The Canadian Milk Supply Management Committee (CMSMC) is a national body for policy development and discussions in the sectors of dairy production and processing. It includes milk marketing boards and government representatives from all provinces and non-voting representatives from national consumer, processor and producer organizations. As chair of the CMSMC, the CDC provides ongoing leadership, advice, and analysis to the Canadian dairy industry, in close co-operation with national and provincial stakeholders.

Secretariat, IT and Translation Services

The CDC coordinated close to 115 meetings, webinars and conference calls and translated approximately 575 documents in support of the regional pools, the CMSMC, and several working groups and national committees.

Workforce Development Initiative

The CDC supports the establishment of a highly skilled, diverse workforce that is well adapted to meet the current and future needs of the dairy producing and processing sectors. Following an inclusive consultation process with dairy industry and academia partners, the CDC launched the Workforce Development Initiative (WDI) in April 2018. This new comprehensive initiative goes beyond the previous Scholarship Program by adding elements such as post-secondary education and continuous training. The WDI encourages productivity, competitiveness and innovation by supporting the education and recruitment of a dynamic workforce. It is composed of four funding programs:

1. Scholarship Program: scholarships for graduate students in fields related to the dairy industry
2. Career Promotion Program: promotion of careers in the dairy industry
3. Education Program: creation of government-certified, full-time education programs in order to train qualified staff to work in dairy plants
4. Continuing Education Program: opportunities for continuing education of current dairy plant and farm staff

A total of $5 million is available for a 3-year period (subject to availability of funds).

Dairy Research Cluster

In 2010, the CDC partnered with Agriculture and Agri-Food Canada (AAFC), the Natural Sciences and Engineering Research Council of Canada and Dairy Farmers of Canada (DFC) to fund a Dairy Research Cluster as part of AAFC's Growing Forward initiative.

The second Dairy Research Cluster, part of AAFC's Growing Forward 2, was launched in 2013 and was intended to build on the results and outcomes from the first Cluster. It focused on three research themes: sustainable milk production, human nutrition and health, and dairy genetics and genomics. DFC invested $5.3 million in addition to the $13.75 million announced by AAFC. The Canadian Dairy Network invested $669,000 and the CDC provided $750,000, bringing the total to $20.5 million in funding to address the dairy sector's research priorities from 2013 to 2018. There were 27 research activities financed through this program involving more than 100 scientists and 65 graduate students working in 15 Canadian universities and eight federal research centres. For more information on the research priorities, the activities financed and the research highlights from 2017-2018, visit www.DairyResearch.ca.

Performance and Goals

ACHIEVEMENTS FOR 2017-2018

The CDC has achieved most of its objectives. Changing industry priorities and market forces have hindered the achievement of some of them.

Growing Markets

5-year objective	Performance measure for 2017-2018	Target	Results	% complete
Investments and innovation have led to continuous market growth	Number of litres used in the Milk Access for Growth program (MAG)	160 million litres	Approved projects have not begun production. New facilities are expected to start production in 2019 and use about 21 million litres that year.	0
	Market growth rate correlated to CDC activities	4% (cumulative)	MAG projects are expected to create growth starting in 2019.	0
	Number of innovative dairy products introduced through the Dairy Innovation Program (DIP)	10 (cumulative)	As of July 31, 2018, one application was approved by the selection committee who met in April 2018.	50

The Role of the CDC in the Industry

5-year objective	Performance measure for 2017-2018	Target	Results	% complete
The CDC is valued as a neutral facilitator and key contributor in the dairy industry	% CDC-led recommendations to industry committees that are accepted	85%	Four recommendations were made and accepted: 1. Growth allowance 2. Reinstate continuous quota 3. Target butter stocks 4. Exceptional circumstances: Classes 1-4 price changes.	100
	Number of invitations to speak/facilitate/train at non-CDC meetings (excluding reports to provincial boards' annual general meetings)	20 per year	The CDC received 20 invitations.	100

A Well-Administered, Responsive and Well-Understood Supply Management System

5-year objective	Performance measure for 2017-2018	Target	Results	% complete
Ensure the respect of federal-provincial and international agreements	Number of audits	91 audits of Special Milk Class Permit Program, Import for Re-Export Program (IREP) and 4(m) participants	88 audits of Special Milk Class Permit Program, Import for Re-Export Program (IREP) and 4(m) participants	97
		55 audits of Class 3(d) participants	63 audits of Class 3(d) participants	100
		50 audits of Class 7 participants	30 audits of Class 7 participants	60
		2 Internal Audits	2 Internal Audits	100
		30 Milk Plant Utilization Audits	30 Milk Plant Utilization Audits	100
	Total producer revenue evolves with market growth	1% annual increase	2% increase	100
	Market supply meets demand through accurate quota calculation and improvement of market analysis and forecasts	Quota is between 99% and 101% of demand	99.32%	100
	Quota allocation and money transfers are performed within the service standards established by the Canadian Milk Supply Management Committee	100% of the time	Quota allocation and money transfers performed on time	100
	Registration to online training modules	15 per year	23 registrations	100

A Well-Managed CDC

5-year objective	Performance measure for 2017-2018	Target	Results	% complete
The CDC is organized and resourced to support the dairy industry into the future	Level of staff satisfaction as measured by an annual survey	Satisfaction rate of 90% or more	Satisfaction rate reached 98%	100
	Number of tools or policies developed internally and adapted to better support the industry	4 per year	Integration of pooling calculations into Euclid's automated calculation system New demand forecasting model Monthly quota management Review of the Audit Manual (ongoing)	100

PERFORMANCE GOALS FOR 2018-2019

The CDC's performance objectives for 2018-2019 are based on the strategic themes and 5-year goals identified in its Corporate Plan.

Theme: Investment, innovation and growth in the Canadian dairy sector
5-year goal – Investments and innovation have led to continuous market growth in the dairy industry.

Performance indicators	5-year Target
Number of litres of milk used in the Milk Access for Growth Program (MAG)	160 million litres
Market growth rate	4% (cumulative)
Number of innovative dairy products introduced through the Dairy Innovation Program	10 (cumulative)

Strategy	2018-2019 objective
Provide support and funding for market development	Market Development Strategy implemented

Theme: The role of the CDC in the industry
5-year goal – The CDC is valued as an effective facilitator and key contributor in the dairy industry

Performance indicators	5-year Target
% CDC-led recommendations to industry committees that are accepted	85%
Number of invitations to speak/facilitate/train at non-CDC (excluding reports to provincial boards' AGMs)	20
Number of registrations to CDC online training modules	15

Strategy	2018-2019 objective
Improve communications with the industry	Stakeholders' engagement is enhanced

Theme: Administration of the milk supply management system

5-year goal – A well-administered, responsive and well-understood supply management system

Performance indicators	5-year Target
Time from receipt of pooling data to quota allocation and money transfers	8 days maximum
Number of audits	20 audits of Class 3(d) 40 audits of Special Milk Class Permit Program participants 42 audits of class 7
Total producer revenues increase driven by growth	1%
Quota as a percentage of demand	Quota is between 99% and 101% of demand

Strategy	2018-2019 objective
Promote more market-responsive management of milk supply	The new quota management system is in place
Ensure the respect of federal-provincial and international agreements	Initiate the modernization of the Comprehensive Agreement on Pooling of Milk Revenue and the National Milk Marketing Plan to reflect changes to the industry Follow NAFTA negotiations
Ensure that efficient producers receive fair returns	Stable or increasing producer revenues through market growth Timely and accurate revenue pooling calculations
Ensure Canadian production meets demand	Timely and sufficient supply of dairy products in the Canadian market Timely and accurate allocation of quota to meet demand

Theme: A well-managed CDC

5-year goal – The CDC is organized and resourced to support the dairy industry into the future.

