SUPPLY CHAIN BASICS:

The Dynamics of Change in the U.S. Food Marketing Environment

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SUPPLY CHAIN BASICS:

The Dynamics of Change in the U.S. Food Marketing Environment

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New Ways in Food Marketing

The growing retail desire for exclusive and specialized food products offers new marketing opportunities for small and medium-sized food suppliers that understand the new world of food merchandising and are capable of delivering food products that satisfy commercial requirements for quality, innovation, and value. This document provides an overview of the changing retail landscape and identifies some of the characteristics associated with successful food retailing. It is designed to help smaller scale food producers and processors develop profitable business strategies and identify customers likely to appreciate their unique products.

Smaller niche-market food producers have good reason to be optimistic in today's marketplace. Increased demand for specialty food products—and consumers' willingness to visit different retailers to get them—is creating new marketing opportunities for food producers and processors that can offer innovative merchandise designed to meet the specific needs and preferences of particular consumer segments. Several of today's most highly profitable retail supermarket chains—typically, privately held firms that operate relatively small numbers of stores—have succeeded because of their ability to closely match their food product offerings to the specific needs of their customer base. Such firms offer promising marketing opportunities to small- and medium-sized food suppliers who can meet their basic product requirements.

Furthermore, the nature of business transactions across the U.S. food supply chain is rapidly being transformed. A natural competitive tension between food buyers and sellers that characterized business relationships appears to be evolving toward a new paradigm of cooperation, encouraging retail businesses to reconsider their traditional roles and adjust their practices to accommodate this changing business climate. Brian Silbermann, president of the Produce Marketing Association, notes that only a few years ago:

- Traditional full-service supermarkets dominated the U.S. food retail landscape.
- Shippers sold to many buyers in wholesale and retail markets, and no single large buyers dominated the market.
- Retail buyers were transaction- and price-oriented, and not open to cooperative partnerships with suppliers.[1]

In today's marketing environment, however, many retail and foodservice channels compete for the consumer food dollar, and increasingly affluent and discriminating shoppers—no longer content to rely on their neighborhood supermarkets for the bulk of their grocery items—seek out products that appeal to their health, environmental, and social interests, and that suit their time-pressed lifestyle. As a result:

- The importance of national brands has receded as food retailers promote their firm's reputation through private label programs and other unique offerings.
- Retail food buyers seek to establish longer term relationships with fewer suppliers to ensure steadier pricing, supply availability, and better quality control.
- The cultural divide between the procurement and marketing sides of food retail firms is disappearing as long-term supply relationships take precedence over short-term price negotiations.

The rapid shift toward supply chain integration is also being encouraged by the growing sophistication and declining cost of technology, especially wireless

1. Derived from presentation delivered at Produce Marketing Association convention, March 2008.

technology, which enables food suppliers and retail buyers to exchange increasingly elaborate data on a cost-effective basis, and to more precisely match the availability of supplies and movement of inventory with demand requirements at all stages of distribution and marketing. (For more information, see Global Data Synchronization on page 27.)

What do these supply chain developments mean for the smaller scale producer, processor, or agricultural cooperative that wishes to sell food products to retail grocers? As the number of retail accounts declines through consolidation (see Retail Concentration on page 24) and retailers become more selective about their business partners, food suppliers must increasingly focus on producing and delivering merchandise that:

- Appeals to growing consumer desire for quality, variety, and innovation.
- Addresses the emerging needs of Asian, Hispanic, and African-American consumers.
- Helps retailers tell their customers the origin of food and the production methods used to raise it.
- Enables retailers to differentiate themselves from their competition, as with locally branded products and exclusive private label items.

Moreover, to be considered as vendors, food producers and processors must:

- Comply with the stringent requirements of a preferred vendor program or production contract in their product preparation, packaging, and quality.
- Be able to participate in real-time electronic data exchange with retail customers using compatible software.
- Use appropriate technologies, such as barcodes and radio frequency identification (RFID), to maintain quality control, enhance transaction efficiency, and reduce recording errors.

This publication addresses two major trends changing retail food marketing—a move toward differentiation as a marketing strategy and a simultaneous shift towards vertical integration between food suppliers and buyers. It examines the ramifications of these developments for the smaller scale food supplier and identifies strategies for remaining competitive in this environment.

Retail Differentiation

Traditional neighborhood supermarkets are losing their dominance of the grocery trade among consumers, especially for nonperishable items. The erosion of consumer loyalty to national brands has led buyers to patronize supercenters and discount outlets such as dollar stores, while competition from alternative retail outlets, such as natural food markets, ethnic food markets, and direct marketing venues, has further nipped away at the share of the perishables market long dominated by the supermarket sector. The one-stop shopping formula that worked so successfully for supermarkets in the past is giving way to an increasingly fragmented and diverse retail market, in which consumers are willing to seek out and patronize different outlets to satisfy their needs for value, quality, and variety. As noted by Deloitte Touche Tohmatsu's research department in March 2003:

> The differences in product and shopping preferences between young and old, rich and poor, married and single, Caucasian and ethnic, urban and exurban, are becoming greater. These consumers are looking for products and services authentic and unique to their communities. One-size-fits-all retailing just will no longer work for a growing segment of the population.[2]

Geographic proximity no longer guarantees a stable customer base for food retailers. Today's consumers are willing to shop at several stores to satisfy their grocery needs. According to a 2005 study by the Food Marketing Institute (FMI), the average household grocery shopper visited more than one store each week to shop for groceries.[3] Fewer than half (46 percent) relied almost exclusively on a full-service supermarket for their groceries. Almost one in five (19 percent) regularly purchased grocery items at supercenters and 12 percent regularly shopped for grocery items at discount stores.

Data tracked by USDA's Economic Research Service (ERS), based on ACNielsen Fresh Foods Homescan data, reveal similar trends. By 2006, only a slight majority of U.S. food expenditures took place at conventional supermarkets, compared with nearly two-thirds of food expenditures in 1986 (table 1). The greatest change in U.S. food shopper behavior is the extent to which food shoppers now rely on nonsupermarket stores as a source of grocery supplies. Compared with a minuscule 0.4% share of U.S. food sales for at-home consumption in 1986, the share of food sales for at-home consumption that took place at supercenters and wholesale club stores accounted for nearly 18 percent of all such sales in 2006. In the words of supermarket industry consultant Phil Lempert, the increasing willingness of the average U.S. shopper to patronize different food stores demonstrates that many supermarkets are "missing an opportunity to capture more consumer dollars by delivering and communicating . . . greater selection and value to their shoppers."[4]

TABLE 1. Sales of food at home by type of outlet, in percent

Outlet Type	1986	1996	2006
Conventional supermarkets	65.3	58.2	57.7
Other grocery	14.3	15.8	3.4
Specialty food stores	5.8	2.6	2.7
Supercenters and wholesale club stores	0.4	4.3	17.9
Mass merchandise stores	1.5	2.1	1.7
Convenience stores	3.3	3.0	2.9
Home deliveries/mail order	1.2	2.8	3.8
Farmers/processors/ wholesalers	2.0	1.9	0.8
Other stores	6.2	10.1	9.2

SOURCE: USDA/ERS

2. "Break it up: deconsolidation and decentralization will dictate retailing's future," Progressive Grocer, February 15, 2003, p. 50.
3. "American Grocery Shoppers Seek Quality, Value, and Convenience from Multiple Retail Formats, According to FMI's Trends 2005." FMI.
4. "Poll Reveals Consumers Are Increasingly Exploring Warehouse Clubs, Supercenters and Other Alternative Grocery Formats, But Supermarkets Remain Preferred Source of Food Purchases," FMI and SupermarketGuru.com, August 13, 2002.

Consequently, while conventional supermarkets remain the primary outlet for many high-value and perishable food products, they no longer supply the majority of nonprescription drugs, paper, household cleaning, or pet products to consumers. Supercenters now occupy an equal share of the market in many of these product categories. Warehouse club stores have also become an increasingly important outlet for grocery products, and are currently the third most important outlet for meat or poultry, breakfast cereal, and frozen foods.[5]

THE CHANGING FACE OF FOOD SHOPPING

Conventional supermarkets are store formats offering a full line of groceries, meat, and produce at average prices. They are up to 30,000 square feet in size and have at least $2 million in annual sales.

Mass merchandisers (Target, Wal-Mart) are stores that primarily sell household items, electronic goods, and clothing, but also offer packaged food products.

Supercenters (SuperTarget, Wal-Mart Supercenter) are large food, drug, and mass merchandise combination stores operating under one roof. They average more than 170,000 square feet, offer a variety of food and nonfood merchandise, and typically devote as much as 40 percent of their space to grocery items.

Warehouse stores (Food 4 Less, Super Saver) are retail/wholesale hybrids with a limited variety of products presented in a warehouse-type environment. Most items are sold at deep discounts in large packages or bulk volumes.

Wholesale clubs (Costco, Sam's Club) are warehouse stores that sell only to members. Memberships require an annual fee.

Super warehouse stores (Cub Foods, Shoppers Food & Pharmacy) are high-volume hybrids of a large traditional supermarket and a warehouse store; they typically offer a full range of service departments, quality perishables, and reduced prices.

Specialty food stores offer a more limited selection than conventional supermarkets, often specializing in organic/natural food, ethnic food, or gourmet food.

Convenience stores (7-Eleven, Quick Stop) are small variety stores with a limited selection of popular items. They usually sell items at higher prices than other stores, but offer the advantage of convenience because they are located either in residential neighborhoods or at gas stations.

Dollar stores (Dollar General, Dollar Tree, Family Dollar) have small store formats and offer food and consumable items at aggressive prices, typically in units or multiples of one dollar.

Fresh format stores (Whole Foods) emphasize perishables and offer center-store assortments—dry grocery, dairy, and frozen foods displayed in the inner aisles of the store—that differ from those of traditional retailers, especially in the area of ethnic, natural, and organic foods.

Limited-assortment stores (Aldi, Sav-A-Lot, Trader Joe's) are discount-priced grocery stores that offer a limited assortment of center-store and perishable items.

Other grocery stores generally refers to small neighborhood stores.

5. Ibid.

Trends in Retail Differentiation

How are mainstream food retailers responding to these changing consumer preferences and shopping patterns? They are differentiating themselves in two ways: by offering competitively priced private label products that meet their quality specifications and promote their firm's image, and by featuring products that target specific consumer market segments and appeal to consumers' desire for health, nutrition, variety, and convenience.

Today's food retailers are also able to take advantage of the growing capacity of technology, which enables precise monitoring of customer preferences and supply replenishment needs and permits delivery of services and products tailored to household consumers. (For more about the growing impact of technology on retail practices, see Global Data Synchronization on page 27.)

Decline of the Traditional Full-Service Supermarket

Conventional supermarkets and grocery stores have experienced steady declines in consumer demand every year since 1995, when ACNielsen began its annual survey of household shopping patterns. Between 1995 and 2004, the number of trips made by the average household each year to a supermarket or grocery store fell 25 percent, from 92 to 69 trips, and a small percentage of household consumers had stopped patronizing traditional supermarkets or grocery stores entirely by 2004 (table 2).

