FINAL TRANSCRIPT

Maple Leaf Foods

Fourth Quarter 2020 Results Conference Call

Event Date/Time: February 25, 2021 — 8:00 a.m. E.T.

Length: 68 minutes

CORPORATE PARTICIPANTS

James Allison
Maple Leaf Foods — Investor Relations & Capital Markets

Michael McCain
Maple Leaf Foods — President and Chief Executive Officer

Curtis Frank
Maple Leaf Foods — President and Chief Operating Officer

Geert Verellen
Maple Leaf Foods — Chief Financial Officer

CONFERENCE CALL PARTICIPANTS

Irene Nattel
RBC Capital Markets — Analyst

Mark Petrie
CIBC World Markets — Analyst

Michael Van Aelst
TD Securities — Analyst

Peter Sklar
BMO Capital Markets — Analyst

George Doumet
Scotiabank — Analyst

Derek Dley
Canaccord Genuity — Analyst

PRESENTATION

Operator

Good morning, ladies and gentlemen. Thank you for standing by. Welcome to Maple Leaf's fourth quarter 2020 financial results conference call.

As a reminder, this conference call is being broadcasted live on the internet and recorded.

All lines have been placed on mute to prevent any background noise.

Please note that there will be a question-and-answer session following the formal remarks, and we will go over the question-and-answer session instructions following the conclusion of the formal presentation.

I would now like to turn the conference call over to James Allison, Investor Relations at Maple Leaf.

Please go ahead, Mr. Allison.

James Allison — Investor Relations & Capital Markets, Maple Leaf Foods

Thank you, Joanna, and good morning, everyone. Speaking on the call this morning will be Michael McCain, Chief Executive Officer; Curtis Frank, Chief Operating Officer; and Geert Verellen, Chief Financial Officer.

Before we begin, I would like to remind you that some statements made on today's call may constitute forward-looking information, and our future results may differ materially from what we discuss. Please refer to our 2020 MD&A and other information on our website for a broader description of operations and risk factors that could affect the Company's performance.

We have also uploaded our Q4 investor deck to our website, which includes support material for the quarter. As always, the Investor Relations team will be available after the call for any follow-up questions or any detailed modelling questions you might have.

And with that, I’ll turn the call over to Michael McCain.

Michael?

Michael McCain — President and Chief Executive Officer, Maple Leaf Foods

Thank you, James, and good morning, everyone, and welcome to our fourth quarter 2020 earnings call. I hope you’re all staying safe in the middle of this environment.

I’m joined today by Curtis Frank, our Chief Operating Officer, and Geert Verellen, our Chief Financial Officer.

I will begin with prepared remarks describing the year, the quarter, and our outlook for 2021 and beyond and then open up the call to questions.

So, 2020. This was a year like no other we’ve ever experienced in a generation. It began with a sense of raw optimism that we had momentum in our strategies, and we were executing consistently.

Then came COVID-19. We halted everything in the moment but for the projects that we could not touch without irreparable harm. We focused on the priorities at hand: number one, protecting our people; number two, ensuring the continuity of our supply chains; and number three, transitioning to a new way of work overnight; and number four, living our practice of shared value principles by supporting all of the stakeholders in the Maple Leaf ecosystem as best we possibly could.

I have to say I’m incredibly proud, likely more than I’ve ever been in my lifetime, in our team and their collective accomplishments in this environment. Over the course of 10 months, they demonstrated all the things that we’d want to see them demonstrate: speed and agility as a seamless transition to remote working unfolded; resilience and empathy as they dealt with the stress of the moment in this pivot; execution skills as we delivered a record financial performance year, a record year after absorbing unplanned COVID operating costs of $58 million; and strategic efficacy and resilience as our vision and our path to becoming the most sustainable protein company on earth demonstrated everything that we would want it to and more. And it was competitively differentiating. It was principled. It was lucrative. And it's proven to be durable.

In short, 2020 was a year where the Maple Leaf team showcased what I believe to be its greatest strengths. First and foremost, we continued to keep our people safe through rigorous implementation of best-in-class safety protocols. Guided by the latest science and working alongside local health officials, our facilities have remained safe, with no evidence of any workplace transmission of COVID-19.

Second, we delivered on our responsibility to customers and consumers and communities across the country and throughout the continent by ensuring the security and continuity of our supply chain. While the second wave of COVID-19 once again posed several challenges to manufacturers, our teams worked tirelessly to ensure our operations continued uninterrupted across our network.

And finally, we remain committed to supporting vulnerable communities throughout this chaos. The continued efforts across our organizations, especially through the Centre, the Maple Leaf Centre for Action on Food Security, have enabled us to assist those most deeply affected by the devastating economic impact of the pandemic.

The financial performance was exemplary. On a full year basis, our Meat Protein business delivered sales growth of 9 percent. Consider that carefully, 9 percent. Now consider the durability of that growth.

Since 2015, just five years ago, we've focused on pivoting from fixing the business to growing the business, building an enterprise that has structural capacity to grow. That's no easy task.

Since 2015, we've repositioned our portfolio towards two high-growth categories, sustainable meat and plant-based protein, which, in 2020, represented fully 20 percent of our annual sales and have generated a combined compounded growth rate in excess of 25 percent combined over the last three years.

I believe this is unprecedented in CPG, unprecedented. Twenty percent of our revenue comes from two strategically positioned categories built for growth, a CAGR of 25 percent combined over the last three years. We've pivoted from fixing the business to growing the business.

But simultaneously, in 2020, we grew our meat segment's adjusted EBITDA margin by 200 basis points to 12.4 percent for the year and significantly advancing us towards our target of 14 percent to 16 percent by 2022. Aggressive top-line growth and margin expansion in a record performance year in the middle of chaos. That can only be described as a success.