Performance indicators	5-year Target
Level of staff satisfaction as measured by an annual survey	90% or more
Number of tools or policies developed and adapted to better support the industry	4

Strategy	2018-2019 objective
Ensure a productive and engaged workforce	Improved employee onboarding and retention Improved internal collaboration among teams
Adapt the IT systems to the industry's environment	Implement the use of common communication platforms with industry Improve Web services Continue adapting IT systems to NIS
Implement new or updated government policies	New government policies are assessed

Financial Report

MANAGEMENT DISCUSSION AND ANALYSIS

The following discussion and analysis of the operating results and financial position of the Canadian Dairy Commission (CDC) for the year ending July 31, 2018, should be read in conjunction with the financial statements of the CDC enclosed and the annual report.

Selected Key Results of Operations

Domestic activities

The CDC purchases and sells butter and skim milk powder (SMP) to regulate the supply of dairy products in the domestic market throughout the year. In the 2017-2018 dairy year, total revenues from domestic sales decreased by $15.9 million, or 5%, compared to the previous year. This is mainly due to lower sales of imported butter, which was only partly offset by higher sales of domestic butter. This also contributed to the net decrease of gross profit on domestic sales, although the impact on domestic gross profit resulting from fewer sales of imported butter was partly offset by increased margins from the sales of skim milk powder in the domestic market.

The CDC purchases butter in bulk under Plan A through the Domestic Seasonality Programs which is resold to processors when domestic seasonal demand increases. Because of strong production this year, the CDC purchased 3,717 tonnes of Plan A butter and sold 464 tonnes on the domestic market, which resulted in revenues of $3.7 million. There were no activities under Plan A last year.

The CDC also purchases Plan B butter through the Domestic Seasonality Programs from processors who must repurchase it within a predetermined period. This year, the CDC sold 29,429 tonnes of Plan B butter compared to 18,695 tonnes last year, representing an increase in revenues of $86.7 million. This increase is the result of higher Plan B inventory levels throughout the year compared to last year, resulting in a higher volume of repurchases from processors.

The CDC continues to import 3,274 tonnes of butter as part of Canada's commitments under the World Trade Organization (WTO) Agreement on Agriculture. Unlike last year, the CDC did not purchase butter, nor butterfat in the form of cream, under supplementary import permits given domestic production was sufficient to meet demand in the further processing industry. As a result, imported butter/butterfat sales decreased to 24.8 million compared to the previous year. These products are purchased by the CDC at prevailing world prices and they are mostly directed to the further processing industry through butter manufacturers.

Domestic activities

	For the year ended July 31		
(in thousands)	2018	2017	$ change
Domestic sales revenue	$305,942	$321,804	$(15,862)
Cost of goods sold - domestic	$291,887	$299,858	$(7,971)
Transport and carrying charges	$6,138	$7,412	$(1,274)
Finance costs	$985	$438	$547
Gross profit on domestic sales	**$6,932**	**$14,096**	**$(7,164)**

Skim milk powder (SMP) sold to animal feed users amounted to 25,484 tonnes in 2017-2018, which is 638 tonnes more than the previous year. Similarly, revenues increased by $2.7 million compared to the previous year. The gross profit generated from this activity increased by $6.4 million mainly due to a higher average sale price, and lower transport and carrying charges.

Export activities

Export sales revenues in 2017-2018 were significantly lower than in the previous year given the CDC no longer sells skim milk powder on the export market. In the current year, export sales revenue result exclusively from the export of a small quantity of butter, while last year they resulted from the export of skim milk powder.

Transport, carrying, and finance costs

Transport, carrying, and finance costs are mostly comprised of transportation expenses, interest expenses on loans, handling and storage charges, and insurance costs. Transport and carrying charges for domestic activities in 2017-2018 decreased by $1.3 million compared to those of 2016-2017 due to lower inventory levels of skim milk powder throughout the year; although the impact is partly offset by increased handling and storage charges associated with higher butter inventory levels throughout the year. On the export side, the costs decreased by $2.2 million in 2017-2018 mainly because the CDC no longer sells skim milk powder on the export market.

Total finance costs for both domestic and export activities increased by $0.5 million compared to the previous year. This increase is due to higher inventory levels of butter during the year, and a slight increase in borrowing rates.

After several years of low interest rates, they are expected to continue to increase slightly in the 2018-2019 dairy year.

Export Activities

For the year ended July 31

(in thousands)	2018	2017	$ change
Export sales revenue	$278	$38,528	$(38,250)
Cost of goods sold - exports	$229	$37,932	$(37,703)
Transport and carrying charges	$3	$2,154	$(2,151)
Finance costs	$-	$12	$(12)
Gross profit (loss) on export sales	**$46**	**$(1,570)**	**$1,616**

Other income

Funding from milk pools represents the revenues obtained from producers and the marketplace to finance a portion of the CDC's administrative expenses, the cost of the annual production study, the costs related to the Storage Assistance Program for Cheese (SAPC), the carrying charges associated with the CDC butter stocks, and any recoverable industry committee expenses. This funding was increased in 2017-2018 to cover increases in administrative expenses. Increased funding also resulted from growth in total industrial milk production which impacts the amount collected from the marketplace through the milk pools.

Parliamentary appropriations are used to partially fund the CDC's administrative expenses. The remainder of the CDC's administrative expenses are funded by dairy producers, commercial operations, and the market place. Funding from the Government of Canada is recognized in the Statement of Operations and Comprehensive Income (loss) based on eligible government-funded administrative expenses incurred.

Audit services revenues relate to the milk plant utilization audits performed by the CDC in 6 provinces on a cost-recovery basis.

Other Income

(in thousands)	2018	2017	$ change
	For the year ended July 31		
Funding from milk pools	$9,069	$7,039	$2,030
Funding from the Government of Canada	$3,881	$3,795	$86
Audit services	$168	$186	$(18)
Total Other Income	**$13,118**	**$11,020**	**$2,098**

Operating and Administrative Expenses

Operating Expenses

"*Industry initiatives*" includes expenses relating to various CDC programs such as the Matching Investment Fund and the Dairy Research Cluster. Funding for these programs increased by $0.3 million in 2017-2018 mostly because this year's expenses include the final payment of $0.25 million for the Dairy Research Cluster.

"*Cost of production study*" includes expenses relating to the annual survey on costs of production. The CDC uses the survey's results when it sets support prices. The study's budget increased slightly in 2017-2018 to reflect inflation.

"*Other charges*" is comprised of charges paid under the Storage Assistance Program for Cheese (SAPC), credits from the CDC's contribution to the cost of the production study, charges incurred by the CDC on behalf of the milk pools, and bank charges from the milk pool account. The decrease in 2017-2018 is mainly the result of lower SAPC payments compared to the previous year, which was partly offset by an increase in bank charges.

Administrative Expenses

The 2017-2018 administrative budget was $9.1 million and the actual administrative expenses for the year totalled $8.8 million. Expenses in 2017-2018 are higher than the previous year mainly as a result of hiring additional staff to address industry needs, and an increase in building rental costs. Salaries and employee benefits of $6.6 million make up the bulk of administrative expenses. The remaining significant expenses relate to rent, travel and administrative support.