Much of the decline in supermarket and grocery store patronage can be attributed to a rise in consumer shopping at discount stores such as supercenters and dollar stores. The average number of visits to

TABLE 2. Changes in food store patronage among U.S. households, 1999-2004

	Percent of Households Using Channel					
Channel	1999	2000	2001	2002	2003	2004
Grocery store	100	100	100	100	100	99
Mass merchandise store	95	94	93	91	91	89
Drug store	87	86	86	86	85	84
Supercenter store	52	54	53	55	54	54
Dollar store	52	55	59	62	66	67
Warehouse store	50	49	50	52	51	51
Convenience store/Gas station	50	48	45	46	45	44

	Trips Per Year					
Channel	1999	2000	2001	2002	2003	2004
Grocery store	83	78	75	73	72	69
Mass merchandise store	26	25	23	22	21	20
Drug store	15	15	15	15	15	15
Supercenter store	15	17	18	21	25	27
Dollar store	10	10	11	12	13	13
Warehouse store	9	10	10	10	11	11
Convenience store/Gas station	13	14	15	14	15	15

SOURCE. "U.S. Consumers Continue Trend of Shopping Less Often in Traditional Grocery Stores," ACNielsen, January 18, 2005.

supercenters for groceries rose from 15 a year in 1999 to 27 a year in 2004. At the same time, dollar stores increased their penetration; more than two-thirds of surveyed households (67 percent) visited a dollar store in 2004 compared with a bare majority of households (52 percent) in 1999. Younger consumers especially are buying groceries at supercenters and discount outlets. Twenty-nine percent of survey respondents age 15–24 used a supercenter or discount outlet as their primary food store in 2004.[6]

No Slowdown in Sight for Expansion of Alternative Retail Channels

With consumers turning away from traditional supermarkets and grocery stores as primary food sources, the importance of the retail grocery channel has declined—and the decline shows no sign of abating. By 2011, non-traditional food retailers are expected to account for 40 percent of the Nation's sales of groceries and consumables, almost equal to the 43.5 percent share expected from traditional supermarkets and groceries (table 3).

TABLE 3. Projected market share, grocery and consumables, 2011

Retail Channel Format	Number of Stores	Annual Sales ($millions)	Dollar Share (in percent)
Traditional Grocery Stores	40,831	$446,024	43.5
Conventional supermarkets	27,115	382,226	37.3
Fresh format stores	981	9,815	1.0
Limited-assortment stores	3,844	25,833	2.5
Super warehouse stores	485	16,380	1.6
Other (small grocery stores)	8,405	11,770	1.1
Convenience Stores	148,131	$166,094	16.2
Convenience stores with gas stations	119,662	143,742	14.0
Convenience stores without gas stations	28,469	22,352	2.2
Non-Traditional Grocery Stores	58,074	$413,923	40.3
Wholesale club stores	1,441	84,173	8.2
Supercenters	3,264	207,958	20.3
Dollar stores	27,696	20,607	2.0
Drug stores	22,097	48,968	4.8
Mass merchandise stores	3,407	47,661	4.6
Military commissaries	170	4,555	0.4
Total All Formats	247,036	$1,026,041	100.0

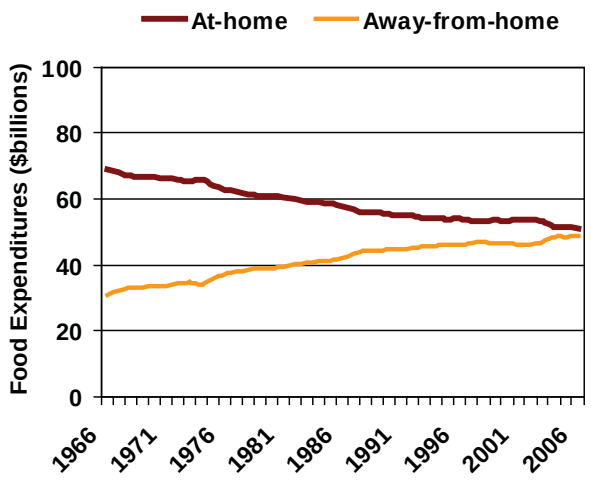
SOURCE. "The Future of Food Retailing," June 2007, Willard Bishop Consulting, Ltd.

6. "Food Retailers Offering More Takeout, Self-Scanning, Fuel Pumps, Drive-Thru Pharmacies, and Other Services fo Convenience-Driven Consumers," FMI, May 2, 2004.

Away-From-Home Food Consumption Increases at Expense of At-Home Food Preparation

The gradual rise in away-from-home food consumption is further eroding the importance of traditional groceries in the United States, leaving supermarkets and nontraditional food retailers competing for a dwindling pool of consumer food dollars. In 2006, consumers spent approximately $1.1 trillion on food consumed in the United States. Foodservice facilities supplied about $529 billion, or 48.9 percent, of this total for on-premise or immediate consumption, the third highest level in U.S. history (figure 1).

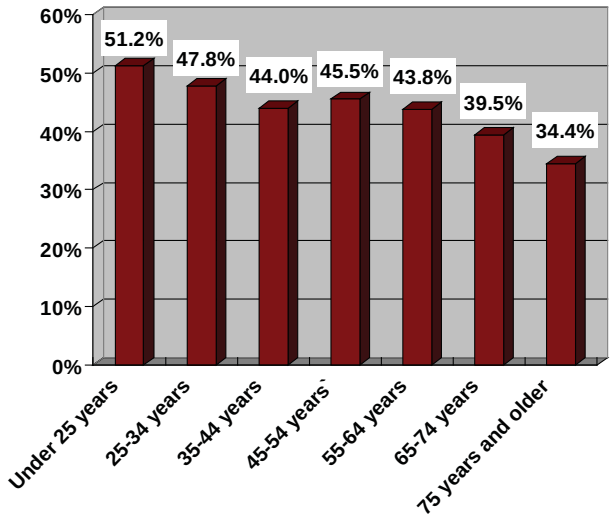
FIGURE 1. Trends in U.S. consumer expenditures for food, 1966-2006



SOURCE. Food CPI, Prices and Expenditures: Food and Alcoholic Beverages: Total Expenditures, ERS.

The tendency to spend money on food outside the home is largely inversely related to age, with the youngest consumers in the United States more likely to spend their food dollars on food consumed outside the home than any other age cohort. Consumers under 25 spend more than 50 percent of their food dollars outside the home, compared with 34 percent among consumers age 75 or greater (figure 2).

FIGURE 2. Expenditures for food consumed away from home, by age group



SOURCE. Consumer Expenditures in 2005, Bureau of Labor Statistics, U.S. Department of Labor, April 2007.

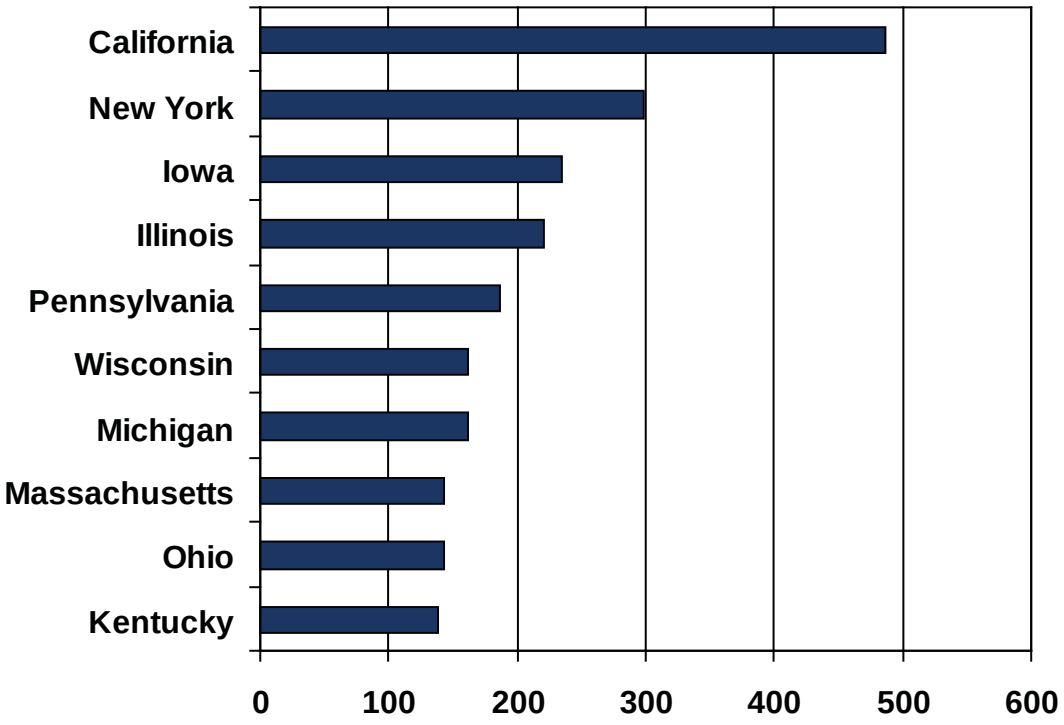
Direct-to-Consumer Marketing Outlets Gaining Traction

The popularity of direct-to-consumer marketing outlets, such as farmers markets, roadside stands, and community-supported agriculture, is another challenge to supermarket profitability. According to the 2002 Census of Agriculture, the value of direct-to-consumer food sales in the United States grew 37 percent between 1997 and 2002—from $592 million to $812 million—reflecting the enormous growth in the number and accessibility of direct-to-consumer marketing outlets, especially in urban and suburban neighborhoods. This increase has been bolstered by the growth in the number of farmers markets in

the United States—from around 1,750 in 1994 to approximately 4,475 by late 2007.[7] By the end of 2005, farmers markets in the United States were estimated to generate more than $1 billion in sales per year.[8] Furthermore, the number of community-supported agriculture (CSA) operations, in which customers purchase advance shares of a farm's production in return for regular deliveries during the growing season, has expanded from an estimated 60 operations in 1990 to approximately 1,150 operations in early 2007.[9]

The farmers market movement in the United States was initially concentrated along the West Coast and within parts of the Northeast. However, during the last few years the number of farmers markets throughout the country has increased significantly, especially in Midwestern States with a tradition of small farms, and where farms are close to population centers (figure 3). Direct-to-consumer marketing channels appear to be especially important to buyers of organic food products. According to the Organic Trade Association, about 7 percent of U.S. organic food sales in 2005 occurred through direct sales at farmers markets and

FIGURE 3. States with the most farmers markets



SOURCE. USDA Agricultural Marketing Service, September 2007

7. AMS. Data current as of September 2007.
8. *USDA Releases New Farmers Market Statistics*, AMS, Washington, DC, December 5, 2006.
9. *Robyn Van En Center for CSA resources*, Wilson College. <www.wilson.edu/csacenter>.

WHY CONSUMERS LOVE BUYING DIRECTLY FROM FARMERS

Permits them to:

- Obtain seasonal foods and other farm products at peak condition.
- Have access to varieties of farm products grown or raised for flavor, rather than tolerance of long-distance shipping.
- Receive fresher products with a longer shelf life.
- Know more about the origin of food and the methods used to produce it.
- Develop a personal relationship with local vendors, and receive more individualized or more responsive customer service.
- Potentially contribute to a reduction in fossil fuel usage by substituting locally grown food for food shipped over long distances.
- Provide additional income to family-run farms and the local economy.
- Help preserve local and regional culinary traditions.

other nonretail direct market outlets (including sales to foodservice customers).[10] In contrast, only 3.9 percent of all U.S. food sales in 2005 were made through any form of direct sale or home/mail order delivery.[11]

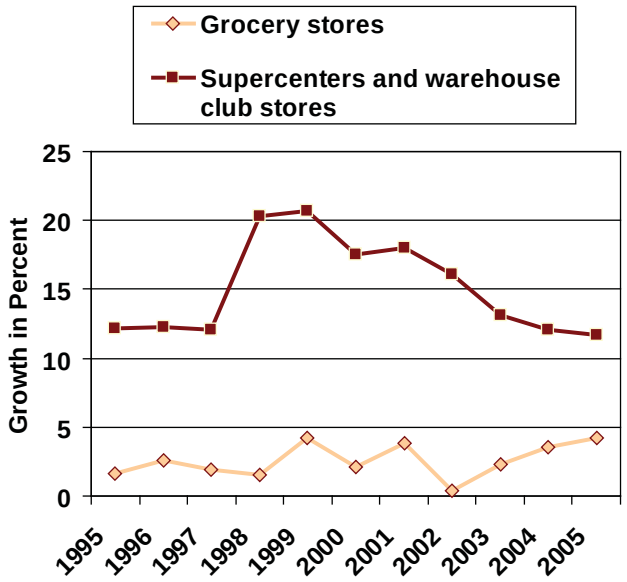
The exponential growth in access to direct marketing outlets, such as farmers markets and CSAs, throughout the country appears to have stimulated significant growth in the value of locally grown food sold to consumers. The market research firm Packaged Facts estimated in 2007 that consumer demand for locally grown food could rise from around $4 billion in 2002 to $5 billion a year by the end of 2007 and to as much as $7 billion a year by 2012, reflecting both increased consumer patronage of farmers markets and CSAs and an expanded effort by retail and foodservice firms to procure more locally grown food that appeals to consumers.[12] Indeed, the popularity of farmers markets has grown so rapidly in the United States that a recent national survey reports that 2 percent of U.S. food shoppers now say farmers markets are their primary food shopping venue.[13] In light of these developments in the marketplace, mainstream news media are giving increasingly prominent attention to the growth of the local food movement.