Of course, the biggest disappointment was a slowdown in the back half of the year in our Plant Protein revenue growth rate. For the full year, we delivered 19.5 percent, which was short of our 30 percent target. There are a lot of reasons for this, and we are acutely, acutely aware of each one of them.

In addition to the supply chain challenges that we had, COVID contributed to category deceleration, impacted our ability to commercialize our innovation pipeline in the year, and limited foodservice channel growth. Additionally, there was a new retail channel entrant which drove competitive activity in one of our many subsegments.

Of course, these things are always concerning in the short term, but they don't change our conviction to the long-term thesis. Number one, we believe that long-term consumer behaviour will not be defined by COVID moments. Number two, we have leading brands in the category and many decades of experience in developing brands. Number three, our supply chain obstacles are being sorted out. Number four, we launched our refreshed brand strategies only in the middle of 2020, and it's really super-early days. And number five, we have a very robust innovation pipeline to support our growth ambitions.

Our challenges are very focused on the fresh meat segment, which is commanding our short-term attention. But the core categories in our portfolio continue to grow robustly, and Curtis will describe this in more detail shortly.

As an investor in Maple Leaf, I can appreciate that this is a challenging period, one which could test conviction around our investments in plant-based businesses. I am certainly fortunate in that I have the ability to see firsthand the pace of innovation, the vibrancy of the market, and draw parallels between the investment and transformation that we've made in the past in our Meat Protein business and what we're doing now in Plant Protein; that our relentless focus in food innovation, brand renovation, and the pursuit of operational excellence will pay off, as evidenced by our success with the same playbook and the resulting exceptionally strong year we've had in Meat Protein.

While this can create some short-term pressure on the stock price, as a long-term investor who believes deeply in this opportunity, I can assure you of this: We unequivocally believe that the investments we're making in this business will be rewarded, albeit causing valuation dislocations in the short term.

We believe that staying the course with our investments is the right course of action. The reasons for our disappointing revenue growth rate in the back half of 2020 are certainly well understood, and we're acting on them. And we will be financially, strategically, and operationally disciplined, as we always, always are, in investing your capital alongside our own in decisions that we make for this business, short, medium and long term.

So in summary, a year like no other. In 2020, Maple Leaf lived by our shared value belief system, demonstrated our strategic resilience and efficacy. We showcased our execution skills and delivered a record financial performance, with one challenge that we're confident we can overcome. Growth will never be linear every year or every quarter, and we're well positioned to continue to realize superior returns.

So with that, I'd like to now turn it over to Curtis who is going to review the operations, and then Geert, who will cover the financials. Curtis?

Curtis Frank — President and Chief Operating Officer, Maple Leaf Foods

Thank you, Michael, and good morning, everyone. Before speaking to our operating performance, I would like to echo Michael's comments with respect to the incredible efforts of our team who have been working absolutely tirelessly to fulfill our obligation and responsibility as an essential service, while also keeping safe.

The second wave of COVID-19 hit our communities harder and faster than any of us expected as we closed off 2020. Our Q4 operating performance is a testament to the resilience of our people, the resilience of our blueprint, and also, the effectiveness of our pandemic playbook.

The success that we've seen in our Meat Protein Group in 2020 is a direct result of the strategic drivers that we have pursued over the past several years, along with our team's ability to execute them.

We've continued to see strong demand across our sustainable meats platform, which grew at over 25 percent in the fourth quarter and now generates over $600 million in sales annually.

We also continued to benefit from strong momentum across our brands, specifically the Maple Leaf brand this quarter, which continues to gain share in prepared meats.

And finally, we continued to make deeper inroads into the US market, again growing at double digits in Q4, led by our greenfield sustainable meats brand.

While our existing offering performed exceptionally well, we also realized important success from new product innovation. Following the exciting launch of Maple Leaf Prepped & Ready and Schneiders Protein Kits as innovations late in Q3, both of these products were recognized as best new products for 2021 in their respective categories, with voting based entirely on consumer results.

The success of our Meat Protein strategies was demonstrated in our Q4 results, with strong top-line growth coupled with adjusted EBITDA margin expansion of 120 basis points to 12.6 percent.

What makes this result especially encouraging is that we achieved these results despite absorbing almost $15 million in COVID costs, facing a slight headwind from the Pork Complex, driven by below-average packer margins and without the benefit from any pork sales to China from our Brandon, Manitoba facility.

As you know, China represents a high-growth, lucrative opportunity for us. And while we are ready to resume shipping into China and we have reapplied for import permits, it remains unclear when an approval to resume shipments will occur. In the interim, our team is working diligently to redirect product to alternative markets, including other Southeast Asian markets of high value.

Overall, we are thrilled with the results in Meat Protein for the quarter and for the year, and we absolutely remain confident in our ability to reach our 2022 strategic margin target of 14 percent to 16 percent.

Turning to the Plant Protein Group, 2020 clearly played out differently than we expected. After a very strong first half where we delivered 34 percent growth, I must echo Michael's disappointment with the slower growth rates we achieved in the back half. While we were able to quickly correct from the packaging issues we experienced in Q3, we did not see the demand we expected in two specific product lines in the fourth quarter, which was due in part to an intensifying second wave of COVID-19.

Given this performance, I think it's important to break down our fourth quarter into three distinct components. Firstly, we continue to see strong underlying momentum in the core components of our Lightlife and Field Roast offerings. We define the core as the broad portfolio of products that are traditionally found in the produce and frozen sections of the grocery retail store.

After recovering sharply from the operational challenges we faced in Q3, this group of core products had growth that was more in line with what we would have expected in terms of contributing to our strategic target for the quarter and for the year.