Distribution to provincial boards and agencies

The distribution to provincial boards and agencies represents a refund of surplus generated from the Domestic Seasonality and Surplus Removal Programs. As milk producers are responsible to finance these programs,

Operating and Administrative Expenses

(in thousands)	2018	2017	$ change
	For the year ended July 31		
Operating expenses			
Industry initiatives	$735	$399	$336
Cost of Production study	$838	$825	$13
Other charges	$176	$345	$(169)
Total operating expenses	$1,749	$1,569	$180
Administrative expenses			
Salaries and employee benefits	$6,608	$6,085	$523
Other administrative expenses	$2,216	$2,112	$104
Total administrative expenses	$8,824	$8,197	$627
Total operating and administrative expenses	**$10,573**	**$9,766**	**$807**

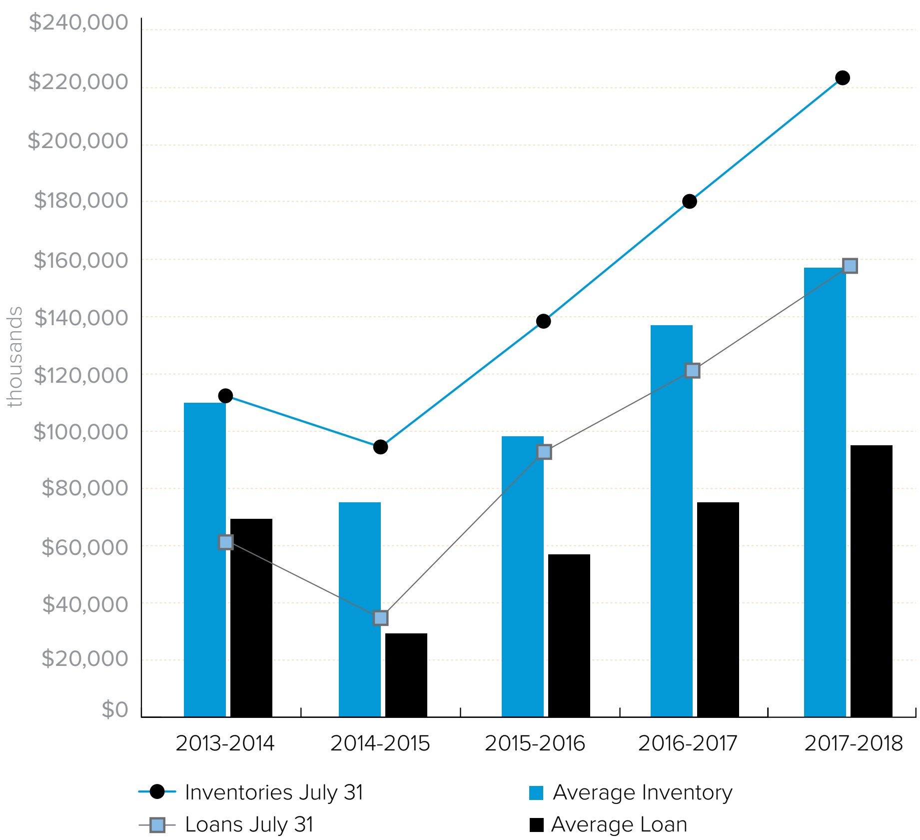
any surpluses are reimbursed to provincial milk marketing boards and agencies. The 2017-2018 refund amounted to $10.9 million.

Inventories and loans

CDC butter stocks at the end of the year totalled 25,901 tonnes, which represents an increase of 9,151 tonnes compared to last year. The needed increase results from measures taken to stimulate milk production in the industry and satisfy demand for butter and butterfat.

Skim milk powder (SMP) stocks at the end of the year totalled approximately 12,706 tonnes, which represents a decrease of approximately 25,484 tonnes since July 2017. This is the result of the CDC no longer purchasing SMP under the Surplus Removal and Domestic Seasonality Programs as of February 1, 2017, following the implementation of some elements of the National Ingredient Strategy. Skim milk powder stocks will be depleted in the next dairy year through sales in the animal feed market.

Inventories and Loans



As butter stocks have a higher monetary value than SMP, the increase in butter stocks value was significantly higher than the decrease in SMP stocks value, resulting in a $45.1 million net increase of the overall value of inventory in 2017-2018.

Given the inventories are financed by the loans from the Government of Canada, there is usually a direct correlation between variations in the value of inventory and the balance of these outstanding loans. As such, the higher inventory value in the current year resulted in higher loan requirements, increasing the loans from the Government of Canada to $152.9 million by the end of the year, compared to $118.7 million at the end of the previous year. The average inventory value for 2017-2018 is up 12.8% compared to the previous year, resulting in an increase in the average loan value.

The CDC, in consultation with the Minister of Finance, has increased its loan limit to $225 million for 2017-2018. This increase in limit was required to maintain its capacity to respond to unforeseen circumstances brought on by changing market conditions.

Risk management

As is the case for any business enterprises, the CDC is subject to risks in its ongoing operations. The CDC has identified the key risk factors to which it is exposed and has established policies and procedures to manage and mitigate these risks.

The CDC has prepared a Corporate Risk Profile which is reviewed and updated at least once per year by management. It is updated during the year as needed with the latest review completed in January 2018. It identifies the key risks associated with CDC business and activities. It also evaluates the probability and potential impact of risk occurrences and defines mitigation measures to avoid or reduce risk. The organization's annual planning process is aligned with the Profile to ensure that higher-risk program areas and activities receive special consideration. The Board and the Senior Management Team (SMT) share the responsibility for risk management. Each plays an integral role in the risk management process at the CDC. The Board ensures that management identifies, monitors, and manages the CDC's corporate risks. It is responsible for providing a clear direction on risk tolerance and approving the Corporate Risk Profile. The Board is kept apprised of any changes to the risk profile through quarterly briefings. At least every quarter, the CDC Audit Committee monitors these risks as well as the progress in the implementation of the various mitigation measures. The SMT is responsible for assessing the CDC's key risk areas and ensuring that appropriate controls and other mitigation strategies are carried out to effectively manage these risks. This includes supporting risk awareness and communication throughout the organization.

Credit risk is the exposure to financial loss due to a customer failing to meet their financial obligations to the CDC. The CDC manages this risk by selling product on a "payment first" basis, securing bank guarantees and obtaining letters of credit. Other strategies include carrying out business with creditworthy customers only.

Foreign currency risk is the potential for financial loss due to unfavourable changes in foreign currency exchange rates. The CDC's foreign exchange risk management includes the use of foreign currency forward contracts to fix the exchange rates on certain sales and purchases in foreign currencies (U.S. dollars). The CDC does not use foreign exchange forward contracts or any free-standing derivative financial instruments for trading or speculative purposes. The CDC only enters into these contracts with Canadian chartered banks.

Market risk is the most difficult to manage due to its unpredictability. The operations of the CDC are affected by many external factors such as world market conditions, trade related developments on agriculture, domestic market trends, and fluctuations in supply and demand. The CDC addresses these risks by instituting sound management practices, hiring and maintaining a competent and skillful workforce, and staying abreast of any market or political development that may affect its operations. Because the CDC deals with supply-managed products such as SMP and butter, the export activity is a relatively small percentage of its overall revenues. Nonetheless, the CDC manages the volatility of world markets by strategically selling its products, mostly by tender, to reliable exporters who seek value-added products, ensuring best returns from its commercial operations. As far as butter imports are concerned, the CDC applies the same prudent rules by buying its products by tenders or competitive offers from reliable importers.