10. U.S. Organic Industry Overview, excerpted from the Organic Trade Association's 2006 Manufacturer Survey. <www.ota.com/pics/documents/short%20overview%20MMS.pdf>.
11. Food and Alcoholic Beverages: Total Expenditures, Food CPI, Prices and Expenditures Briefing Room, ERS <www.ers.usda.gov/briefing/cpifoodandexpenditures/Data/>.
12. *Locally Grown Foods Niche Cooks Up at $5 Billion as America Chows Down on Fresh!*, <www.packagedfacts.com/anout/release.asp?id=918>.
13. National Grocers Association/SupermarketGuru.com consumer panel survey, Fall 2003, reported in "When shoppers stray," Progressive Grocer, April 1, 2004, p.10.

Dwindling Store Loyalty Translates Into Lower Supermarket Profits

As might be expected, the steady decline in supermarket and grocery store patronage—influenced by the growing popularity of alternative retail channels and away-from-home food consumption—has contributed to sluggish sales growth in the traditional grocery sector. According to U.S. Census Bureau statistics, overall sales growth at conventional supermarkets and grocery stores averaged 2.4 percent a year between 1995 and 2005, compared with 16.6 percent a year at supercenters and warehouse club stores during the same period (figure 4).

FIGURE 4. Annual retail sales growth, grocery stores versus supercenters and warehouse club stores, 1995-2005



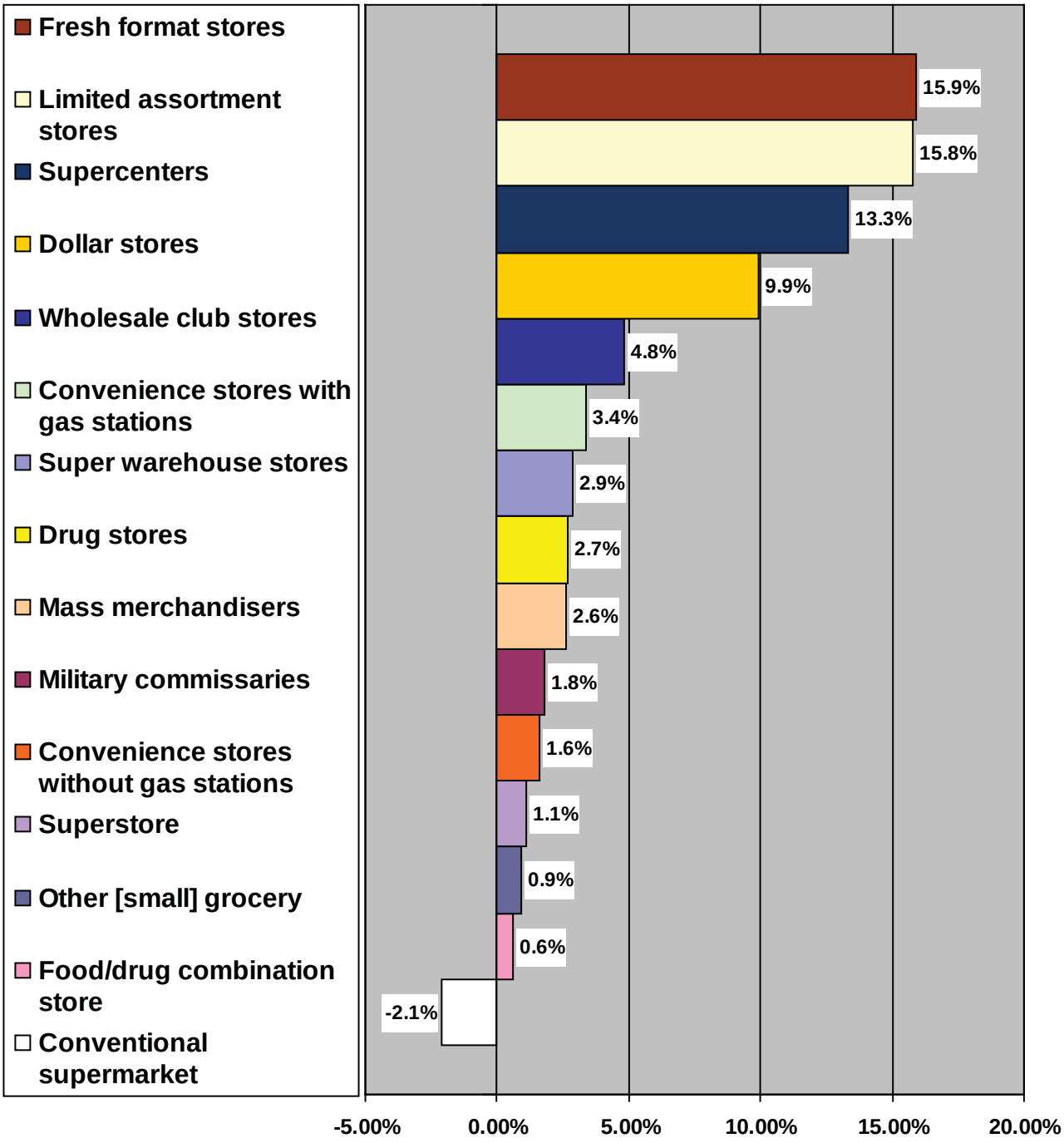
SOURCE. "Estimated Annual Retail and Food Service Sales by Kind of Business, 1992 Through 2005," Annual Benchmark Report for Retail Trade and Food Services: January 1992 Through February 2006, U.S. Census Bureau, March 2006.

Furthermore, when deflated by the food price index, it appears that recent sales growth in the U.S. supermarket sector has struggled to keep up with the rate of U.S. population growth, which currently averages just under 0.9 percent per year.[14] Although U.S. supermarket sales rose 4.6 percent in 2006 over 2005 levels, the industry's highest growth rate in 6 years, the Food Institute reported that "real" growth was actually 1.82 percent once inflation was taken into account.[15, 16] These figures suggest that even under unusually favorable circumstances, the growth of the supermarket industry is barely keeping pace with the growth in U.S. population.

Nor does this 2006 sales growth figure reflect the impact of hefty food price inflation during 2007, accentuated by energy price hikes and competing demands for agricultural commodities. By August 2007, the Consumer Price Index (CPI) for food had already risen 4.3 percent above the comparable level in 2006, and the ERS predicted that, by the end of 2007, the food CPI will have risen 3.5 to 4.5 percent over the previous year's level.[17] Moreover, the steepest rise in food prices is expected to take place among food items consumed at home, marking a significant departure from recent trends. Food-at-home prices are forecast to increase 3.5 to 4.5 percent between 2006 and 2007, well above the rise of 1.7 percent in food-at-home prices between 2005 and 2006.[18] In view of these developments, it's not surprising that many food retailers are expected to face sluggish growth over the next few years, with traditional supermarkets continuing to lag well behind food retailers with highly specialized formats, such as fresh format stores, limited assortment stores, and supercenters (figure 5).

14. Based on 2007 U.S. population growth forecasts published in The World Factbook, Central Intelligence Agency. <https://www.cia.gov/library/publications/the-world-factbook/print/us.html>.
15. "Independent and Large Chain Retailers Lead Strong Sales Growth; Energy and Credit Card Costs Top Industry Issue Agenda, According to 'Food Retailing Industry Speaks 2006', FMI , May 7, 2006.
16. "Grocers' real sales growth at 6-year high in '06", Food Institute Report, January 29, 2007.
17. "Food CPI, Prices, and Expenditures: Analysis and Forecasts of the CPI for Food," ERS. <http://www.ers.usda.gov/Briefing/CPIFoodAndExpenditures/consumerpriceindex.htm>.
18. Ibid.

FIGURE 5. Expected compound annual sales growth rate: 2005-2010 (grocery and consumables)



SOURCE. "Sales Growth for Grocery Retailers Not Expected to Keep Pace with Inflation," Food Institute, <www.foodinstitute.com/pressreleases.cfm>. Projections based on Willard Bishop and ERS forecasts.

Succeeding in the "Brave New World" of Food Marketing

Although the near-term prospects for the U.S. supermarket industry seem somewhat bleak overall, some individual retailers have fared extremely well—a phenomenon easily obscured by looking at average sales alone. In 2004, the top 25 percent of performers in the supermarket industry increased sales by more than 7 percent and the top 50 percent of performers posted sales gains of nearly 5 percent. In contrast, the average sales gain for the bottom 25 percent of supermarket firms was only 0.5 percent.[19]

Many supermarket chains that seem to be staying "ahead of the curve" are those that successfully differentiate themselves from their competitors by offering products and services that appeal to specific segments of consumers, especially if they adopt a cautious approach to store expansion and financial leverage. These retail businesses are astutely responding to a general movement within the United States toward social fragmentation and deconsolidation. According to one industry analyst, in "virtually every [. . .] aspect of society, polarization is occurring, made manifest in various ways:

- The widely divergent voting blocs in the Nation
- A divergence of lifestyles between married and single people
- Geographical choices—leaving suburbs for cities on one hand, and suburbs for exurbs on the other
- A growing distinction between affluent and impoverished
- An increasing separation of young from old
- An increasing separation of ethnic groups from each other, and from the mainstream
- An increasing fragmentation of information-delivery means."[20]

Bigger Is Not Always Better.

Supermarket chains with a relatively small number of stores can compete successfully with larger chains by using innovative merchandising techniques and building reputations for quality and service. For example:

- In 2004, Raley's and Wegmans Food Market ranked among the largest 25 U.S. food retailers in annual sales. This ranking is especially impressive when you consider that Raley's operated only 137 stores and Wegmans Food Market 67 stores at the time of the report, compared with an average of 853 stores among other supermarket firms listed in the top 25.
- By 2004, Whole Foods Market, a national retailer of natural and organic foods, had climbed into the top 20 list of largest U.S. food retailers, with annual sales of $3.9 billion, even though the firm operated only 166 retail stores at the time. Chief Executive Officer John Mackey reported that 2004 had been the firm's best year to date, with a 14.9-percent increase in same-store sales growth contributing to an overall 23-percent increase in sales over 2003 levels.
- In 2006, Wegmans Food Market, Publix, and Raley's—all privately held companies—were rated by Consumer Reports magazine the best conventional supermarket chains in the United States.[24]

19. "FMI Speaks—Executive Summary: Measuring a Complex Year," FMI, May 2005.
20. "Excerpted from speech delivered by Carl Steidtmann, Chief Economist and Director of Consumer Business Research with Deloitte Touche Tohmatsu at the FMI Midwinter Executive Conference, January 2005, reprinted in "Trends Indicated Growing Opportunity for Niche Retailers," Supermarket News, January 31, 2005.
21. "Wal-Mart dominates," Rod Smith, Feedstuffs, July 11, 2005, p. 7.
22. Ibid.
23. Supermarket News, April 5, 2005.
24. "Win at the grocery game: How to shop smarter, cheaper and faster, Consumer Reports, October 2006. <www.consumerreports.org/cro/money/shopping/where-to-buy/supermarkets-10-06/overview/1006_supermarkets_ov1.htm>.