Two of the bright spots within the core offering were our Lightlife Tempeh and our Field Roast Chao Cheese items. As the largest North American tempeh producer, in recent years, we have helped the category to realize absolutely exceptional growth as it gains recognition and expanding consumer adoption. We do believe that there remains significant upside. And in November, we strengthened our partnership with Walmart USA by adding tempeh distribution to 3,500 stores, a tenfold increase.

We have also had success with our Field Roast Chao Cheese lineup. Chao has the number one SKU of plant-based cheese in North America, with offerings in multiple formats, including slices, blocks, and shreds. After early success in launching five new flavours and formats in Q3, we doubled our distribution with Walmart to over 2,000 US locations in late Q4. Our Chao portfolio can now be found at over 18,000 retail locations across the US.

The second component of our Q4 performance is related to our Lightlife fresh product line. Our fresh line consists largely of burgers, sausages, and grounds, which are mainly found in the meat case of the grocery store. Here, COVID delayed the rollout of new and innovative products, and demand for this line softened as the overall category growth slowed and a new competitor entered the retail space.

It is important to acknowledge that these products are appealing to a large set of consumers who are relatively new to plant-based protein and are still developing their motivations to purchase.

Recall that, as part of our renovation, we relaunched the Lightlife fresh line in the third quarter with new formulas and packaging, along with a new marketing campaign focused on Lightlife's fresh and clean ingredients. And while it's early days, we believe our simple, healthy ingredients provide a clear point of differentiation that will resonate with consumers over the long term.

The third component of performance resulted from weak growth in foodservice. The second wave of COVID-19 caused a swift reversal of easing government restrictions at the end of 2020. This severely impacted restaurants and quick-serve businesses. While we have maintained existing relationships and see significant opportunities for growth in the future, the timing of both the recovery and onboarding of new business in the foodservice channel will inevitably be bound to the reopening of economies as the pandemic comes under control.

Stepping back and looking at the performance beyond the quarter, we achieved many significant milestones in the Plant Protein business throughout the year 2020. These milestones are deeply important as they serve to set up the business for success in 2021 and well into our future.

Firstly, we stabilized our logistics and distribution costs in the fourth quarter to better serve our high-growth business model.

Secondly, we are closing in and nearing the completion of the renovation and relaunch of two of North America's best-known and most-loved plant-based protein brands; in Lightlife, which focuses on clean and simple ingredients, and in Field Roast, which is doubling down on its commitment to delivering bold and adventurous taste.

Paralleling the success of our brand renovation in meat protein, we believe these brand strategies offer focus points of differentiation that are backed by significant consumer research.

Third, we have assembled a first-class team of food innovators and marketers to support our vastly growing business.

And finally, we continue to find capital-efficient methods to quickly scale production capacity, including leveraging available footprint across our Maple Leaf network and seizing on a unique opportunity for a brownfield conversion for tempeh.

While these investments have not yet fully surfaced in our financial performance, we remain confident that they provide a solid foundation, high levels of growth well into the future.

I'll now turn it over to Geert to discuss our financial results in more detail.

Geert?

Geert Verellen — Chief Financial Officer, Maple Leaf Foods

Thank you, Curtis, and good morning, everyone. I will begin by discussing the Company's consolidated performance during the fourth quarter. I will then turn to a more detailed look at both our Meat and Plant Protein Groups. I'll conclude by speaking to some key financing metrics, capital expenditures, and an outlook for 2021.

Sales were approximately $1.1 billion, an increase of 11 percent from the prior year. This increase was driven by an extra week in the fourth quarter of 2020 and strong performance in Meat Protein, which more than offset weaker sales growth in Plant Protein.

Adjusted EBITDA was approximately $109 million, an impressive increase of 45 percent from the prior year. The increase was driven by strong performance in Meat Protein, as well as the fact that we are lapping strong investment in Plant Protein at the end of 2019.

Total company adjusted EBITDA margin was 9.7 percent for the quarter, an increase of 225 basis points from last year.

These results include the impact of incremental operating costs due to COVID-19, which totalled $15 million in the quarter. These costs are largely captured in cost of goods sold and were in line with our expectations.

As in prior quarters, we were able to mitigate some of these costs through savings in discretionary spend such as travel and training. The net impact was $13 million, which had a dilutive impact on our adjusted EBITDA margin.

Adjusted operating earnings were $59 million compared to $28 million in the prior year, resulting from strong commercial performance in Meat Protein, more than offsetting the COVID-19 costs I just discussed.

Net earnings were approximately $21 million or $0.16 per basic share compared to $17 million or $0.14 per basic share last year. After removing the impact of non-cash fair value changes in biological assets and derivative contracts from both periods, adjusted earnings per share were $0.30 for the quarter compared to $0.12 per share in the prior year.

I'll now turn to a discussion of Maple Leaf's two operating segments.

First, our Meat Protein sales for the fourth quarter were nearly $1.1 billion, an increase of 11 percent from the prior year. The increase was due to a favourable shift in sales towards sustainable meats and branded products, pricing action taken in the third quarter to reflect structural inflation, and the impact of an extra week in the fourth quarter of 2020.

Meat Protein adjusted EBITDA for the quarter was $137 million, a significant increase of 24 percent over prior year. This growth was mainly due to an improved sales mix from a higher percentage of sustainable meats and branded retail sales, pricing action to mitigate inflation, and other structural cost increases and strong operational performance. These positive drivers more than offset the incremental COVID-19 costs incurred in the quarter.

Adjusted EBITDA margin for the Meat Protein segment was 12.6 percent, a 120-basis-point improvement over the prior year. This represents the fifth quarter of consecutive adjusted EBITDA margin expansion and progression towards our 2022 target.

Turning now to Q4 results in our Plant Protein Group where we continue to invest for growth in a fast-paced and high-potential market. Sales were $53 million, an increase of 5.5 percent from the prior year or 7 percent in constant currency terms. The sales increase was predominantly driven by an extra week in the quarter, as well as by annual pricing actions taken to reflect structural cost inflation.