Future accounting changes

The *International Accounting Standards Board* has several projects underway, some of which may affect International Financial Reporting Standards (IFRS) applicable to the CDC. Management will continue to monitor all proposed and ongoing projects and consider whether any changes are expected to impact the CDC's reporting of financial information. A more detailed discussion of future financial reporting standard changes can be found in Note 3 of the financial statements.

Looking to the future

Demand for butterfat continues to grow, albeit at a slower pace than in the two previous years. Dairy farmers increased milk production to meet this demand, creating a situation of slight over production in the spring and summer of 2018. In response, marketing boards, in collaboration with the CDC, implemented measures to slow down production. The challenge is going to be to provide a soft transition between the past need to quickly ramp up production and the current situation, which requires a slower growth in milk production. Precise production and demand forecasts will be very important, as well as stock management. The CDC has developed forecasting models for the coming year.

To respond to increased demand for its services on the part of the industry, the CDC added 9 positions in the last two years, mostly in the Audit and Evaluation Division. These additions were based on an evaluation of the future needs of the industry. All the additional resources are fully used as industry demands materialize and audits increase in complexity due to new manufacturing processes. In the coming year, the CDC will re-evaluate its future HR needs and some additional training may be necessary.

On the international trade policy front, the CDC is following the implementation of the Comprehensive Economic and Trade Agreement between Canada and the European Union as well as the implementation of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership because they will both have an impact on the imports of dairy products into Canada.

The CDC is also following developments regarding the proposed United States-Mexico-Canada Agreement (USMCA) and its potential impact on the dairy industry.

Management Responsibility for Financial Statements

The financial statements of the Canadian Dairy Commission and all information in this Annual Report are the responsibility of management. Those statements have been prepared in accordance with International Financial Reporting Standards, using management's best estimates and judgments where appropriate. Financial information presented elsewhere in the Annual Report is consistent with the statements provided.

In discharging its responsibility for financial reporting, management maintains and relies on financial and management control systems and practices designed to provide reasonable assurance that transactions are authorized, assets are safeguarded, and proper records are maintained. These controls and practices ensure the orderly conduct of business, the accuracy of accounting records, the timely preparation of reliable financial information and the adherence to CDC policies and statutory requirements. This process includes the communication and ongoing practice of the CDC's Code of Ethics.

The Audit Committee of the Canadian Dairy Commission, made up of the commissioners, oversees management's responsibilities for maintaining adequate control systems and the quality of financial reporting. The CDC's internal and external auditors have free access to the Audit Committee to discuss the results of their work and to express their concerns and opinions.

The financial statements of the CDC have been audited by the Auditor General of Canada, the independent auditor for the Government of Canada.

Serge Riendeau, CEO

Chantal Laframboise, Director
Finance and Administration

Ottawa, Canada
October 4, 2018

Office of the Auditor General of Canada

Bureau du vérificateur général du Canada

Independent Auditor's Report

To the Minister of Agriculture and Agri-Food

Report on the Financial Statements

I have audited the accompanying financial statements of the Canadian Dairy Commission, which comprise the statement of financial position as at 31 July 2018, and the statement of operations and comprehensive income (loss), statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the financial statements present fairly, in all material respects, the financial position of the Canadian Dairy Commission as at 31 July 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on Other Legal and Regulatory Requirements

As required by the *Financial Administration Act*, I report that, in my opinion, the accounting principles in International Financial Reporting Standards have been applied on a basis consistent with that of the preceding year.

Further, in my opinion, the transactions of the Canadian Dairy Commission that have come to my notice during my audit of the financial statements have, in all significant respects, been in accordance with Part X of the *Financial Administration Act* and regulations, the *Canadian Dairy Commission Act* and regulations, the by-laws of the Canadian Dairy Commission, and the directive issued pursuant to section 89 of the *Financial Administration Act*.

MK Kerrigan

Mary Katie Kerrigan, CPA, CA
Principal
for the Auditor General of Canada

4 October 2018
Ottawa, Canada

Canadian Dairy Commission
Statement of Financial Position

(in thousands of Canadian dollars)

	As at	
	July 31, 2018	**July 31, 2017**
Assets		
Current		
Cash	$ 6,925	$ 205
Trade and other receivables		
Trade receivables	467	772
Advance to provincial milk boards and agencies	7,582	5,989
Milk pools	1,985	1,740
Inventory (Note 4)	221,970	176,905
	238,929	185,611
Non-Current		
Equipment	120	53
Intangible asset	170	196
	$ 239,219	$ 185,860
Liabilities		
Current		
Bank overdraft (Note 5)	$ 7,582	$ 5,989
Trade and other payables		
Trade payables	15,558	12,881
Distribution to provincial milk boards and agencies	10,900	8,400
Other liabilities (Note 6)	17,736	3,908
Loans from the Government of Canada (Note 7)	152,852	118,714
	204,628	149,892
Equity		
Retained earnings	34,591	35,968
	$ 239,219	$ 185,860

Commitments (Note 13)

The accompanying notes are an integral part of these financial statements.

These financial statements were approved and authorized for issue on October 4, 2018.

Serge Riendeau
Chief Executive Officer

Alistair Johnston
Chairman

Chantal Laframboise
Director, Finance and Administration

Canadian Dairy Commission
Statement of Operations and Comprehensive Income (Loss)

(in thousands of Canadian dollars)

	For the year ended July 31, 2018	For the year ended July 31, 2017
Sales and cost of sales		
Domestic sales revenue	$ 305,942	$ 321,804
Cost of goods sold - domestic	291,887	299,858
Transport and carrying charges	6,138	7,412
Finance costs	985	438
Gross profit on domestic sales	6,932	14,096
Export sales revenue	278	38,528
Cost of goods sold - exports	229	37,932
Transport and carrying charges	3	2,154
Finance costs	-	12
Gross profit (loss) on export sales	46	(1,570)
Total gross profit	6,978	12,526
Other income		
Funding from milk pools	9,069	7,039
Funding from the Government of Canada (Note 10)	3,881	3,795
Audit services	168	186
	13,118	11,020
Total gross profit and other income	**20,096**	**23,546**
Operating expenses		
Industry initiatives	735	399
Cost of Production study	838	825
Other charges	176	345
	1,749	1,569
Administrative expenses		
Salaries and employee benefits (Note 11)	6,608	6,085
Other administrative expenses	2,216	2,112
	8,824	8,197
Total operating and administrative expenses	**10,573**	**9,766**
Profit before distribution to provincial milk boards and agencies	**9,523**	**13,780**
Distribution to provincial milk boards and agencies	10,900	8,400
Total comprehensive income (loss)	**$ (1,377)**	**$ 5,380**

The accompanying notes are an integral part of these financial statements.

Canadian Dairy Commission
Statement of Changes in Equity

(in thousands of Canadian dollars)

	For the year ended July 31, 2018	For the year ended July 31, 2017
Retained earnings, beginning of the year	$ 35,968	$ 30,588
Total comprehensive income (loss) for the year	(1,377)	5,380
Retained earnings, end of the year	$ 34,591	$ 35,968

The accompanying notes are an integral part of these financial statements.