Another indicator that "bigger is not always better" is that supermarket firms with relatively small annual sales volumes are doing better financially than many of their larger peers. In FY 2003, for example, food retailers with annual sales under $100 million posted 6-year highs in net profits (1.45 percent) and return on equity (20.38 percent), compared with an average net profit for the industry of 0.88 percent, and a return on equity of 9.4 percent.[25]

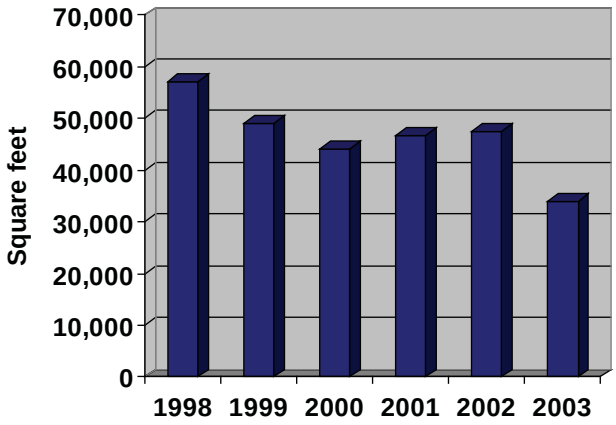
Importance of Target Marketing

Recent figures on new supermarket store construction reveal the growing importance of target marketing among supermarket firms. Stores catering specifically to consumers of ethnic, natural, and high-end "gourmet" foods account for a growing percentage of food retail outlets. According to the FMI, 14.5 percent of surveyed food retail firms opened at least one niche-focused store in 2005. Of these, 44 percent had ethnic formats, predominantly oriented toward the Hispanic consumer market. Retailers were also building natural and organic stores for consumers concerned about health and wellness and gourmet outlets for high-income shoppers.[26]

As stocking a broad range of products gives way to increased emphasis on target marketing, the average size of new supermarkets in the United States also has declined substantially in recent years (figure 6). The average size of new supermarkets fell from 47,500 square feet in 2002 to 34,000 square feet in 2003, the first time in 10 years that it had fallen below 40,000 square feet.

Given expectations for flat growth in the traditional grocery sector during the next few years, it comes as little surprise that food retailers are attempting to capture market share in the few sectors with prospects for expansion: organic foods, gourmet foods, and various ethnic foods. A brief glance at prospects in each sector reveals why consumers of organic/natural, gourmet, and ethnic foods attract such disproportionate attention from U.S. food retailers.

FIGURE 6. Average size of new supermarket stores in the United States



SOURCE. FMI

Growth of Organic Food Markets

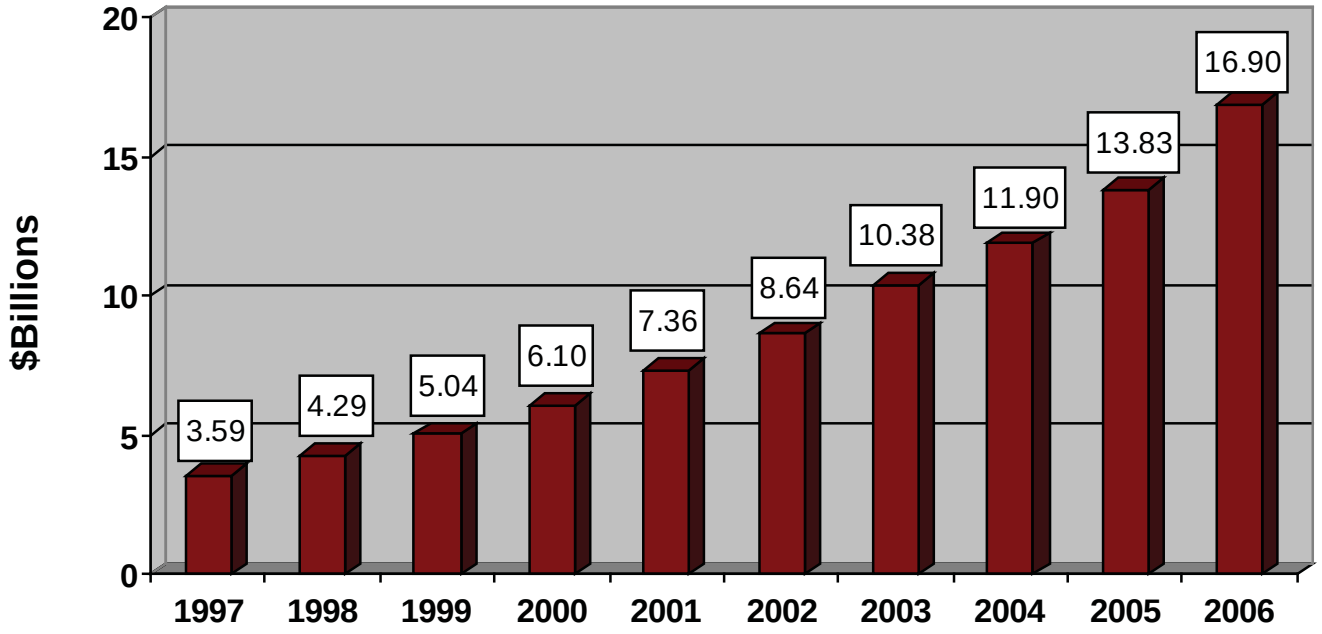
Despite several consecutive years of aggressive sales growth in recent years (figure 7), the organic food market is expected to continue expanding rapidly, rising an average of 16 percent per year between 2005 and 2010, compared with a projected annual growth

25. "Smaller Food Retailers More Profitable Than Larger Chains Last Year," from on-line edition of Progressive Grocer, March 17, 2005.
26. "FMI Facts About Store Development 2006: New Supermarkets Deliver a Diverse Mix of Fresh Foods," Food Export, March 2, 2007. <http://www.allbusiness.com/agriculture-forestry-fishing/4437834-1.html>.

of 2–3 percent in the conventional food sector.[27] With organic food sales currently representing less than 3 percent of the U.S. food market, consumer demand for organic foods appears far from saturated.[28] A slight slowdown in growth rates for well-established product categories such as fresh produce (about 39 percent of the organic food market) is likely to be overshadowed by a growth surge in such less-well-established product categories as meat, poultry, dairy, and sauces/condiments.[29]

The Hartman Group, a market research firm that investigates trends in the natural product marketplace, reported that two-thirds of U.S. consumers purchased organic food and beverages on an occasional basis in 2004 and that 30 percent purchased them on a regular (daily or weekly) basis.[30] Additionally, organic food purchases were motivated primarily by health and nutritional concerns, most specifically an interest in avoiding pesticides, chemicals, antibiotics, and growth hormones. However, the motivation behind organic food and beverage purchases becomes more complex

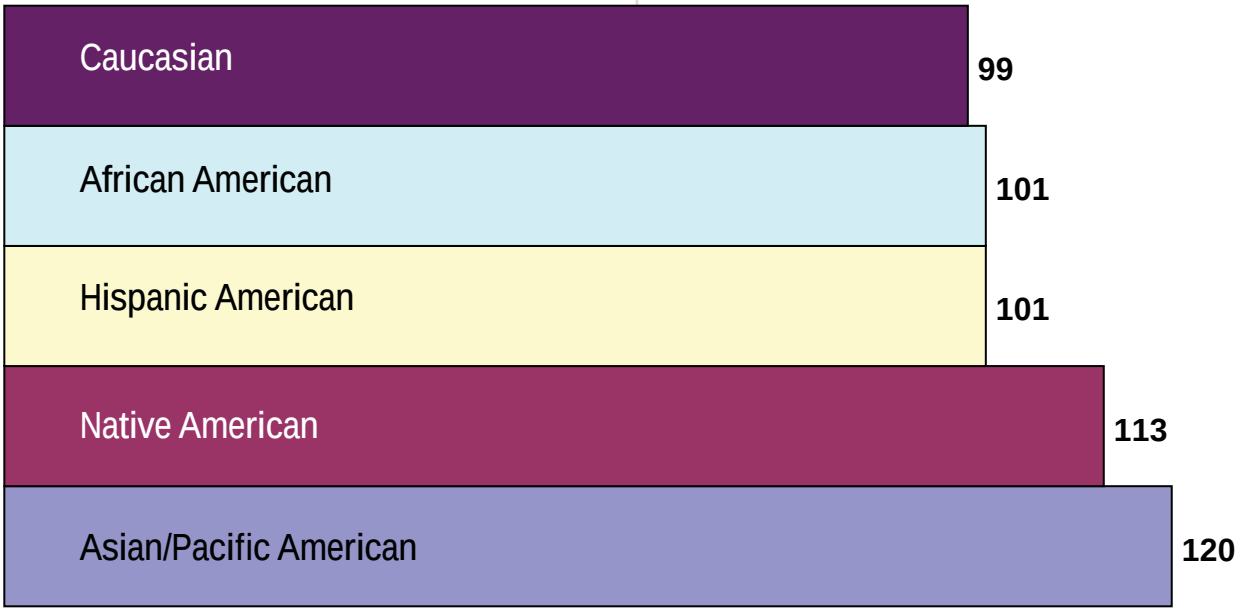
FIGURE 7. Annual growth in U.S. organic food sales, 1997–2006



SOURCE. "U.S. Organic Industry Overview," Organic Trade Association 2006 Manufacturer Survey. <http://www.ota.com/pics/documents/short%20overview%20MMS.pdf>

27. Progressive Grocer, March 1, 2005, reporting projections by the market research firm Packaged Facts.
28. "Organic Sales Continue to Grow at a Steady Pace," Organic Trade Association, May 7, 2006.
29. "U.S. Organic Industry Overview," Organic Trade Association 2006 Manufacturer Survey. <http://www.ota.com/pics/documents/short%20overview%20MMS.pdf>.

FIGURE 8. Organic ethnic purchase index



SOURCE. Organic Food & Beverage Trends 2004: Lifestyle, Language and Category Adoption," The Hartman Group, Summer 2004, pp. 26–27.

as the level of organic patronage increases. Among the most dedicated "core" organic consumers (accounting for 21 percent of organic food and beverage shoppers), most prefer to support brands that "are not owned by conglomerates" and that have "an authentic story behind their creation."[31] The interest of core organic consumers in learning where their food comes from and in supporting small businesses creates unique opportunities for those food producers and processors that can satisfy this interest.

In addition, the organic food market can expect to receive a boost from demographic trends as increased buying power among Hispanic-Americans, Asian-Americans, and African-Americans should further help promote consumer demand.[32] Recent analysis of organic food patronage by the Hartman Group indicates that Caucasian consumers in the United States as a whole are less likely than other racial/ethnic groups to purchase organic foods on a regular basis.

Growth of Gourmet Markets

According to the market research firm Packaged Facts, the U.S. market for high-end "gourmet" foods and beverages is currently worth $41.2 billion and can be expected to reach $62 billion by 2009.[33] Nearly 20 percent of surveyed food shoppers report they try to eat gourmet food "whenever they can."[34] Several factors contribute to the growing demand for gourmet foods,

30. Ibid., pp. 5–6.
31. Ibid., p. 7.
32. Organic Food & Beverage Trends 2004: Lifestyle, Language and Category Adoption," The Hartman Group, Summer 2004, pp. 26–27.
33. "Nearly 20% of Americans Can be Considered 'Gourmet' Consumers, New Report Finds," PR Newswire, August 18, 2005.
34. Ibid.