And as Curtis indicated earlier, strong growth in Greenleaf's core product lines was offset by weaker growth in the fresh line and a contraction in foodservice, as we lapped a strong fourth quarter last year that was unaffected by COVID.

Gross margin for the quarter was 0.5 point. It was severely impacted by lower-than-expected sales volumes leading to higher overhead costs related to long-term capacity expansion, as well as indirect costs associated with brand renovation and the impact of COVID. These factors more than offset volume impact of the extra week in the fourth quarter of 2020.

SG&A expenses in Plant Protein were $32.5 million, in line with our plan, and brought SG&A investment for the full year to $144 million. SG&A as a percentage of sales decreased to 62 percent from 91 percent a year ago as we lapped a period of heightened investment in the back half of 2019.

Turning now to our balance sheet. Maple Leaf's balance sheet remains strong, with $645 million in net debt and $1.3 billion in undrawn committed credit. Of the debt, $432 million is construction capital, which is carried on the balance sheet and is not currently generating a return but will within the next few years.

During the quarter, we invested $191 million in CapEx, including construction capital of $135 million primarily related to the construction of our new poultry facility in London, Ontario.

For the full year, we invested just over $491 million in capital expenditures, including about $192 million in construction capital. This was in line with our revised target investment we communicated back in October of between $450 million and $500 million.

While we have the financial flexibility necessary to complete near-term capital projects, we remain focused on deploying this capital in an efficient and balanced manner, with the goal of maximizing shareholder value. For example, we recently announced the planned acquisition of an existing food processing plant in Indianapolis. This building is only four years old and will enable us to quickly and cost-effectively add additional tempeh production capacity to meet burgeoning demand.

And yesterday, our Board of Directors approved a 13 percent increase to our quarterly dividend to $0.18 per share, commencing in the first quarter of 2021. This represents the seventh consecutive year of dividend growth, underscoring our commitment to a balanced capital allocation and the confidence we have in our business plans and future financial strength.

I'd like to conclude with an outlook for our business for 2021. I should note that our expectations for 2021 are based on certain assumptions regarding the state of the market over the year ahead. While we are hopeful the end of the pandemic and related government measures is near, there remains a level of uncertainty around timing and pace. This may also include continued volatility in commodity and currency markets.

We have outlined our assumptions within our Outlook section of our MD&A and within our slide deck, both of which are available on our website.

So in the Meat Protein Group, we expect to deliver mid-to-high single-digit sales growth in 2021, on a 52-week comparable basis, coming from continued momentum in sustainable meats, growth in branded volumes as we continue to benefit from our brand renovation and sales to the US.

We also expect adjusted EBITDA margin expansion progression towards the 2022 target of 14 percent to 16 percent, driven by mixed benefits in prepared meats resulting from growth in sustainable meats and our branded product, as well as operational efficiencies.

Our outlook assumes that the North American Pork Complex will be in line with the five-year average.

In our Plant Protein Group, we expect 2021 sales growth to be broadly in line with our strategic target of 30 percent, excluding any impact from fluctuations in foreign exchange. This growth is expected to come from continued momentum in our core Lightlife and Field Roast product lines, improved velocities and distribution in our recently launched fresh line, and resurgence in the foodservice market as COVID restrictions abate.

We expect gross margin in Plant Protein to be volatile in the near term as the benefits from structural improvements in our supply chain may be impacted by investment opportunities to drive sales growth in a rapidly evolving market. Also, in Plant, we expect SG&A expenses to be broadly in line with the 2020 levels, excluding the impact of foreign exchange, while declining as a percentage of sales as we continue to leverage investments in advertising, promotion, and marketing to elevate the Lightlife and Field Roast brand renovations, drive innovation, and build scale in the business.

We anticipate total capital expenditures to be between $550 million and $650 million in 2021. And CapEx is weighted, again, towards construction capital, including the London poultry facility, the new Indianapolis plant protein tempeh facility, and enhancements in our prepared meats business.

I will now turn the call back to Michael.

Michael?

Michael McCain

So thank you very much, Curtis, and thank you, Geert. I appreciate the very detailed review.

Our strength at Maple Leaf Foods in consumer packaged goods and brand development and product positioning and manufacturing has been built over decades in the food industry. We’ve been focused and strategic in our approach, in our investments, in our execution, in how we build Maple Leaf Foods for long-term growth and long-term profitability.

Our experience in the meat protein industry has taught us that building brands and operational capacity and efficiency can take time and perseverance. We don’t waiver based on a quarter or two, yet we do maintain our highly disciplined and highly analytical focus and approach to execution.

As each quarter passes, we see the benefits of our strategic direction and our investments in capital and in brands, giving us even greater confidence that we will deliver on our financial objectives.

Similarly, in Plant Protein, we're building a remarkable business with leading brands in one of the food industry's most exciting markets. We're looking ahead to getting back on track in 2021 and delivering on the promise of this business.

As we close the books on 2020, I'd like to conclude by expressing a deeply and profound gratitude to our frontline team members that came to work every single day to make the food on which we all depend. I'm humbled and I'm grateful for your commitment and inspired by the dedication of all of our people to persevere and succeed in this most extraordinary environment.

So with that, I'd like to now open it up to your questions. Operator, please?

Q&A

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press the *, followed by the 1 on your touch-tone phone. You will hear a three-tone prompt acknowledging your request. If you are using a speakerphone, please lift the handset before pressing any keys.

We also ask that you limit time to one question plus one follow-up before cycling back into the queue. We'll pause for a moment to compile the Q&A roster.

Your first question is from Irene Nattel. Please go ahead.