Canadian Dairy Commission
Statement of Cash Flows

(in thousands of Canadian dollars)

	For the year ended July 31, 2018	For the year ended July 31, 2017
Cash flows used in operating activities		
Cash receipts from sales of goods	$ 320,253	$ 364,892
Cash paid to suppliers and others	(351,211)	(393,087)
Cash receipts from provincial milk boards and agencies (pooling)	7,231	4,423
Cash paid to provincial milk boards and agencies	(8,400)	(5,944)
Cash receipts from the Government of Canada	3,881	3,795
Interest paid on loans	(765)	(402)
Net cash flows used in operating activities	(29,011)	(26,323)
Cash flows from financing activities		
New loans from the Government of Canada	297,330	266,045
Loan repayments to the Government of Canada	(263,192)	(241,523)
Net cash flows from financing activities	34,138	24,522
Net decrease (increase) in net bank overdraft	5,127	(1,801)
Net bank overdraft at beginning of year	(5,784)	(3,983)
Net bank overdraft at end of year	$ (657)	$ (5,784)
Components:		
Cash	$ 6,925	$ 205
Bank overdraft	(7,582)	(5,989)
Net bank overdraft	$ (657)	$ (5,784)

The accompanying notes are an integral part of these financial statements.

1. Authority and objectives

The Canadian Dairy Commission (CDC) was established in 1966 through the *Canadian Dairy Commission Act*. It is a federal Crown corporation named in Part I, Schedule III and Schedule IV to the *Financial Administration Act* and is not subject to the provisions of the *Income Tax Act*. It is an agent of Her Majesty the Queen in right of Canada and reports to Parliament through the Minister of Agriculture and Agri-Food.

The objectives of the CDC are to provide efficient producers of milk with the opportunity to obtain a fair return for their labour and investment, and to provide consumers with a continuous and adequate supply of dairy products. To achieve its objectives, the CDC works closely with the Canadian Milk Supply Management Committee (CMSMC), which it chairs, as well as with provincial governments and provincial milk marketing boards and agencies. This collaboration is framed by federal-provincial agreements.

The CDC is partly funded by parliamentary appropriations. This is supplemented by funding from milk producers and the market, as well as by the CDC's own commercial operations.

Directive on Travel, Hospitality, Conference and Event Expenditures

In July 2015, the CDC was issued a directive (P.C. 2015-1104) pursuant to section 89 of the *Financial Administration Act* to align its travel, hospitality, conference and event expenditure policies, guidelines and practices with Treasury Board policies, directives and related instruments on travel, hospitality, conference and event expenditures in a manner that is consistent with its legal obligations, and to report on the implementation of this directive in the CDC's next Corporate Plan. As at July 31, 2018, the CDC continues to meet the requirements of this directive.

2. Basis of preparation

Statement of compliance

These financial statements are prepared in accordance with International Financial Reporting Standards (IFRS).

The financial statements were approved and authorized for issue by the CDC Board effective October 4, 2018.

Basis of presentation

The financial statements are prepared on a historical cost basis, as set out in the accounting policies below, except as permitted by IFRS and otherwise indicated within these notes.

Reporting period

The CDC reports on a dairy year basis which starts August 1 and ends July 31.

Use of judgement, estimates and assumptions

The preparation of financial statements in accordance with IFRS requires management to exercise judgment and make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the year. Areas where management has exercised judgment and made significant use of estimates and assumptions are discussed below.

Plan B Inventory

Under section 9(1) of the *Canadian Dairy Commission Act*, the CDC operates domestic seasonality programs, which includes the purchase of Plan B inventory (butter and skim milk powder) from manufacturers who are contractually obligated to repurchase the inventory at the prevailing support prices within the next dairy year.

Although the CDC customarily honours manufacturers' requests for repurchase, the CDC has determined that the significant risks and rewards of ownership of the asset are transferred to the CDC when the inventory is initially purchased (until it is sold), given conditions set out in the purchase agreements do not obligate the CDC to sell the inventory to the manufacturers, and the CDC bears all costs of holding the inventory, including theft and damage.

Allowance for inventory write-down

Management determines the allowance for inventory write-down through the use of assumptions. The net realizable value of inventory on hand at year end is estimated using the price of milk on the international market as well as the price of existing contracts at or around year-end. These estimates are reviewed annually and as adjustments become necessary, they are recognized in the Statement of Operations and Comprehensive Income (Loss) of the period in which they become known.

Functional and presentation currency

These financial statements are reported in Canadian dollars, which is the functional and presentation currency of the CDC.

3. Significant accounting policies

Cash

Cash includes funds on deposit at financial institutions.

Financial instruments

Financial assets and financial liabilities are initially recognized at fair value. Their subsequent measurement is dependent on their classification as described below. Their classification depends on the purpose for which the financial instruments were acquired or issued, their characteristics, and the CDC's designation of such instruments.

Classifications:

Trade and other receivables	Loans and receivables
Bank overdraft	Financial liabilities measured at amortized cost
Trade and other payables	Financial liabilities measured at amortized cost
Loans from the Government of Canada	Financial liabilities measured at amortized cost
Derivative assets and liabilities	Financial assets or liabilities measured at fair value through profit or loss (FVTPL)

Loans and receivables

Loans and receivables are reported at amortized cost using the effective interest method.

Financial liabilities measured at amortized cost

Financial liabilities measured at amortized cost are measured using the effective interest method.

Financial assets or liabilities measured at FVTPL

Financial assets or liabilities classified as FVTPL are measured at fair value at the Statement of Financial Position date with changes in fair value reported in profit or loss on the Statement of Operations and Comprehensive Income (Loss).

Transaction costs

All transaction costs in respect of financial instruments classified as loans and receivables or financial liabilities measured at amortized cost are capitalized in the period in which they are incurred. All transaction costs in respect to financial instruments classified as financial assets or liabilities measured at FVTPL are expensed in the period in which they are incurred.

Derivative financial instruments

The CDC uses derivative financial instruments such as forward contracts to counter the adverse changes in foreign exchange related to purchases and sales denominated in foreign currencies, including anticipated transactions, as well as to manage its cash balances and requirements. The CDC does not use freestanding derivative financial instruments for trading or speculative purposes.

The CDC does not designate its foreign exchange forward contracts as hedges of underlying assets, liabilities, firm commitments or anticipated transactions and accordingly, does not apply hedge accounting. As a result, foreign exchange forward contracts, when held, are reported on the Statement of Financial Position at fair value as an asset when the contracts are in a gain position and as a liability when the contracts are in a loss position. Changes in fair value are recognized as gains or losses in "Other charges" on the Statement of Operations and Comprehensive Income (Loss).

Inventory

Inventory is reported at the lower of cost, which is purchase cost, or estimated net realizable value. Cost is determined on a first-in, first-out basis except for Plan B inventories where cost is determined based on specific identification. Write-downs to net realizable value are reversed when there is a subsequent increase in the value of inventory up to a maximum of the purchase cost. The reversal is recognized as a reduction to cost of sales and an increase to the net value of inventory in the year in which it occurs.

Equipment

Equipment is reported at cost less accumulated depreciation. Cost includes all measurable expenditures directly attributable to the acquisition and installation of the equipment.

Depreciation is reported in "Other charges" on the Statement of Operations and Comprehensive Income (Loss) and begins when the equipment is available for use by the CDC. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset less estimated residual value as follows:

Generator	10 years
Computer equipment	3-5 years

Equipment is reviewed annually for indications of impairment or changes in estimated future economic benefits. If such impairments or changes exist, the carrying value is adjusted accordingly.

