



People who know Manufacturing, know BDO.

Assurance | Accounting | Tax | Advisory | www.bdo.ca/manufacturing



BDO USA RiskFactor Report highlights concerns about skilled worker shortage as the industry looks towards growth

BY JOSEPH GIPP — BDO CANADA LLP

As the US manufacturing sector continues to recover, many Canadian manufacturers may be looking to expand their operations south of the border to capitalize on this recovery. In fact, 80 per cent of respondents in the recently released *Canadian Manufacturers and Exporters' (CME) Management Issues Survey* indicated the US as the top country for future growth in new markets. While the outlook for the US manufacturing sector appears positive, Canadian organizations should be prepared for many of the same challenges they face here when looking to the US as a source of growth.

BDO USA's second annual *Manufacturing Risk Factor Report* highlights the top industry risks reported by manufacturing companies. The top risks, as identified by analyzing risk factors listed in the most recent filings of the largest 100 public US manufacturers, are supply chain, regulatory and labour concerns. Not surprisingly, this mirrors the findings of the recently released *CME Management Issues Survey*.

Concerns over supply chain risks, such as commodity cost control, may be good news for Canadian companies who are able to supply and ship materials at a lower cost as the Canadian dollar continues to decrease. However, challenges with labour and regulatory issues require Canadian companies to be cautious when looking to the US as a complete solution for their growth goals.

Labour shortages are a concern on both sides of the border

Growth and recovery of the US economy is fueling demand for skilled labour. However, with baby boomers starting to leave the workforce, attracting and retaining skilled labour presents a risk for operational expansion. Of those surveyed, 97 per cent of US manufacturers cited labour factors as a risk

this year, compared to almost 60 per cent in the CME survey. This growing skills gap may be further compounded by the increasing trend towards repatriation of US manufacturing jobs.

Historically, the manufacturing sector outsourced much of their supply chain overseas. With recent changes to global economic and political conditions, and exposures due to natural disasters, many manufacturing companies are taking a closer look at how secure and efficient their supply chains are. The top reported risk, in the risk factor report, is US and foreign supplier/vendor concerns and distribution disruptions. This concern is causing many US manufacturers to reshore their operations which increases demand for skilled tradespeople as they staff up. Manufacturing organizations, either in Canada or the US, who are able to develop innovative solutions to bridge the labour gap and further secure their supply chain (through investments in technology or investments in training and apprenticeships) will be better poised for growth.

M&A Opportunities in US due to increased competition for scarce resources

Increased growth in the manufacturing industry is creating fierce competition for scarce labour and supply chain resources. Canadian expansion into the US market will continue to squeeze these resources, potentially leading to increased merger and acquisition activity.

Competition and consolidation are seen as a risk by 94 per cent of US manufacturers. The recent Hillshire Farms and Pinnacle deal in the US food processing industry is further proof that many companies are turning to acquisitions to gain a competitive advantage. Vulnerable companies who have not addressed these risks may provide an opportunity for Canadian manufacturers to gain a foothold in the US market.

Lower Canadian Dollar and Willingness to Invest in Technology Provides Opportunity for Canadian Companies

Additional factors such as commodity or raw material prices, foreign exchange fluctuation, access to capital and even risks around maintaining IT systems and operational infrastructure, may present opportunities for Canadian organizations in the US market. With the majority of the CME survey respondents anticipating new investments in R&D, machinery and equipment, and facilities in the next three years, it is evident that Canadian companies are already thinking about these challenges. Available SR&ED and other government incentives, for those that qualify, may provide organizations access to capital for these investments and the lower Canadian dollar makes exporting to the US more cost effective, increasing Canadian companies' ability to compete.

Overall, the outlook for manufacturing across North America seems positive. "Growth in the economy and an increase in capital spending is excellent news for the manufacturing industry," said Howard Sosoff, Manufacturing & Distribution practice leader at BDO USA, LLP. "But with greater opportunity comes greater challenges. Manufacturers will face intense competition this year as they work to attract new orders and workers and expand their capabilities." Canadian manufacturers looking to expand into the US will need to prepare for these challenges in order to minimize their risks.

The 2014 BDO Manufacturing RiskFactor Report examines the risk factors in the most recent 10-K filings of the largest 100 publicly traded US manufacturers across five sectors including fabricated metal, food processing, machinery, plastics and rubbers and transportation equipment. The factors were analyzed and ranked by order of frequency cited. The top 20 risk factors are listed in the chart on the right. For more information on the 2014 BDO Manufacturing RiskFactor report, visit www.bdo.com. ²⁰²⁰

Joseph Gipp, CPA, CA is a Partner at BDO and BDO Canada's Manufacturing Industry Leader. He can be reached at jgipp@bdo.ca.

2014 Rank		2014	2013
#1	US and Foreign Supplier/Vendor Concerns and Distribution Disruptions	100%	83%
#2	Federal, State and/or Local Regulations	99%	96%
#3	Labour Concerns; Underfunded Pensions	97%	75%
#4	General Economic Conditions	96%	98%
#4t	Commodity/Raw Material Prices	96%	86%
#6	Competition & Consolidation in Manufacturing	94%	92%
#7	Threats to International Operations	91%	87%
#8	Management of Mergers & Acquisitions	89%	80%
#8t	Access to Capital	89%	78%
#10	Currency/Foreign Exchange Fluctuation	88%	73%
#10t	Natural Disasters, Terrorism and Geo-Political Events	88%	68%
#12	Environmental Laws, Regulations & Liability	87%	86%
#12t	Changes to Accounting Standards and Regulations	87%	66%
#14	Less Demand for Products	86%	91%
#15	Failure to Properly Execute Business Strategy	82%	74%
#16	Maintaining IT Systems & Operational Infrastructure	80%	75%
#17	Legal Proceedings	79%	57%
#18	Ability to Innovate to Meet Changing Customer Needs	78%	69%
#18t*	Privacy Concerns Related to Security Breach	78%	64%
#20	Restrictive International Trade Policies	77%	66%

*t indicates a tie in the risk factor ranking