Irene Nattel — RBC Capital Markets

Thanks, and good morning, everyone, and really, thank you for all of that colour. Just starting on the Plant business. Really interesting colour around the new volume that you're getting out of Walmart in the core products. If we think about the 30 percent targeted growth for 2021, 30 percent-ish, how much of that could be attributed to sort of that volume that's already "locked in"?

Michael McCain

I don't think we can give you a specific answer to that. A significant portion of growth always depends on a combination of current activity and innovation. Obviously, our innovation pipeline was impaired in 2020. We are seeing that coming back on track in 2021. So I don't think that we can segment that in terms of how much is secure versus insecure.

Obviously, in a high-growth market like this, Irene, there's a lot of variables at play and not the least of which is the continuity of the second wave or, in some cases, third wave of COVID, which blended into the first quarter. And that obviously had an impact on it as well.

So I think that thematically, we're doing the right things. It's a combination of starting to realize on the efficacy of our brand renovation that just began in the back half of 2020, the restarting our innovation pipeline, getting our foodservice segment sort of recovered, would be the right word, and then continued execution in the core businesses.

I can't emphasize enough that we have a very robust core business and challenges in the fresh meat case with one subsegment, and that's what we're focused on.

Curtis, is there anything you'd add to that?

Curtis Frank

No. I think you characterized it well, Michael. The only thing I might add is, is the Chao business, in and of itself, we disclosed in our materials that we put out earlier this morning, saw significant growth in the quarter, over 30 percent, and we're adding new distribution on top of that. So a very fast-growing component of our business and one that we're very bullish on well into the next year, Irene.

Irene Nattel

That's great. Thank you. And then just sort of continuing on the plant. I mean it's really interesting to see the strength in those core leading products, which tend to be a little bit niche here. But given sort of your expertise in the whole sort of CPG space, is there a way to kind of sort of not quite tip it, but kind of move those so that they have somewhat greater or somewhat broader appeal to really build on this sort of your very strong shares in that element of the space?

Michael McCain

First of all, I wouldn't describe them, Irene, as niche-y. It's the hot dog space. It's cooked sausage. It's roasts. There's a range of products in those categories. We have very broad presence in those. It includes the cheese line, the dairy line—non-dairy, I should say, that Curtis referred to.

So I wouldn't describe them as niche-y. They're just not the fresh segment in the meat case, which has become super competitive. And that's why we are investing in differentiation strategies in the fresh case. And we think that, over time, those differentiation strategies that emerged in the back half of 2020 in that subsegment will have a positive effect on performance in due course.

The only category that is super high growth and very lucrative, and we're investing in capacity that might be a little more niche-y, as to your description, is tempeh. And we've got a very large share of tempeh, and we're investing in advanced manufacturing capacity and capabilities in the investment in Indiana to be able to support that growth.

We are innovating in those core categories, as Curtis outlined, in addition to investing in our brand differentiation in the new fresh meat case categories that we've described. So I don't know if that answers your question specifically, but I think we see opportunities for growth in both.

Irene Nattel

Yes. That’s great. Thank you.

Operator

Thank you. Your next question comes from Mark Petrie. Please go ahead.

Mark Petrie — CIBC World Markets

Hey. Good morning.

Michael McCain

Good morning, Mark.

Mark Petrie

Just following up on the plant business, I understand you took price increases through 2020. But as you mentioned or we’ve seen, there’s competition in the fresh category. We’ve seen price reductions from some of your competitors. I guess in that context, can you just talk about the steps that are required to improve gross margin there? I know it’s a multi-layered sort of approach with regards to innovation and brand renovation and also manufacturing scale, but could you just help us understand sort of the importance of those various drivers and how you expect that to materialize? Maybe not necessarily 2021, but even 2022?

Michael McCain

The one item that’s a core driver that you didn’t list, Mark, which is probably the number one over time, is stability. When you’re managing a business that is kind of stable and predictable, you can manage it for margin and for consistency in margin. These categories and the activities here are anything but stable. When you add the impact of COVID, you add the impact of new competitive entrants, the cost of starting up and maintaining high growth rates in critical categories, the cost of relaunching brands, which was a very significant one in the last quarter, ultimately, what will drive the consistency of that margin will be stability and more than any of the other—dramatically more than any of the other levers that you referred to.

Curtis, do you want to add some colour to that?

Curtis Frank

Yeah. Sure, Michael. I think what you saw in the fourth quarter, Mark, was a combination of transitory or short-term issues related to the impact of instability, and stability certainly will be our friend over the long term. Those are things like the ongoing renovation costs that we're experiencing, building capacity out ahead of the potential that we see to grow significantly over the next short little while. And then, of course, COVID costs and higher freight and storage costs, which tailed off actually in freight and storage, I think really importantly, near the end of the quarter. And we think we've made significant headway there as well.

So stability—I think Michael's point is spot on—will be favourable to us as time progresses, but that will play out over the long term.

Mark Petrie

And do you think that stability could be reasonably expected by 2022? Or do you think it's going to be a sort of more multiyear kind of progression?

Michael McCain

No. The short answer to that, Mark, is no. We're focused. It's important in the business model to understand what we are trying to accomplish. We pay attention. We're not money-wasters. It's not our nature to be money-wasters. But we are focused on driving the brands, the brand position, the growth rate, and the model here of high-revenue growth over a longer period of time.

I do not expect stability in that gross margin in 2021 or 2022. That doesn't necessarily mean bad performance or a bad number. It means highly unpredictable, to me. And so I just want to make sure that we're super clear on what those expectations are in this situation.

We have a model in plant-based business focused on revenue growth and terminal value. And we're going to be completely—we've always been extraordinarily disciplined in our approach to financial decisions, strategic decisions, operational decisions.