Intangible asset

Software

Internally developed application software is stated at cost less accumulated amortization. Cost includes all measurable expenditures directly attributable to the development of the software including employees' salaries, consultant fees and other identifiable costs specific to the project.

Amortization of the intangible asset is reported in "Other charges" on the Statement of Operations and Comprehensive Income (Loss) and is calculated on a straight-line basis over its estimated useful life of ten years.

Software is reviewed annually for indications of impairment or changes in estimated future economic benefits. If such impairments or changes exist, the carrying value is adjusted accordingly.

Distributions to provincial milk boards and agencies

Distributions to provincial milk boards and agencies represent gross profit on sales excluding imported butter. Distributions to provincial milk boards and agencies are reported as expense in the year that they are determined.

Revenues

Sales revenues

Domestic and export sales revenues are recognized when product is shipped.

When sale payments are received in advance, the recognition of revenue is deferred until the product is shipped. Such deferred revenue is reported on the Statement of Financial Position under "Other Liabilities" (see Note 6: *Other liabilities*).

Funding from milk pools

As acting agent in carrying out administrative functions of the Comprehensive Agreement on Pooling of Milk Revenues (a federal-provincial agreement), the CDC collects and redistributes producer market returns. For these services, the CDC receives from producers an annual fixed fee which offsets its cost for the administration of the agreement as well as the estimated carrying charges for normal levels of butter inventory. Furthermore, the CDC is reimbursed for other direct costs as set out in the agreement including carrying charges for surplus butter inventories.

Funding is recognized as revenue in the period as services are rendered and are accrued on a monthly basis over the fiscal year.

Funding from the Government of Canada

Funding from the Government of Canada is recognized as revenue in the period the expenses are incurred.

Audit services

Revenues from audit services are recognized in the period the services are rendered.

Cost of sales

The CDC purchases all butter and skim milk powder tendered to it at either the Canadian support price or at other prices established by the CDC, depending on the intended resale markets, except for a portion of butter imported by the CDC at international market prices. These costs are expensed under cost of sales when the goods are shipped to customers.

Foreign currency translation

All foreign currency transactions are translated into Canadian dollars at the exchange rate in effect on the transaction date.

Trade receivables and payables in foreign currencies are adjusted to reflect the exchange rate in effect as at the Statement of Financial Position date. Any ensuing exchange gains or losses are recognized in "Export sales revenue" for receivables and "Cost of goods sold – domestic" for payables on the Statement of Operations and Comprehensive Income (Loss).

Most sales and purchases in foreign currencies have corresponding foreign exchange forward contracts (see "Derivative financial instruments" above and Note 12: *Financial Instruments – Currency risk*).

Employee benefits

Pension benefits

Substantially all of the employees of the CDC are covered by the public service pension plan (the "Plan"), a contributory defined benefit plan established through legislation and sponsored by the Government of Canada. Contributions are required by both the employees and the CDC to cover current service cost. Pursuant to legislation currently in place, the CDC has no legal or constructive obligation to pay further contributions with respect to any past service or funding deficiencies of the Plan. Consequently, contributions are recognized as an expense in the year when employees have rendered service and represent the total pension obligation of the CDC.

Application of new and revised accounting standards

The following amendment has been issued by the International Accounting Standards Board (IASB) effective for CDC's accounting period that began on August 1, 2017, and affected amounts reported or disclosed in the financial statements:

> Disclosure Initiative – Amendments to IAS 7 – *Statement of Cash Flows* clarifies the disclosures required for changes in liabilities arising from financing activities. The amendments require entities to disclose both changes arising from cash flows and non-cash changes. The amendments are effective for annual periods beginning on or after January 1, 2017. The most significant modification made as a result of the adoption of these amendments, include the specification of the sources of changes in liabilities arising from financing activities in Note 7 - *Loans from the Government of Canada*.

Future accounting standards (accounting standards issued but not yet applied)

A number of new accounting standards and amendments effective for CDC on or after August 1, 2018, have been issued by the IASB. As at the date of the financial statements, the following applicable standards and amendments have been assessed as having a possible impact on the CDC:

> IFRS 15 – *Revenue from Contracts with Customers* was issued to provide guidance on the recognition of contract revenues. This new standard will be effective for annual periods beginning on or after January 1, 2018. The CDC has completed its assessment of IFRS 15 and expects the impact of the adoption and implementation to be limited to additional disclosures related to significant judgements and disaggregation of revenue.

> IFRS 9 – *Financial Instruments* The final version of this new standard was issued in July 2014. This standard largely retains the classification and measurement requirements and new hedge accounting model included in earlier versions, while introducing a single forward-looking expected credit loss impairment model. The new standard is effective for annual periods beginning on or

(In thousands of Canadian dollars, unless otherwise indicated)

after January 1, 2018. The CDC has completed its assessment of IFRS 9. The adoption and implementation is not expected to have a material impact on the CDC's financial statements.

IFRS 16 – *Leases* provides a single lessee accounting model, requiring assets and liabilities to be recognized for all leases, unless the lease term is 12 months or less or the underlying asset has a low value. The new standard is effective for annual periods beginning on or after January 1, 2019. The CDC has completed its assessment of IFRS 16. The new IFRS will require the CDC to recognize a lease asset and a lease liability for its lease of office space, which is currently classified as an operating lease (see Note 13 – *Commitments)*. Based on preliminary estimates, the lease asset and lease liability on transition will both be valued at approximately $3.5M. Additional disclosures will also be required in the notes to the financial statements.

4. Inventory

The CDC's inventory is comprised of butter and skim milk powder purchased under the domestic seasonality and surplus removal programs. Since February 1, 2017, in accordance with the National Ingredient Strategy, the CDC is no longer purchasing skim milk powder under these programs, and the remaining inventory on hand will be liquidated within the next twelve months. The CDC also imports butter under the World Trade Organization (WTO) Agreement on Agriculture.

Inventory:

	July 31, 2018		July 31, 2017	
	in $	in tonnes	in $	in tonnes
Plan B Butter	$ 175,254	21,818	$ 129,777	16,210
Other butter	32,520	4,083	4,161	541
Other skim milk powder	15,934	12,706	44,222	38,190
	223,708		178,160	
Less: allowance for inventory write-down	(1,738)		(1,255)	
Total net realizable value	$ 221,970		$ 176,905	

Inventory expensed in the current year was $292.12 million (July 31, 2017: $337.79 million) and is reported on the Statement of Operations and Comprehensive Income (Loss) in "Cost of goods sold (domestic and exports)".

Inventories of $Nil (July 31, 2017: $11.07 million) are expected to be realized after more than twelve months.

5. Bank overdraft

The CDC has established a line of credit with a member of the Canadian Payments Association. This line of credit was authorized by the Minister of Finance up to a maximum of $50 million with its intended use of advancing funds to the provincial milk marketing boards and agencies. The line of credit is provided in the form of a bank overdraft. As at July 31, 2018 the authorized credit limit is $10 million (July 31, 2017: $7 million). This loan is due on demand and bears interest calculated at the prime rate of 3.7% per annum as at July 31, 2018 (July 31, 2017: 2.95%).