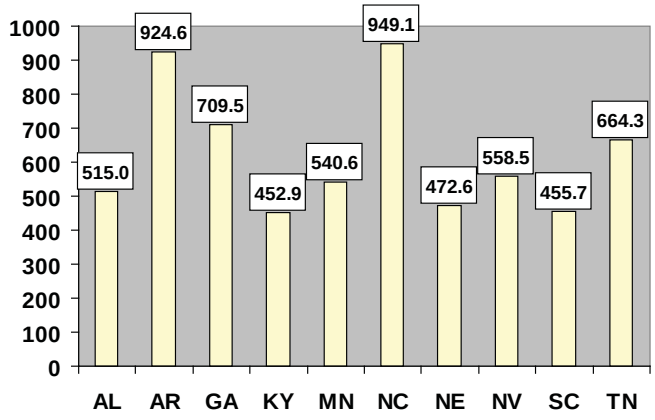
including a greater commitment to the category on the part of mainstream food marketers, the expanding availability of gourmet food products (especially those in convenient, ready-to-eat formats), and a growing synergy between the natural and gourmet foods industries. From Packaged Facts:

> More gourmet products are using natural and organic ingredients (and appealing to consumers' social consciences by offering products that are good for the environment and for the workers who produce them), and more natural foods retailers are carrying upscale, gourmet food and beverage items that meet their quality standards.[35]

Changing Ethnic Demographics

Another development triggering profound changes in grocery merchandising is the expanding contribution of Hispanic, Asian, and African-American consumers to the market, reflecting geographic shifts, population growth, and increasing affluence among these segments of the consumer population. As the United States becomes more ethnically diverse, the relative importance of Hispanic, Asian, and African-American purchasing power has grown enormously, changing the nature of consumer demand in many localities. Within the 5-year period 1999–2004, the buying power, or total amount of personal income available for spending on goods and services by Hispanic, Asian, and African-American residents increased by several hundred percent in many States[36] (figures 9-11):

FIGURE 9. Percentage increase in Hispanic buying power, by State, 1999-2004 (ten fastest growing States)



35. Ibid.
36. Source, figures 7–9: "Fastest-growing consumer markets in 1999-2004," Progressive Grocer, February 15, 2005, citing the Selig Center for Economic Growth, Terry College of Business, University of Georgia.

FIGURE 10. Percentage increase in Asian buying power, by State, 1999-2004 (ten fastest growing States)

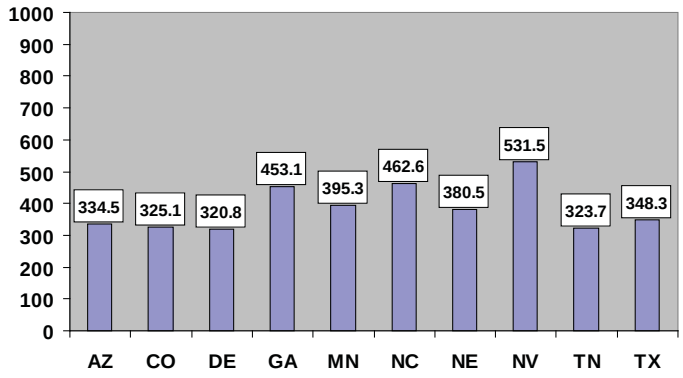
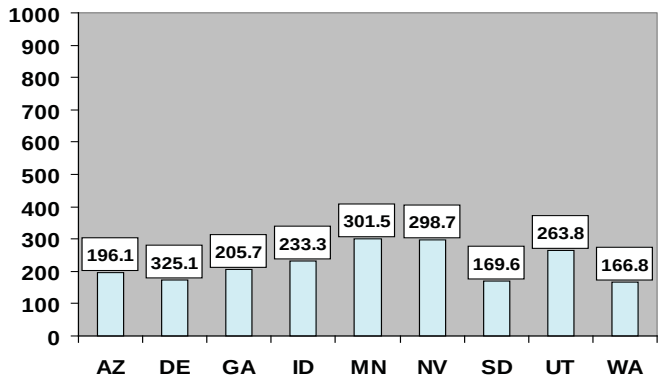


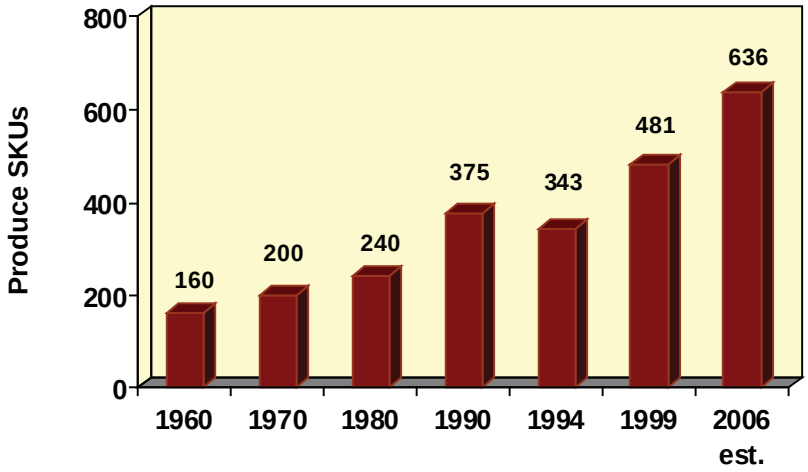
FIGURE 11. Percentage increase in African-American buying power, by State, 1999-2004 (ten fastest growing States)



New Market Opportunities

In many ways, today's retail marketplace offers great opportunities for a smaller food producer able to supply steady volumes of high-quality, consumer-ready products to retail markets. To stay competitive in today's highly concentrated grocery sector, food retailers are offering an expanded array of highly differentiated and customized products to meet the needs of their increasingly diverse and discriminating customer base. The average number of stock keeping units (SKUs) in produce departments, for example, more than doubled between 1980 and 2006 (figure 12).[37]

FIGURE 12. Average number of produce SKUs offered by retail outlets



SOURCE. FreshTrack 2001, Cornell University

37. FreshTrack 2001, Cornell University (Includes only firms with annual sales more than $1.5 billion).

Freshness is increasingly important to consumers. Growing exposure to farmers markets has led them to expect merchandise of comparable freshness on supermarket shelves, giving local suppliers a competitive advantage.

A firm's size could also determine the types of goods it prefers to buy from smaller suppliers. Research by USDA's Agricultural Marketing Service (AMS) shows independent grocers and regional supermarket chains often prefer to feature branded products from local suppliers as a way to promote their connections to their communities. Offering distinctive local merchandise allows them to differentiate themselves from larger competitors.[38] On the other hand, to the extent that national and large regional supermarket chains are motivated to buy products from smaller scale suppliers at all, they usually do so from a desire to purchase products with specific or exclusive quality attributes, regardless of geographic origin—including items that can be sold under private labels. For smaller producers, private label programs can generate steady business with large customers and eliminate some of the expense of promoting, advertising, and packaging branded merchandise.

PROMOTING LOCAL ORIGIN: CASE STUDY #1: APPALACHIAN HARVEST

Two regional supermarket chains that have been leaders in showcasing local food are headquartered in Virginia: Ukrop's Super Markets, a 30-store chain based in Richmond with outlets in central Virginia, and Food City, a privately held, family-owned supermarket chain based in Abington with nearly 100 stores in southwestern Virginia, northeastern Tennessee, and southeastern Kentucky. In 2000, both firms began purchasing local produce from a southwestern Virginia alliance of organic family farmers that market under the Appalachian Harvest label. About 60 growers in southwestern Virginia and eastern Tennessee now participate in the Appalachian Harvest marketing program.

Other retail customers of the Appalachian Harvest marketing collective include Ingles Supermarkets, a supermarket chain based in Asheville, N.C., and Whole Foods Market stores in the District of Columbia, Pennsylvania, and northern Virginia. Not only have these retailers eagerly embraced the opportunity to purchase local produce, but one firm (Ukrop's) was so interested in establishing a steady supply of locally grown organic produce that it helped the Appalachian Harvest network recruit former tobacco farmers to grow organic produce.[39]

Ukrop's also extended its in-store promotion of local food to include value-added food products manufactured with locally grown ingredients. In 2002, Ukrop's was the first grocery to offer in its produce department herb salad dressings from Shenandoah Growers along with national brands.[40] This Harrisonburg, VA, firm is known for its organic culinary herbs. The dressing was displayed in a stand-alone section next to a display of fresh herbs, underscoring the "freshness" of the locally manufactured product, with each bottle of dressing displaying the "Virginia's Finest" State logo.

38. *Enhancing Commercial Food Service Sales by Small Meat Processing Firms*, AMS, March 2004.
39. "Tobacco Farmers Seek Diversification after Buyout," Associated Press, February 19, 2005.
40. "Ukrop's Teams Herbs, Dressings in Produce," Supermarket News, June 3, 2002.

PROMOTING LOCAL ORIGIN: CASE STUDY #2: FAMILYFARMED.ORG

In the Chicago area, sixteen retail grocery firms, comprising a mixture of independently owned grocery stores, specialty food retailers, and regional supermarket chains, recently agreed to begin carrying FamilyFarmed.org food. This label indicates the food is grown in Midwestern States by family owned and operated farms that either are certified organic or employ similar sustainable agricultural practices. A nonprofit organization known as Sustain coordinates and recruits participants for FamilyFarmed.org. Participation allows members to:

- Post their farm's story and photo on the FamilyFarmed.org Web site <http://familyfarmed.org>.
- Participate in an annual exposition where they can market their food directly to household consumers and commercial buyers.
- Use FamilyFarmed.org labels in their product merchandising and advertising. The label effectively communicates their farms as small, locally operated, family businesses that use sustainable production methods. Members can purchase stickers featuring the FamilyFarmed.org label from Sustain at prices ranging from $25–$50 per 1,000, depending on volume.

Sustain also offers its members customized design services for boxes, bags, and other product packaging on a fee-for-service basis. The designs showcase a farm's personal story on consumer-ready packaging units. Figure 13 shows a custom-designed 5-pound bag for organic potatoes by Igl Farms of Antigo, WI. The FamilyFarmed.org label appears in the lower left-hand corner of the front of the bag. The back of the bag (not shown) features a photograph of the Igl family, a quote from the growers about the mission of their farm, a potato recipe, a Wisconsin State logo, a USDA organic seal, information about the farm's organic certifying agent, and basic nutritional information.

FIGURE 13. Promotional Materials from FamilyFarmed.org

Retail buyers not only recognize the appeal of locally grown food to their increasingly discriminating clientele, they also realize that the growing popularity of farmers markets raises expectations of freshness in supermarkets. This gives a substantial competitive advantage to local producers that can deliver high-quality seasonal produce. Richard Draeger, vice president of Draeger's Supermarkets, a three-store supermarket chain based in Menlo Park, CA, recently observed to a Supermarket News reporter that "regular customers expect nothing less than ripe, ready-to-eat produce" because they've shopped at farmers markets.[41]

41. "Produce Profitability Depends on Freshness," Lynne Miller, *Supermarket News*, April 18, 2005, p. 50.

MEETING RETAIL DEMAND FOR LOCALLY GROWN FOOD: A CASE STUDY OF BIG RIVER FOODS

Big River Foods is the newest program of the Minnesota Food Association, a nonprofit organization based near Stillwater, MN, whose mission is to build a more sustainable food system. Big River Foods is closely linked with the Minnesota Food Association's New Immigrant Agriculture Project (NIAP), established in 1999 to help immigrant and other limited-resource farmers learn sustainable agriculture methods and farm business management. Since its inception, more than 250 immigrants (primarily Southeast Asian Hmong and Latinos) have benefited from these training sessions. Big River Foods (BRF) became a natural outgrowth of NAIP as a means of meeting the growing marketing needs of a number of the more commercially oriented immigrant farmers, many of whom were looking for marketing outlets beyond farmers markets. BRF is set up as a "training distribution company" that combines brokering functions and transportation logistics with on-farm production and post-harvest handling training.

BRF is well positioned to tap into the growing demand by supermarkets and other retail outlets to provide their customers with locally grown and sustainably produced fresh fruits and vegetables. In only its first year of operations, BRF has successfully brokered deals and distributed to one regional and two local supermarket chains operating in Minneapolis/St. Paul and the surrounding area. BRF sells several tomato varieties (grape, slicer, heirloom) to Lunds and Byerly's (a high-end supermarket with 21 locations); Kowalski's Market (a supermarket chain with eight locations and a focus on organic and natural foods); and Cub Foods (a regional supermarket chain with 84 locations in the Midwest). It also sells heirloom and grape tomatoes to the Wedge in Minneapolis, one of the largest food co-ops in the country, and green peppers to the restaurant chain Chipotle.