We're investing our own money. This is not some unidentified shareholder capital that is being blown out the door. It's our money, along with all of our shareholders, and we're very disciplined about the execution of that. But the model in this category to succeed is focused on revenue growth, brands, long-term market position, terminal value, and not volatility of gross margins in the short term. And that's the nature of this business model.

Mark Petrie

Yeah. Understood. Okay. And just pivoting to a business that is showing stability, great progress, obviously, in the Meat Protein. Could you just clarify how you expect the 14 percent to 16 percent margin target to materialize in 2022 just like from a timing perspective? And I think you've said sort of low end of the range.

And then separate but related, how does poultry kind of contribute to that? Also, sort of timing and magnitude? Thanks.

Michael McCain

Well, the most important new news, I think, in the entire year and quarter and for all of our stakeholders is the insight that now 20 percent of the entire Maple Leaf portfolio, that's just under $1 billion in revenue, is in two strategic categories, sustainable meat at over $600 million and the balance in plant protein, that have a three-year CAGR of 25 percent. We've said consistently that our growth in sustainable meat would drive top-line growth and margin, and it is.

We've made significant progress towards the 14 percent to 16 percent target. We're within spitting distance of that, actually, in 2020. We expect to make further progress in 2021, and we expect to hit the zone, as we said a year-and-a-half ago or a year, year-and-a-half ago, likely the lower end of that zone in 2022.

Having said that, when we hit the lower end of that zone in 2022, please know that there's still another 200 basis points beyond that as soon as the poultry plant starts up in London. We have over $400 million of capital on the balance sheet today, which is not delivering a single dollar. It's construction capital. And that construction capital, by the time 2022 rolls around, will be over $700 million for that one asset alone. And within 12, 18 months of start-up, an additional, on top of that, 200 basis points of return.

So are we confident in the 14 percent to 16 percent? Yes. It will be driven by sustainable meat, the benefits of our brand growth, which we began in 2017, our commitment to our cost culture, other investments that we've been making along the way, and the poultry investment will be over and above that in 2023.

So it gives us a fairly high level of optimism, Mark, in the future of our meat protein business over the next few years, and we're pretty excited about that. I actually feel like it's a great testament to the perseverance of being disciplined financially and strategically in this business.

Did I answer the question? I think I did, but I'm not sure. I hope I did.

Mark Petrie

Yeah. Yeah. That was great, Michael. Thank you very much. Appreciate it and all the best.

Michael McCain

Okay. Cheers.

Curtis Frank

Thank you. Same to you.

Operator

The next question comes from Michael Van Aelst. Please go ahead.

Michael McCain

Hello, Michael. How are you?

Michael Van Aelst — TD Securities

Good. Good morning. How are you?

Michael McCain

I'm good. You staying safe?

Michael Van Aelst

Trying to. Yeah. Okay. So the meat business again, I wanted to get back onto that because, obviously, doing very well on that front. And I guess, what stood out to me in your outlook was that you're still expecting mid-to-high single-digit sales in 2021, which is quite impressive, I would think, considering that in 2020, at least initially, you got a benefit from the retail shift during early stages of COVID. So can you talk to where you think the biggest sources are? And how you're going to overcome potential shift back into foodservice, which might be a slight negative?

Michael McCain

The channel shift, retail foodservice was a very—was not a huge contributor here. I would just go back to the momentum of that insight of 20 percent of our revenue today in two categories, in the

Meat Protein business in one category, over $600 million of sales that has the strategic positioning, the competitive advantage, and the growth rate that that category has for us.

It drives that growth rate in both Canada and the United States because we have strategic advantage in our position in the US marketplace, which underpins that growth.

So to extrapolate that with any kind of assumptions in the next few years would contribute to the growth rates that we're aspiring to quite comfortably.

Michael Van Aelst

Okay. And the price increases you took to mitigate inflation, can you give us any kind of sense or colour as to the size, like the magnitude? And then roughly when they became effective in your numbers?

Michael McCain

Yeah. Curtis, do you want to take that one? Curtis, you might be on mute. Curtis may be on mute or something happened technically. But basically, our approach to the pricing adjustments that are made in—that took effect in early part of Q4 as part of our annual rhythm, Michael, our purpose to essentially offset inflation.

Curtis Frank

Sorry. Can you hear me, Michael?

Michael McCain

I can now, Curtis. I'll just finish this response, and then you can weigh in.

Curtis Frank

Hello?

Michael McCain

It was purposed to offsetting—

Curtis Frank

Sorry, Michael. The pricing that we took, in case you didn't hear me there—I apologize—was initiated early in Q4 and played out throughout the early parts of the fourth quarter. The inflationary components included labour and the structural items related to COVID-19, and we believe those will carry through, obviously, into 2021. So hopefully, you were able to hear me there okay. Sorry, I just had some technology challenges.

Michael Van Aelst

I'm sorry. Was that in like the 2 percent to 3 percent range? Or was it more material?

Michael McCain

Yes. It was in that range, Michael. I think Curtis is having some technology challenges here at the moment. But yes.

Michael Van Aelst

Okay.

Michael McCain

It was in that 2 percent to 3 percent range. It was not much beyond that.

Michael Van Aelst

Okay. And then COVID costs, where do you expect them to be? I know it's a bit of a crystal ball question, but where do you expect them to be in Q1, I guess, and just probably better visibility right now? And then for 2021?

Michael McCain

Our intent is not to continue factoring out the COVID costs on a quarter-to-quarter basis, Michael, largely because we believe we're at a structural level for the foreseeable future. And we've just embedded that in our operating costs, and we've reflected it in our pricing along with everybody else in the segment.

So this is kind of the new normal, and therefore, we're not going to continue isolating those costs.

Michael Van Aelst

So that full $15 million—that $15 million is the structural level?

Michael McCain

I think they'll likely be a little less than they were in the fourth quarter. But financially, it won't be a material item to call out—

Michael Van Aelst

Okay.