6. Other liabilities

Other liabilities includes:

	July 31, 2018	July 31, 2017
Deferred revenue	$ 16,800	$ 3,234
Other liabilities	936	674
Total	$ 17,736	$ 3,908

Deferred revenue is comprised of revenue received in advance for the sale of butter or skim milk powder inventories not yet transferred to the purchaser as at year-end.

(In thousands of Canadian dollars, unless otherwise indicated)

7. Loans from the Government of Canada (Consolidated Revenue Fund)

Loans from the Government of Canada's Consolidated Revenue Fund are available to finance operations, up to a maximum of $225 million (July 31, 2017: $210 million). Individually, the loans mature one year after the funds are advanced. Principal and interest is paid regularly during the year when funds are available. Changes in Loans from the Government of Canada are due to financing activities, limited to changes arising from cash flows, which is reflected in the Statement of Cash Flows.

Interest on the loans is calculated at the normal rates established for Crown corporations by the government and based on the latest available yields on comparable term Treasury bills plus one-eighth of one percent at simple interest. Interest rates and interest expense were as follows:

	July 31, 2018	July 31, 2017
Interest rates		
Low	0.64%	0.58%
High	1.45%	0.70%
Interest expense	$ 985	$ 450

8. Capital management

The CDC's capital consists of loans from the Government of Canada (see Note 7) and retained earnings. As at July 31, 2018 these accounts totaled $152.85 million (July 31, 2017: $118.71 million) and $34.59 million (July 31, 2017: $35.97 million) respectively. The CDC is not subject to any externally imposed capital requirements.

The CDC's capital management framework ensures sufficient liquidity to settle financial obligations and adequate funding for programs that benefit the dairy industry. The CDC does not utilize any quantitative measurements to monitor its capital, but the CDC adjusts its capital management framework on an ongoing basis as amounts fluctuate during the year. In 2018, there were no adverse changes made to the capital management framework or its definition thereof.

9. Foreign exchange gains and losses

"Export sales revenue" in the Statement of Operations and Comprehensive Income (Loss) includes exchange net gains or losses arising from currency translation of transactions that transpire in foreign currencies.

Also, "Cost of goods sold – domestic" in the Statement of Operations and Comprehensive Income (Loss) includes exchange net gains or losses arising from currency translation of import purchase transactions that transpire in foreign currencies.

	July 31, 2018	July 31, 2017
Net gain (loss) on:		
Export sales	$ -	$ (242)
Domestic cost of goods sold	$ 691	$ 2,676

10. Funding from the Government of Canada

Funding of the CDC's administrative expenses is shared among the federal government, dairy producers, commercial operations, and the market place.

Government of Canada funding of total administrative expenses is as follows:

	July 31, 2018	July 31, 2017
Total administrative expenses	$ 8,824	$ 8,197
Funded by Government of Canada	$ 3,881	$ 3,795

11. Salaries and employee benefits

Salaries and employee benefits includes:

	July 31, 2018	July 31, 2017
Salaries expense	$5,506	$5,028
Pension contributions	645	658
Medical insurance expense	264	232
Other expenses	193	167
Total	$6,608	$6,085

(In thousands of Canadian dollars, unless otherwise indicated)

Pension plan

Substantially all CDC employees are covered by the public service pension plan (the "Plan"), a contributory defined benefit plan established through legislation and sponsored by the Government of Canada. Contributions are required by both the employee and the CDC. The President of the Treasury Board of Canada sets the required employer contributions based on a multiple of the employee's required contribution. The general contribution rate effective for the year ended July 31, 2018, was on average 1.01 times the employee's rate (July 31, 2017: 1.06 times).

The Government of Canada holds a statutory obligation for the payment of benefits relating to the Plan. Pension benefits generally accrue up to a maximum period of 35 years at an annual rate of 2% of pensionable service multiplied by the average of the best five consecutive years of earnings. The benefits are coordinated with Canada/Québec Pension Plan benefits and they are indexed to inflation.

12. Financial instruments

In the normal course of operation, the CDC is exposed to the following risks, which are managed and mitigated with corresponding policies and procedures.

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates, will affect the fair value or future cash flows of a financial instrument.

Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The CDC is exposed to this risk through normal international commercial operations. The CDC mitigates this exposure by only contracting in US and Canadian dollars. Also, the CDC uses foreign exchange forward contracts to lock future exchange rates on certain foreign currency exposures to stabilize the impact of exchange on future cash flows resulting from sales and purchases on existing contracts requiring payment in US dollars.

The fair value of the CDC's derivative financial instruments is measured using the Bank of Canada's published foreign exchange rate as at the date of the Statement of Financial Position. This rate was 1.3017 as at July 31, 2018 (July 31, 2017: 1.2485). The CDC had no foreign exchange forward contracts as at July 31, 2018, or July 31, 2017.

"Other charges" on the Statement of Operations and Comprehensive Income (Loss) includes $Nil in unrealized exchange net gains or losses (July 31, 2017: unrealized exchange net gains of $0.01 million) on derivative financial instruments.

The CDC's exposures to currency risk as at year-end are the following, based on Canadian dollar equivalent amounts:

In CAD	July 31, 2018	July 31, 2017
Trade receivables	$ -	$ -
Trade payables	-	(1,499)
Net derivative asset (liability)	-	-
Net exposure	$ -	$ (1,499)

Based on the current net exposure, and assuming that all other variables remain constant, had the Canadian dollar appreciated 10% against the US dollar, the impact to net income for 2018 would have been $Nil (July 31, 2017: increase of $0.15 million). Conversely, a 10% weakening in the Canadian dollar against the US dollar would have resulted in the equivalent impact for 2018 (July 31, 2017: decrease of $0.15 million).

Interest rate risk

Interest rate risk is the risk that a financial asset containing a fixed interest rate component decreases in fair value with a rise in interest rates or that a financial liability with a floating interest rate component results in increased cash outflow requirements as a result of an increase in interest rates. The line of credit, for which interest varies as a function of prime, and loans from the Government of Canada, for which interest varies as a function of the yield on comparable Treasury bills, expose the CDC to a cash flow risk. The CDC's interest rate risk is not significant given its low interest bearing loans, for which adverse rate increases are not expected over the next twelve months.

Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices, other than those arising from interest rate risk or currency risk. The CDC is not significantly exposed to this type of risk.

Liquidity risk

Liquidity risk is the risk that the CDC will not be able to meet its financial obligations as they fall due. As at the Statement of Financial Position date, all of the CDC's financial instruments are current and the CDC has a current ratio equal to 1.17 (July 31, 2017: 1.24). In managing liquidity risk, the CDC has access to additional borrowings for commercial operations from the Government of Canada in the amount of $72.15 million (July 31, 2017: $91.29 million), as well as $2.42 million (July 31, 2017: $1.01 million) on its line of credit for the pooling of market returns, both as at July 31, 2018.

Credit risk

Credit risk is the risk of financial loss for one party due to another party failing to meet its financial obligations. The CDC's main credit risk exposure comes from the carrying amount of the pooling and trade receivables balances, net of any allowance for losses. The CDC manages this risk by selling product on a "payment first" basis, securing bank guarantees and obtaining letters of credit. As at July 31, 2018, and July 31, 2017, the CDC does not have an allowance for doubtful accounts and all trade receivables are current.

The CDC is also exposed to credit risk when it holds foreign exchange contracts. This exposure is limited to the notional amount of Derivative asset – foreign exchange contracts. The CDC manages this risk by only entering into foreign exchange contracts with major Canadian financial institutions. To date, no such counterparty has failed to meet its financial obligation to the CDC. As at July 31, 2018, and July 31, 2017, the CDC does not hold any foreign exchange contracts.