BRF is tapping into only a fraction of this retail demand, currently working with five family farm operations, most of which are growing on less than 2 acres of land. BRF entered the distribution business knowing that demand for locally grown food would be higher than its production capabilities. Nonetheless, it has had a successful start by sticking to some core marketing principles:

- Produce for the market rather than trying to market what you produce. BRF reached out to numerous retail buyers to find out what products were in highest demand. By matching its own production capacity to retail buyer needs, BRF saw a lucrative market for selling tomatoes and green peppers.

- Develop a brand identity that reflects the core values of the company and appeals to what consumers want in a product. The BRF logo states simply that its products are "Fresh. Local. Honest."

- Live by the standards espoused in your brand. For BRF, this means ensuring its farmers are certified to use good agricultural practices (GAPs), carry liability insurance, and grow their produce using ecologically sound practices.

- Ensure credibility with retail buyers by knowing everything about the products you are selling. BRF decided to limit sales to tomatoes and green peppers. The BRF team knew every aspect of production and post-harvest physiology and handling for these two products. When speaking with retail buyers, BRF could confidently answer questions concerning production capacity, handling, storage, and delivery mechanisms.

- Start small and within your present capacity. With limited cleaning facilities and cold-storage capacity, tomatoes and green peppers were well-suited for BRF. Cleaning, grading, and packaging could be done on-farm, and both products could be stored in cold storage units of similar temperature. The farmers were also comfortable growing these two products at a level that met the quality standards expected from the retail buyers.

- Communication, communication, communication. Cultivating a strong relationship with a retail buyer requires constant communication. This starts by finding out how the buyer prefers to communicate, whether this is by fax, phone, or email. It then means regularly communicating with the retail buyer, from assuring the buyer that product quality and handling standards are met to updating the buyer on orders and delivery dates.

Further information on Big River Foods can be found at the Minnesota Food Association's Web site, http://www.mnfoodassociation.org

Private Label Products

Private label or store brand programs represent another potential market opportunity for smaller food producers and processors. Such programs appeal to retail buyers who seek food products with specific—and sometimes exclusive—quality attributes. Although in the past private label products had a reputation for inferiority, a 2005 report by Citigroup/Smith Barney reported that sales of private label products in the United States increased 48 percent between 1997 and 2003, compared with a 22-percent increase for branded items and 25 percent for other packaged goods.[42] The retail industry has enthusiastically adopted private label programs in recent years, with the result that, by 2007, one of every five items sold in supermarkets, drug stores, and mass merchandise stores was a private label product, accounting for more than $65 billion in sales per year.[43]

According to the market research firm Mintel, in recent years sales of private label food have outpaced other food products. Sales of the 20 best-selling categories of private label food—items such as cheese, frozen vegetables, and cookies—rose 23 percent between 1999 and 2004, while overall sales of the same product categories rose only 14 percent.[44] Consumers have generally embraced private label food products—seven out of ten consumers recently told the market research firm Packaged Facts that private label foods are as good or better than national brands.[45]

Private label products are becoming increasingly attractive to supermarket buyers for several reasons. Consumers are shopping at an ever-broader array of food stores, and are able to buy national brand products at a growing number of firms. Therefore, traditional full-service supermarkets can no longer attract customers by featuring a wide selection of national brands and depending on brand loyalty to drive sales. To remain successful, they need to differentiate themselves from other retail outlets. Private label products fit into this strategy by enabling supermarkets to offer exclusive food items that aren't available to their competitors and also directly promote their company's reputation.

Private label products also offer financial and quality control advantages to both retailers and consumers. In the past, private label and store brand programs enabled retailers to pass along savings to their shoppers by eliminating some expenses and frills associated with branded products from major food manufacturers, such as manufacturers' advertising costs or their elaborate packaging. In today's highly competitive retail environment, where big-box and mass-merchandise stores continue to chip away at supermarkets' share of the food market, the lower prices of private label products attract supermarket buyers.

In an era distinguished by consumer attention to food quality, private label products enable retailers to exert greater control over food production and processing methods, and to use this control as a marketing advantage. As one managing consultant put it, "companies [these days] view risk to their brands as their single biggest business hazard."[46] Business alliances that permit retailers to inform consumers about the origin of their food and assure its quality, and to act quickly in the event of a recall, bestow substantial marketing advantages as well as the opportunity to educate customers about the distinctive qualities of their store brand products. Smaller scale food producers and processors are in a position, both geographically and operationally, to develop exclusive relationships with retailers that value—and are willing to pay for—products with assured quality characteristics that can quickly be traced back to their source.

42. *Supermarket News*, April 5, 2005.
43. Private Label Manufacturers Association <http://plma.com/storeBrands/sbt07.html>.
44. *Baltimore Sun*, May 4, 2005.
45. Excerpts from "Private Label Food and Beverage in the U.S.," Packaged Facts, Rockville, MD, February 2007. <http://www.packagedfacts.com/Private-Label-Food-1282369/.
46. Greg Pellegrino, Global Managing Director with the consulting firm Deloitte Touche Tohmatsu, quoted in "Prospering in the Secure Economy," *Meat and Poultry* magazine, October 2004.

CASE STUDY OF A PRIVATE LABEL: DOROTHY LANE

A recent interview in Supermarket News explored a successful private label marketing campaign for meat that relies upon a direct relationship between a retail grocer and small-scale suppliers of natural meats.[47] As part of its private label program, Dorothy Lane Market, a three-store specialty grocer based in Dayton, OH, offers consumers a choice of several free-range poultry, natural beef, and natural/no-nitrate pork products. The specifications incorporate attributes related to environmental sustainability and humane practices. For example, Dorothy Lane Market's private label free-range turkeys are guaranteed to be:

- Raised "free-range" (meaning, according to the market's definition, the birds are free to range outside, to scratch the ground, and forage on plants).
- Raised without antibiotics.
- Raised without hormones or growth stimulants.
- Vegetarian-fed—with no animal by-products in the feed.
- Locally grown and raised on a small family farm (Bowman & Landes in New Carlisle, OH).

In a February 2005 interview with Supermarket News, Jack Gridley, the director of meat and seafood purchasing for Dorothy Lane Market, said his firm buys beef only from one source: Coleman Natural Beef. All beef entering his company's private label program originates from Coleman in order to ensure traceability of the food products from "farm to plate." Market officials estimate they can identify the farm source for 93 percent of their meat transactions, so if there is a recall, they can respond immediately.

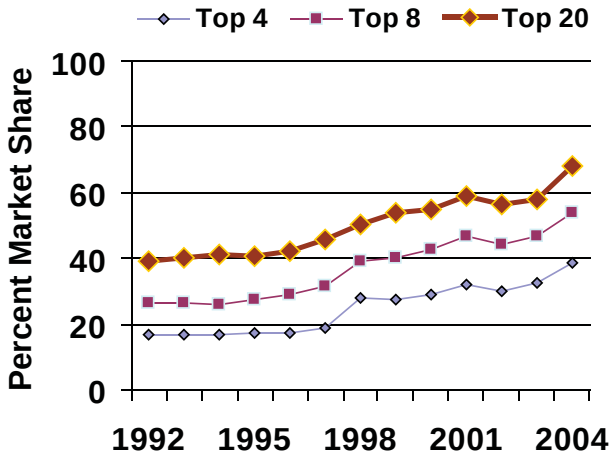
While Dorothy Lane Market's private label program may include unusually stringent quality, animal husbandry, and social welfare standards, a growing number of retailers have begun to incorporate some type of certification or natural food labeling into their private label programs, as such programs have proven to be winning marketing strategies for some early market entrants. Whole Foods Market, the prominent retailer of natural foods, led the charge in developing organic and natural store brand programs back in 1997 and 1998 by launching its 365 Organic and Whole Kids lines of products.[48] By early 2005, these store brands represented about 15 percent of the company's revenue.[49] Several conventional supermarket chains have followed Whole Foods Market's lead by launching their own store-brand organic programs over the past few years, including Kroger Company (Naturally Preferred), Shaw's Supermarkets (Wild Harvest), Giant Food/Stop and Shop (Nature's Promise), Safeway (O Organics), and Wegmans Food Markets (Wegmans Organic).

47. "Organic, Natural Meat Sales Exploding," Bobbie Katz, *Supermarket News*, February 2005.
48. Timing of private label programs obtained from Whole Foods Market.
49. "Whole Foods has Another Robust Quarter," Austin *American-Statesman*, February 28, 2005.

Retail Concentration

The number of supermarket chains operating in the United States has dwindled in recent years as many of the country's largest supermarket firms have increased their scale of operation and sought to improve profitability by acquiring assets from less successful competitors. Today the U.S. grocery sector is increasingly controlled by fewer and fewer grocery firms (figure 14). Whereas in 1998 the top 20 grocery firms in the United States accounted for slightly more than half of total sales, by 2004 they accounted for more than two-thirds. During the same period, the top four grocery firms increased their market share from 30 percent to almost 40 percent of total grocery sales volume.

FIGURE 14. Market share of top supermarkets, 1992-2004



SOURCE. USDA/ERS

Two trends appear to be responsible for the intensified concentration of the grocery sector over the past couple of decades—the growing range of marketing outlets that sell food, which has undermined the longstanding role of supermarkets as a primary source of food, and the declining importance of at-home food preparation, which has boosted sales of ready-to-eat foods (often from foodservice outlets) at the expense of other food purchases.

Channel Blurring

The growing influence of discount mass merchandise stores in the retail sector has transformed the way people shop for food. In 1990, supercenters—combination retail stores that blend an economy supermarket with a discount department store—sold just under 2 percent of all food sold in the United States. By 2005, their share of the U.S. food market had grown to nearly 14 percent.[50] Their ability to purchase food products in large volume and use their buying power to offer unusually low prices to consumers appears to have earned them a lasting niche in the retail grocery marketplace.

50. "Competitive Edge," Willard Bishop Consulting, Ltd., July 14, 2005, and "The Future of Food Retailing," Willard Bishop Consulting, Ltd., July 2006.

The Squeeze on Grocers

According to recent analysis by ERS, the market for groceries is essentially saturated. Despite steady increases in the U.S. population, the growth potential of retail grocers in the United States remains limited by the declining share of consumer income spent on food.[51]

Further exacerbating the financial pressure on supermarkets has been the steady increase in the share of food dollars on food eaten away from home. Between 1966 and 2006, the share of food dollars spent on food consumed outside the home climbed from 31 percent to nearly 49 percent.[52] For more information about food eaten at home versus away from home see figure 1 on page 7.

In this increasingly competitive marketing environment, supermarkets are looking for ways to improve their profit margins. Supermarkets at all scales of operation are working with their vendors to integrate supply chain management systems and ensure end-to-end quality control. These systems use information technology to streamline the distribution process, and include special arrangements with vendors to increase supply chain efficiency.

Integrated data systems have already led to savings among the early adopters. With the costs of technology continuing to fall, supermarkets will continue to adopt increasingly complex technology to support their distribution operations, especially as the potential for long-term cost savings becomes widely recognized. For more detailed information about technology in the food supply chain, see our companion publication, *Supply Chain Basics: Technology: How Much—How Soon*, available at http://www.ams.usda.gov/MarketingServicesPublications.

How Does Retailing Efficiency Affect Food Suppliers and Processors?

The use of information technologies, from barcodes to RFID and data synchronization, has increased the amount and efficiency of the information supermarkets share with their suppliers—and that they expect in return. Results from a 2000 food industry survey show that more than 80 percent of surveyed retailers demand more services from their suppliers than they did in 1993.[53] The top three services reported by retailers were the provision of private label products, category management services, and electronic data interchange capability.[54] Consequently, to be taken seriously as suppliers in today's retail marketplace, food producers and manufacturers must develop the technological capability to exchange product information electronically.