Michael McCain

—positive or negative.

Geert Verellen

No. We've fully organized ourselves for that. I mean, it's fully included in our plan. It's totally embedded in our structural operational costs. And as we just explained, we've priced for it as well. So this is our new normal now.

Michael Van Aelst

Okay. And then do you have an idea of when your plants or when the employees in your plants will be vaccinated? Like are they closer to the front of the line, given that they're essential service employees?

Michael McCain

The indications we're getting from governments is that they will be in the next phase on a priority basis in our frontline teammates. And the likelihood of that will be in the second quarter.

Michael Van Aelst

Okay.

Michael McCain

That doesn't necessarily mitigate the protocols that we've put in place, though, that keeps people safe, but it doesn't mitigate those protocols. We intend to continue to be vigilant, even with the existence of a vaccine.

Michael Van Aelst

Thanks very much.

Operator

The next question comes from Peter Sklar. Please go ahead.

Peter Sklar — BMO Capital Markets

Good morning. Just a couple of—

Michael McCain

Good morning, Peter.

Peter Sklar

—questions. Yeah. Good morning. Just a couple of questions left. What's happening with Shelbyville? Is that still on hold? As I recall, you did some site prep, but I don't think you actually broke ground. So if you can give us an update on Shelbyville and what your capacity plans are for the plant-based.

Michael McCain

Geert, do you want to take that one?

Geert Verellen

Sure. Good morning, Peter. Peter, I think over the last couple of quarters, we've said that we would continue to look for capacity in our existing footprint because we believe it's the best use of our capital. We would also look for opportunistic solutions, and I think we found one in the tempeh plant that we talked to you about early January, I think it was, in Indianapolis. And with all that, I think, if you look at the capacity that we have today available, all those plants that we have available will serve our capacity needs beyond 2022.

So that gives us today a little more time to continue the thinking around what Shelby needs to represent, what Shelby needs to solve for, and we're going to take that time. So, as you said, yes, we have the land. We did some site preparation work. No construction has started, but we keep that option open at this point in time.

So we're taking our time to figuring out what that Shelbyville plant is going to look like. And in the meantime, we've found capacity solutions for one of the fastest-growing parts of our business, the tempeh category.

Peter Sklar

Okay. And then I had a question on the poultry side of the business. I see that the Schomberg plant was put to you. And I'm just a little confused. You're building this big London poultry plant. Why are you buying this plant in Schomberg? Is that just related to a previous deal when it got put to you? Or it has a different product category? Or are you more interested in acquiring quota? If you could just kind of explain what's going on there and what your strategy is.

Michael McCain

Well, the strategy, when we acquired that business, the Cericola business, Peter, was basically bird supply. And the long-term value to the business was bird supply.

We fully expect that the footprint attached to that will be utilized for value-added components of the business, particularly in some high-growth niches that we're investing in. But the underlying commercial thesis was bird supply, not footprint. And the put that was included in the original transaction was anticipated, built into the business case in the first instance, and it's played out exactly as we anticipated.

Peter Sklar

Okay. Oh. And then the last thing I wanted to ask you is, if you look at the Canadian CPI data for January, I don't have the numbers right in front of me, but I do recall that pork inflation was quite strong. Now, obviously, they're measuring at the retail level. But the amount of retail inflation we're seeing in pork, is that the inflation that the grocers are experienced because of the price you've taken? You talked about it in December. Or can there be a discrepancy between the inflation you're seeing at retail versus the pricing that you're taking with the retail channel?

Michael McCain

I think the pricing that we were referring to was in prepared meats, Peter. I think the numbers you're looking at is in fresh pork, not prepared meats. So they're two different, I think, components of the protein business that we're describing.

Globally, there's been some inflation, although it didn't play out this way in the fourth quarter, but I think there's continued expectations that it will be the case. There's global inflation in overall proteins, not just pork, but pork and other animal proteins, connected largely to a global supply shortfall connected to the ASF outbreak in China. There is one global pool of protein supplies, and China is the largest producing and consuming market in the world for pork, and they lost 50 percent of their hog production over the course of the last several years.

That has inflationary tendencies, and it's played out in the global markets for fresh pork. And I think you see that. It didn't play out so much in the fourth quarter, but I think that's the macro trend that you're seeing.

Peter Sklar

Okay. That's all I have. Thanks.

Michael McCain

Okay, Peter. Thank you.

Operator

Thank you. The next question comes from George Doumet. Please go ahead.

George Doumet — Scotiabank

Hi guys. Good morning.

Michael McCain

Hey, George. How are you?

George Doumet

Good. Thank you. I just want to talk a little bit about this new entrant in the plant protein space. Just wondering how sustainable you think that price competition is going to be. And does our 30 percent growth target for the year imply that that pricing competition subsides a little bit?

Michael McCain

It was less of a pricing competition, just a new competitive entry in the retail space in the back half of this year, which I think you're fully aware of what I'm referring to. But so it wasn't so much pricing competition as a new competitive entrant that commanded some initial share and trial and all of those things.

Our strategies, which are investing in brands for the long term, is about differentiation. That's the thesis, is differentiating our brands in that marketplace, and particularly against the two disruptive brands over the last couple of years. And I think, according to the playbook and the research, it's a super-important consumer benefit and differentiation that underpins our work. And we've aligned our packaging and our products and formulations around those brand strategies.

So will those two entrants continue? Will they still be here over the course of '21 and '22? The answer is unequivocally yes. But we're confident over time in the strategies that we launched in the back half of 2020 to differentiate our products that line up relative to those two new entrants, one new last year and the previous one.

George Doumet

Okay. Thanks for that. And I guess in the past, you guys guided for 25 percent to 30 percent gross margins at that segment. Assuming we do 30 percent growth this year, is there anything structurally impeding us from getting to those margins within our network?