Fair values

The carrying amount of cash, trade and other receivables, bank overdraft, and trade and other payables approximate their fair value due to the immediate or short-term maturity of these financial instruments. Therefore, as at the Statement of Financial Position date, no amounts representing changes in fair value of these financial instruments are reported on the Statement of Operations and Comprehensive Income (Loss).

Fair value hierarchy

Financial instruments reported at fair value on the Statement of Financial Position are classified using a fair value hierarchy that reflects the significance of the inputs to valuation techniques used to measure fair value. The fair value hierarchy, which for the CDC only applies to derivative financial instruments, has the following levels:

Level 1: inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2: inputs are other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and

Level 3: inputs are unobservable inputs for the asset or liability (i.e. not based on observable market data).

When the CDC holds foreign exchange derivatives, their fair value is calculated using the Bank of Canada's published foreign exchange rate as at the date of the Statement of Financial Position. This input to the valuation technique used to measure fair value is classified as Level 2 on the fair value hierarchy (July 31, 2017: Level 2). For the reporting periods ended July 31, 2018, and July 31, 2017, there were no transfers between levels. The CDC does not hold any foreign exchange derivatives as at July 31, 2018, and July 31, 2017.

13. Commitments

a) Industry Initiatives

Matching Investment Fund

The CDC funds and administers the Matching Investment Fund which provides non-repayable contributions to Canadian-registered companies or food technology centers for product development, on an investment matching basis. As at July 31, 2018, the CDC has outstanding contractual commitments of up to $15.03 million.

(In thousands of Canadian dollars, unless otherwise indicated)

The expected timing of expenditures in relation to the Matching Investment Fund is as follows:

	July 31, 2018	July 31, 2017
Less than one year	$ 7,520	$ 183
Later than one year but not later than five years	7,506	$ –
	$ 15,026	$ 183

Workforce Development Initiative

The Workforce Development Initiative encourages productivity, competitiveness, and innovation in the Canadian dairy industry by supporting the education and recruitment of a qualified workforce. The CDC Board adopted this initiative in December 2017 and has agreed to grant $5.00 million over three years to qualifying learning institutions and dairy associations (producers or processors) across Canada. This initiative includes four programs: career promotion, development of full-time education programs, development of continuing education, and graduate scholarships. As at July 31, 2018, there are no outstanding contractual commitments under this initiative.

b) Purchase Commitments

As at July 31, 2018, the CDC has commitments to purchase predetermined quantities of butter. These commitments amounted to approximately $0.40 million (July 31, 2017: $2.76 million) and were fulfilled by August 2018.

c) WTO Tariff Rate Quotas for Butter

The Government of Canada establishes tariff rate quotas (TRQ) for a number of dairy products, limiting the quantity of product that can enter the country with little or no duty. For butter products, under the terms of the 1994 WTO Agreement, Canada is committed to providing minimum annual market access opportunities totalling 3,274 tonnes, setting the minimum TRQ on butter products at the same level. Since 1995, subject to renewal each quota year (August to July), the CDC is mandated by the Minister of International Trade to ensure that Canada's butter TRQ is fully used, and that imported butter is redistributed to the Canadian food sector through butter manufacturers.

As at July 31, 2018, the TRQ on butter is entirely used for quota year 2017-2018. The CDC is committed under the same conditions for quota year 2018-2019. The TRQ on butter for 2018-2019 remains at 3,274 tonnes. The financial impact of this commitment for the next period is affected by the price variability between countries and type of eligible butter products, as well as the foreign exchange rates.

The total cost to purchase imported butter for the year ended July 31, 2018, was $26.35 million (July 31, 2017: $121.47 million).

d) Operating Lease

The CDC is committed under a long-term lease with Agriculture and Agri-Food Canada for office space ending in March 2022. The lease contains escalation clauses for maintenance costs and taxes. The CDC has the option to renew the lease for an additional period of five years with rates revised to reflect the rental market value pursuant to the Treasury Board's Policy on Real Property.

The minimum lease payments are as follows:

	July 31, 2018	July 31, 2017
Less than one year	$ 370	$ 370
Greater than one year and less than five years	$ 986	$ 1,356

14. Related party transactions

Government of Canada entities

The CDC, as per the *Canadian Dairy Commission Act*, is an agent of Her Majesty the Queen in right of Canada. This effectively gives the Government of Canada significant influence over the CDC and its activities.

The CDC is related in terms of common ownership to all other Government of Canada departments, agencies and Crown corporations. The CDC enters into transactions with these entities in the normal course of operations and at normal trade terms. These related party transactions are reported at their exchange amounts.

(In thousands of Canadian dollars, unless otherwise indicated)

Under IAS 24 – *Related Party Disclosures,* the CDC is exempt from certain disclosure requirements relating to transactions and outstanding balances with:

- a government that has control, joint control or significant influence over the reporting entity; and
- another entity that is a related party because the same government has control, joint control or significant influence over both the reporting entity and the other entity.

Accordingly, the CDC discloses limited information regarding transactions entered into with the Government of Canada and its departments, and with all federal Crown corporations not considered to be individually or collectively significant.

The CDC's transactions with government-related entities that were individually significant are Loans from the Government of Canada (Note 7) and Funding from the Government of Canada (Note 10).

Other transactions with government-related entities that were collectively, but not individually, significant are:

Key management personnel

The CDC's key management personnel are the members of the Commission's Board and the directors.

No loans or similar transactions with key management personnel are outstanding as at July 31, 2018, or July 31, 2017. There were no transactions of this nature during either year.

Post-employment benefit liability for key management personnel reported under "Other liabilities" on the Statement of Financial Position amounts to $0.10 million as at July 31, 2018 (July 31, 2017: $0.09 million).

Compensation of key management personnel for the year ended July 31, 2018 is $1.21 million (July 31, 2017: $1.14 million).

Government entity	July 31, 2018	July 31, 2017
Public Works and Government Services Canada	$ 1,126	$ 1,062
Agriculture and Agri-Food Canada (mainly operating lease – Note 13)	455	229
Other related Government entities	131	215
Total	$ 1,712	$ 1,506

Tables and Data (unaudited)

Total Milk Production, Quota and Requirements (million kg butterfat)

	Total Requirements	Total Quota	Total Production
2013-2014	321.36	316.55	313.68
2014-2015	328.67	326.57	327.67
2015-2016	344.81	336.57	338.78
2016-2017	364.20	355.56	358.21
2017-2018	371.11	368.59	380.03

Number of Farms and Cows

	Number of farms	Number of cows (thousands)
2013-2014	12,234	959.1
2014-2015	11,962	956.7
2015-2016	11,683	954.6
2016-2017	11,280	959.1
2017-2018	10,951	945.0

Milk Production by Province* (million kg butterfat)

Province	2016-2017	2017-2018
Newfoundland and Labrador	2.01	2.08
Prince Edward Island	4.76	5.03
Nova Scotia	8.00	8.48
New Brunswick	6.17	6.60
Quebec	133.38	139.80
Ontario	118.48	123.91
Manitoba	14.03	16.06
Saskatchewan	10.46	11.45
Alberta	29.89	33.08
British Columbia	31.03	33.54
Total	**358.21**	**380.03**

*Before pooling