Beyond anticipating consumer demand and streamlining logistics with information technology, retailers are exercising leverage to negotiate purchases of food products customized to their procurement and marketing needs. To ensure that suppliers meet their standards, some retail firms are initiating Vendor Certification Programs (VCP) that require certified vendors to guarantee specific safety, handling, traceability, packaging, and quality control practices.

To ensure that inventory levels are finely coordinated with demand, supermarkets have made arrangements with some vendors to ship directly to stores instead of to a centralized distribution warehouse. (This movement is discussed in detail in the section "Direct Store Delivery.") The move to customized product offerings for each grocery store opens new marketing opportunities for small- and medium-sized food producers and processors that might not produce

51. *Competition Alters the U.S. Food Marketing Landscape*, Steve W. Martinez, ERS, November 2003.
52. Food, CPI, Prices and Expenditures: Foodservice as a Share of Food Expenditures <http://www.ers.usda.gov/Briefing/CPIFoodAndExpenditures/Data/table12.htm>.
53. "Understanding Retailer Purchasing Trade Practices in the Produce Industry," Willard Bishop Consulting Web site, June 2000.
54. National Food and Agricultural Policy Project Policy Briefing Paper, March 2001.

enough to supply the large number of retail stores served by a distribution center, but that do have the capacity to supply products to a selected number of individual store outlets.

Advantages of Supply Chain Coordination

The retail food industry is forming tightly aligned supply chains to gain two key objectives—efficiency and improved customer response.

Efficiency

Supply chain efficiencies are gained by effectively sharing information between and within firms. When information is shared among a firm's departments rather than each department operating in isolation, the firm becomes more efficient. A lack of communication among departments slows a firm's response time, possibly marketing products consumers don't want. Departmental integration focuses all departments on the same goal and makes the firm more responsive to customer demand. Efficient internal communications are essential to effective external communication with suppliers.

Data sharing between retailers and their suppliers is not new, but it has become more efficient and richer in detail. The advent of inexpensive computer equipment and software allows increased collection and tracking of many kinds of product data all along the supply chain.

The streamlining of data exchange with suppliers helps supermarkets match their product inventory to consumer needs on a store-by-store basis. At the same time, suppliers benefit from the information-sharing arrangements by learning consumer needs and preferences faster and with greater accuracy. As the cost of technology declines and its capability expands, the trend toward close coordination between retailers and suppliers can be expected to accelerate until it becomes the new standard for partnerships between supermarkets and their suppliers in firms of all sizes.

Improved Customer Response

Firms today aspire to become demand-driven supply networks, with the agility and efficiency to succeed in a rapidly changing global economy. This business model is driven by capturing information about consumer demand, not by forecasts or plans. Suppliers with real-time data collected at point of sale can quickly modify their products, quantities, and package sizes based on customer preferences. For more detailed information about electronic exchange of information along the supply chain, see our companion publication, *Supply Chain Basics: Technology: How Much—How Soon*.

Traits of Top Grocery Firms

Top grocery firms share a commitment to communication and integration with their suppliers through adoption of information technology, which can lead to cost reductions for business operations as well as increased sales. Streamlined data and information exchange with their suppliers help retail firms customize their product assortments to consumer needs on a store-by-store basis. On the other hand, producers benefit directly from information-sharing arrangements with retailers by developing a more precise understanding of consumer needs and preferences quickly. As the cost of technology declines and its capability expands, the trend toward close coordination between retailers and suppliers can be expected to accelerate and become the new standard for business partnerships between retailers and vendors, regardless of firm size. Consequently, small and mid-size food producers interested in supplying the retail grocery market will need to employ such technologies as barcodes or RFID tags that enable them to share product data throughout the production, handling, and distribution processes.

Global Data Synchronization

In the modern world of global sales, it has become imperative for businesses in different countries to coordinate their supply chain data. This coordination is called *Global Data Synchronization* (GDS). The goal of GDS is to create a universal product code that can be understood by sellers and buyers everywhere. With such a code, stores and their suppliers can communicate clearly, unambiguously, and—most important—accurately about the goods they are buying and selling.

How Does Data Synchronization Work?

Data is exchanged between retailer and supplier through data pools, which provide transparent gateways through which suppliers and retailers exchange close-to-real-time information about products, packaging, and logistics. Before data are made available for access, they are checked for accuracy and configured into standard formats. The data pool defines each data element to ensure that buyer and seller are "speaking" the same language. This standardized data format provides accuracy and allows buyer and seller to know exactly where to locate information.

GDS began with a program called Efficient Consumer Response (ECR). ECR programs, introduced in the 1990s, were designed to allow a seamless flow of product from producer to consumer, minimizing inventory holding costs while reducing the number of out-of-stock items and maintaining high levels of customer satisfaction. ECR ties grocery manufacturers, wholesalers, and retailers together with information systems. The four basic strategies of ECR are:

- Efficient store assortment.
- Efficient replenishment (Just-in-time inventory minimizes the amount of inventory held by distribution centers and store back rooms).
- Efficient promotion.
- Efficient product introduction.

Prior to ECR, supermarkets and food manufacturers had focused primarily on reductions in logistical expenses.

GDS is an extension of ECR. Like ECR, it is designed to reduce excess inventory but, because it reduces the incidence of data errors and allows data to be shared more efficiently, it saves time and money throughout the supply chain process. The advent of computerization, the Internet, and the declining cost of high-powered computer equipment and software have made this type of constant communication and intensive inventory management increasingly possible and affordable.

The Global Data Synchronization Network

In 2003, FMI and the Grocery Manufacturers Association (GMA) sponsored six case studies measuring the impact of data synchronization on grocery firms and food manufacturers between November 2002 and January 2003. Three manufacturers and three retailers were selected, ranging from relatively small regional firms to large conglomerates: Bi-Lo (a discount retail grocery subsidiary of Ahold USA) Kraft Foods, Nestle, Purina Pet Care, Proctor and Gamble, Shaw's Supermarkets, and Wegmans Food Markets. Each of the firms in the case study had implemented data synchronization. The resulting report is titled *Data Synchronization Proof of Concept: Case Studies from Leading Manufacturers*.[55]

55. GMA-FMI Trading Partner Alliance: Action Plan <http://www.1sync.org/documents/GDSN/GMA-FMI%20Data%20Sync%20Action%20Plan.pdf>.

The findings of the study were promising and resulted in the launching of the Global Data Synchronization Network (GDSN), an electronic system that exchanges data between suppliers and retailers using a standardized format. GDSN is the electronic network that makes GDS practical, allowing suppliers and retailers to communicate product information accurately, quickly, and efficiently. Early adopters of GDSN have experienced significant time and cost savings and want their suppliers to participate in data synchronization.

As the technology spreads to other supermarkets, more food buyers will require their vendors to participate in GDSN. Since mid-2003, food industry participation in GDSN has risen from 100 companies to nearly 10,000, and the number of registered food items grew from 60,000 to more than 580,000 in 2005.[56] GDSN is increasingly a requirement for food suppliers.

OVERVIEW OF GDSN

GDSN is a network of data pools with a global registry for sharing information about products and companies. It was conceived, and is supported by, the European Article Number (EAN) Association, the Uniform Code Council (UCC), and leading companies and industry groups worldwide. It enables trading partners in the supply chain to exchange data that is accurate, up-to-date, and compliant with universally supported EAN and UCC system standards[57]. GDSN is based on a centralized global registry that connects to data pools around the world, enabling standardized data to be synchronized on a near real-time basis.

GDSN was developed in response to the high costs associated with inaccurate data. To ensure GDSN meets the business needs of the user community, EAN and UCC established an oversight committee of 17 senior executives from manufacturing, retailing, and EAN member organizations to govern GDSN, promote its global adoption, and address strategic issues related to its rollout.[58] More information about GDSN can be found in our companion publication, *Supply Chain Basics: Technology: How Much—How Soon*.

56. Synchronization: *The Next Generation of Business Partnering*, Accenture, 2006. <http://www.accenture.com/Global/Services/By_Industry/Consumer_Goods_and_Services/R_and_I/SynchronizationPartnering.htm>.
57. Global Data Synchronization Network FAQs, Drummond Group. <http://www.drummondgroup.com/html-v2/gdsn-faq.html>.
58. Ibid.

Initially, it was thought the benefits of GDS would come from improved standards, accuracy, and synchronization. However, improvements have surpassed these basic areas and include such improvements in vital processes as demand forecasting, procurement, replenishment, and logistics. Researchers believe this is just the tip of the iceberg, and still more improvements in RFID, Electronic Product Code (EPC), and price synchronization can be expected as GDS becomes the standard for the retail grocery sector.

What are the Advantages of GDS to Retailers?

- *Reduced inbound and outbound freight costs.* GDS improves the accuracy of product weights and measures information resulting in truckloads more completely filled but not exceeding weight limits. The improved efficiency results in lower transportation costs.
- *Improved productivity within distribution networks.* Labor costs are reduced due to fewer work hours needed to correct and align product information between retailers and suppliers.
- *Improved DSD receiving capabilities.* More accurate data means that more items scan correctly at the back door and fewer labor hours are required to correct errors.
- *Improved productivity within order and item administration.* Correct item information streamlines administrative activities, resulting in improved response time of continual replenishment programs, less time for order inspection, and reduction in labor hours required to process new items.
- *Reduced need to adjust and reconciliate invoice and coupon discrepancies*, which lowers labor costs.
- *Reduced time from item entry to retail shelf.* (Speed to market and customer service).
- *Reduced time spent addressing item data issues.*

What are the Advantages of GDS to Suppliers?

- *Reduced inbound and outbound freight costs.*
- *Improved productivity within distribution networks.*
- *Improved productivity within order and item administration.*
- *Reduced time from item entry to retail shelf.*
- *Reduced time addressing item data issues.*
- *Makes your company more appealing to retailers who have or will soon adopt GDS.*

How does GDS Better Utilize Current Technology?

Prior to GDS, suppliers and retailers created, stored, and used electronic data exclusively for their internal operations. Retailers' and suppliers' product data had no standard format, data fields varied from firm to firm, and the information collected was not generally shared among companies.

Data synchronization organizes into a standard format product data that has been captured electronically by scanning barcodes, uniform product codes (UPC), or RFID tags. The stored information can be accessed on the network by both supplier and retailer. Because product information is synchronized, both have the same information in a standardized format, making it easy to find and understand product information. For example, when a supplier changes any catalogued characteristic of a product on GDSN, the new product characteristic is shared with the retailer almost immediately, eliminating errors due to incorrect information. Retailers know exactly what they are getting and they get the products they ordered. The synchronized data makes the supply chain transparent to buyers and sellers, reducing confusion and costly errors.

When a retailer receives a shipment utilizing GDSN, these are the benefits when an electronic invoice is scanned:

- The retailer saves the time it takes to record the shipment manually;
- Errors are avoided that could occur by manually recording the contents of the shipment;
- The shipment can be compared electronically with the original order.

When the retailer acknowledges receipt to GDSN, the supplier sees the receipt and the date and time received.

Unexpected Benefits of Data Synchronization

In the spring of 2006, sponsored by GMA, FMI, Wegmans Food Markets, and 1SYNC, a GDSN data pool, a follow-up to the 2003 study investigated the benefits of GDSN. The resulting report, *Synchronization—The Next Generation of Business Partnering*,[59] not only confirmed the findings of the 2003 initial study but surpassed some original projections. It found that:

- Using accurate data to drive business processes develops value for all industry players.
- Data synchronization is not only technology—it is people and processes working together to form a highly integrated and collaborative value chain.
- Manufacturers and retailers that lead the way are realizing significant benefits.