Michael McCain

Where? In 2021?

George Doumet

Correct. Yeah.

Michael McCain

Stability. I don't think that we have an aspiration to be stable and predictable in our gross margins in 2021, George.

George Doumet

Okay.

Michael McCain

I mean, it goes to the observation I made for Mark. The business model is about revenue growth and terminal value. We're going to be responsible and disciplined in our financial decisions along the way. The biggest driver of that instability is the growth rates themselves and investment levels. And the definition of instability is, from our perspective, is the impact is unpredictability. It doesn't necessarily mean a bad performance. It just says it's highly unpredictable and, therefore, hard to give you some guidance on that.

But I would tell you that the business model that we're investing in is not focused on that number relative to driving revenue growth and terminal value.

George Doumet

Okay. And just one last one, if I may there, Michael, on the SG&A spending for the plant business. Is there anything that we're doing different this year versus last year in terms of how we spend those SG&A dollars?

And is there any chance at all that we spend less this year than in 2021 than we spent in 2020?

Michael McCain

I doubt it. But Curtis, maybe you could add some colour. No. Our intention is not to spend less. It's an investment level that we're confident in. Curtis, over to you.

Curtis Frank

Yeah. The intention, to Michael's point, is not to dial back the spending and investments in the brands. The focus for the year is squarely on building out the leading brand positions that we have in the category.

And the facts are, we've just completed the work to move the renovation of Lightlife and Field Roast forward. Phase 2 of the Lightlife renovation actually breaks at the end of the first quarter, so we're into Phase #2. Lightlife is now 100 percent vegan certified, non-GMO verified, and made by a carbon-neutral company. So we're quite pleased with the positioning in Lightlife around clean and simple ingredients, and we're going to be investing significantly behind completing the renovation of that brand.

Concurrently, we're accelerating our plans on Field Roast as well. And really, it's going to take to the end of Q2 until the renovation is fully behind us. It'll probably be about 75 percent done at the end of Q1 with respect to Field Roast. Again, squarely focused on new design and packaging all around flavour. And very, very pleased with where we're headed with Field Roast; Chao embedded within that.

So I think it would be fair to say that the investments we're making in SG&A should be relatively [audio gap] this year. And we're quite proud of that.

Geert Verellen

George, maybe if I could add, I think, two things. Number one, this level of spend and the consistency of spend is very consistent with the model that we hold up to ourselves in terms of 30 percent sales growth, aspiring growing into that 30 percent gross margin, and growing into the dollar spend in terms of SG&A until we get to a point where we start to leverage even more. So that's number one.

Number two is, we are not spending for the sake of spending. There's an enormous amount of pressure on the teams to make sure that we are spending where we get the best ROI for our buck. And this being a new market, that means that we try and pull and try and pull until we get the best return. And we feel comfortable with that level of spend for this year, and we've guided towards the same level broadly in line with last year.

George Doumet

Okay. Thanks for your answers. Good-bye.

Operator

The next question comes from Derek Dley. Please go ahead.

Derek Dley — Canaccord Genuity

Just a quick one for me. Just back on that comment on inflation, can you just clarify—because I think you said you saw inflation sort of soften at the end of the quarter. But just looking at lean hog prices, they've kind of spiked here to start Q1. And from other retailers and companies we cover, we're hearing that they are seeing an increase in inflation, whether that's transportation costs, labour, et cetera. So what are you guys seeing to start 2021?

Michael McCain

Yeah. It just didn't play out that way in the fourth quarter, Derek. But yeah. I completely agree with you that we're starting to see some of that coming into 2021. But fully anticipated from our perspective, and I think we've built that into our pricing expectations.

Where that plays out probably more than in the pork business, actually, is the direct correlation between the inflation in the Grain Complex and how that shows up in poultry pricing.

So there's been some pretty rapid pricing movement, but also supply contraction in the poultry market, but that plays out in 2021, not 2020.

Derek Dley

I see. Okay. No. That's helpful. And then in terms of that shift between retail and foodservice, I suppose it's probably too early to say, but have you seen any of that sort of come back or normalize? Like have you seen the foodservice business start to accelerate a little bit here?

Michael McCain

Not so much in the second wave. Curtis, do you want to maybe provide some colour on that one?

Curtis Frank

Yeah. No, actually. The answer is no. We haven't seen the foodservice channel come back at this point. We started to see some pickups, obviously, throughout the summer and as we headed into Q3. But with the onset of the second wave, the foodservice channel has taken a step backwards.

We do expect that, over the course of the year, we'll gradually start to see some normalization naturally between foodservice and retail, but that's obviously dependent on speed and efficacy of vaccinations and easing government restrictions. So I think over the course of the year, we'll start to see some normalization, but that certainly hasn't been the case so far.

Derek Dley

Okay. Thank you very much.

Operator

Thank you. There are no further questions at this time.

I will now turn the call back over to Michael McCain for closing comments.

Michael McCain

Okay. Well, thank you very much for everybody's engagement here this morning. We're super proud of how 2020 unfolded. There's no business that doesn't have some opportunities in front of it, and we've got our fair share in a few areas. But on the whole, we just feel extraordinarily proud of how 2020 unfolded for us in a once-in-a-generation year. And mostly, of all that, I'm super proud of the team that I have the privilege of working shoulder to shoulder with.

And so I look forward to updating you in the next quarter. And we have a big agenda for 2021, and highly confident in the execution that this team as demonstrated this past year. And we'll look forward to keeping you posted on how that unfolds over the course of the coming year.

So, thank you for your time this morning and look forward to visiting in the next quarter.

Thank you, Operator.

Operator

Thank you. Ladies and gentlemen, this concludes your conference call for today. We thank you for participating, and we ask that you please disconnect your lines at this time. Enjoy the rest of your day.