Not only have manufacturers improved productivity, but they have also reduced the time it takes for a new item to reach the retail shelf. Due to greater efficiencies in the distribution network, one surveyed manufacturer was able to condense a spreadsheet-based process used to align product information with its distributors from 5 days to 48 hours.[60] Some significant productivity improvements include reduction in the

59. Synchronization: The Next Generation of Business Partnering, Accenture, 2006. <http://www.accenture.com/Global/Services/By_Industry/Consumer_Goods_and_Services/R_and_I/SynchronizationPartnering.htm>
60. Ibid.

time needed to add new products; change existing product characteristics such as size, case count, and palletization requirements; reduced instances of coupon rejections at store check-out; and reduced time for a new item to reach the shelf.

One participant in the GMA/FMI synchronization study introduced 720 new products into its portfolio with significantly less labor than projected, saving 3,480 hours of employee time annually—an estimated savings of $288,000.[61] This sizable addition to its portfolio represented a 50-percent increase in its product line. Prior to the implementation of GDSN, the process of assembling and circulating all relevant data associated with these products to internal units and trading partners would have required hiring an additional two full-time employees to enter the data, print or develop documentation, and send it out.[62]

TABLE 4. Benefits of data synchronization

Performance Metrics (Process Area)	Source of Benefits[a] % Improvement over Current State	
	Retailer[b]	Manufacturer[c]
Reduced Inbound and Outbound Freight Costs (Transportation)	6.5%	1–8%[d]
Improved Productivity Within Distribution Network (Distribution)	1%	64%[e]
Improved DSD Receiving Capabilities (Store Operations)	9%	Not Applicable
Improved Productivity Within Order and Item Administration (Order Administration)	50%	2–67%
Reduced Out-Of Period Adjustments and Reconciliation of Invoice and Coupon Discrepancies (Accounting Administration)	8%	Not Applicable
Reduced Time from Item Entry to Shelf (Speed to Market)	23%	67%
Reduced Time from Item Entry to Shelf (Customer Service)	40%	Not Applicable
Reduced Time Spent Addressing Item Data Issues (Sales)	Not Available	25-55%

SOURCE. *Synchronization—The Next Generation of Business Partnering*, Accenture, 2006.
a. Where actuals were not available, estimates were provided
b. Percentages were calculated using weighted averages, based on dollar values
c. Represents spot benefits for particular manufacturers; percentages do not reflect savings across all participants
d. Eight percent based on mill transit savings for a single product line at a particular manufacturer. Total mill transit savings by this manufacturer is pending completion of a full product portfolio audit and is expected to be lower.
e. Improvement is in a particular area at manufacturer; does not represent improvement across entire distribution network.

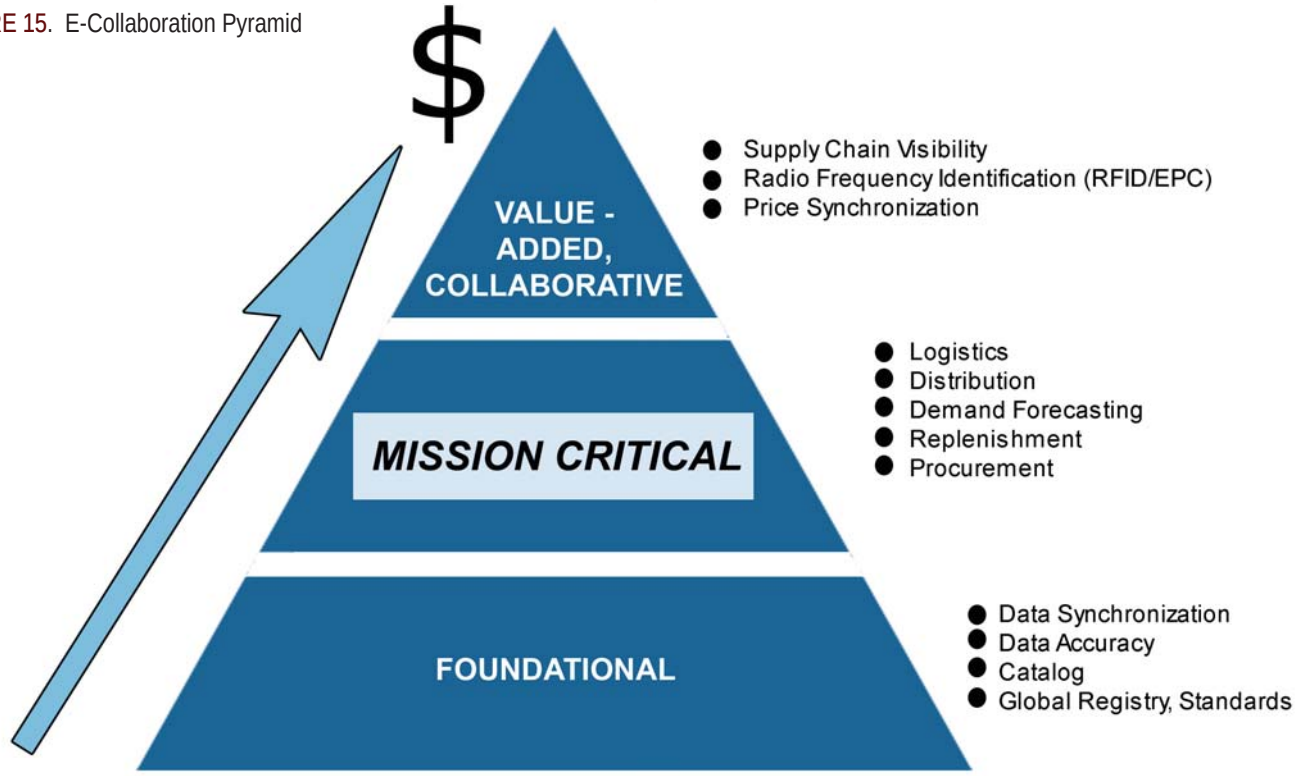
61. Ibid.
62. Ibid.

Initially, most benefits were expected to be derived from improved accuracy, synchronization, and standards for product registration and changes. However, those savings were just the beginning. Benefits also are achieved through enabling employees to concentrate on such "mission critical" tasks as demand forecasting, procurement, replenishment, and logistics, rather than validating item information and doing other administrative paperwork. Ultimately, even greater benefits may emerge as industry participants continue to work together on collaborative processes such as RFID, EPC, and price synchronization.[63]

Figure 15 illustrates improvements in the supply chain brought about by data synchronization. The 2006 Accenture report noted that initial improvements such as data accuracy and common global registry standards are the catalyst for improvements and savings in logistics, distribution, demand forecasting, replenishment, and procurement. These second-tier improvements, in turn, pave the way for enhancing the ability to track and control products through the supply chain, adoption and enhancement of RFID technology, and the development and use of price synchronization.[64]

Even in the initial stages of adoption, GDSN is already providing significant benefits to the food industry. For example, prior to the implementation of GDSN, one of the food manufacturers featured in the study had been fined $300,000 to $500,000 a year by retailers for inaccurate product information. After the adoption of GDSN, the fines assessed on the same manufacturer for inaccurate information were close to zero. Another food manufacturer improved the time needed to move new items from 4 to 8 weeks to only 2 weeks. Yet another study participant saved $2.2 million in annual transportation costs by correcting a weight error on a single item.[65]

FIGURE 15. E-Collaboration Pyramid



SOURCE. *Synchronization—The Next Generation of Business Partnering*, Accenture, 2006.

63. Ibid.
64. *Synchronization: The Next Generation of Business Partnering*, Accenture, 2006.
65. Ibid.

WEGMANS FOOD MARKET EXPERIENCE WITH DATA SYNCHRONIZATION

As of the summer of 2006, 95 percent of Wegmans Food Markets' vendors were participating in its data synchronization program, 92 percent had actually traded at least one item through their synchronization network, and 66 percent were completely synchronized. The value of benefits to Wegmans Food Markets from more accurate data is estimated at $3.5 million in annual transportation costs. In addition, new items arrive on retail shelves about 7 days quicker, labor and inventory carrying costs are reduced by about $1 million annually, and coupon scanning rejections are cut by about 40 percent.[66] This translates to cost reductions of $500,000 for every additional $1 billion in sales, as well as increased simplicity throughout the supply chain process.

Overall, food manufacturers participating in Wegmans Food Markets' data synchronization program are projected to reap $1 million in savings for every billion in sales. This increase in earnings represents estimated savings from reducing bloated inventory levels and stocking problems due to inaccurate data.[67]

Direct Store Delivery

While supermarkets generally prefer "just-in-time" inventory practices for budgetary and logistical reasons, maintaining low inventory levels throughout the distribution system has the potential to increase out-of-stock levels at individual retail stores, which can be a financially risky undertaking. Consumers' disappointment when they don't find the items they want on retail shelves is estimated to cost manufacturers $28 million and retailers $32 million for every billion dollars of sales.[68] According to a recent Franklin Covey study of the U.S. retail industry, called *Mapping Management Practices that Drive Great Performance*, the typical out-of-stock level for retailers is about 8.5 percent.

There are many causes for out-of-stock items: inaccurate forecast of consumer demand, shipment by the supplier of the wrong package size or flavor, unfit products due to product damage during shipping, expired product shelf life, or the seller's inability to track inventory accurately in its stores or distribution centers. Given the frequency of out-of-stock problems, and the huge financial burden that large out-of-stock levels can create for supermarkets, suppliers able to help supermarkets avoid out-of-stock items are likely to attract retail food buyers. Consequently, some enterprising supermarket chains are beginning to explore using *Direct Store Delivery* (DSD), an arrangement in which suppliers deliver directly to stores instead of to a distributor. DSD helps supermarkets overcome out-of-stock problems while keeping minimum inventory at their distribution centers.

The move to greater acceptance of DSD among retail chains may provide expanded market access to smaller scale local food producers and processors with the capacity to supply food items appealing to specific segments of a firm's customer base, but may not have the capacity to supply products to every store supplied by the chain's centralized distribution center. Recent market research by AMS suggests food items that perform extremely well in certain markets may not be as profitable for a broader sales territory.[69] Firms that

66. Ibid.
67. "In Sync: Wegmans and P&G Collaborate on Product Data, Grocer and CPG Giant Prevent Discrepancies," *ERI Journal*, July 2006.
68. Presentation by Jim Flannery, Proctor and Gamble, for the SN Interactive Forum on Maximizing Store Performance via Trading Partners Collaboration, June 28, 2006.
69. *Enhancing Commercial Food Service Sales by Small Meat Processing Firms*, AMS, March 2004.

are open to receiving food items via DSD and tracking product performance on a store-by-store basis may be more accommodating of smaller scale local producers than firms more heavily dependent on centralized procurement mechanisms. Indeed, a straw poll taken during a recent webcast sponsored by Supermarket News discovered that food retailers found it easier to collaborate with suppliers at the store level with DSD than with warehouse deliveries. Sixty percent believed DSD provided easier collaboration, 20 percent found warehouse deliveries better, and 18 percent found no difference.[70]

Producers and processors of locally grown and raised food may find it easier at first to approach retail firms that showcase foods from the nearby region. For example, Whole Foods Market, as part of its marketing philosophy, is strongly committed to purchasing locally grown produce. Not only do the firm's regional buyers purchase locally grown products, but the firm also allows individual stores to purchase selected merchandise directly from local producers via DSD, tailoring product offerings in its store to the preferences of its particular market area. In 2006, regional buyers from Whole Foods Market were explicitly directed to focus more attention on sourcing local products for their stores, and subsequently obtained merchandise from more than 2,400 independent farms.[71] Purchases from individual and family farmers (including marketing alliances of family farms pooling production under a common brand name) accounted for 78 percent of Whole Foods Market's total fresh produce purchases in 2006.[72]

In addition to purchasing products from local growers, Whole Foods Market established a $10 million promotional program for local agriculture, which offers low-interest, long-term loans to small agricultural entrepreneurs.[73] The loan program targets local producers of grass-fed beef, goat milk dairies, pasture-based eggs, and farmers with animal-compassionate policies. A portion of the loans will be available to vegetable farmers as well. Each year, Whole Foods Market makes an additional $10 million available for these loans. As the loans are repaid, the funds are recycled for additional loans to small producers.

A CASE STUDY OF MARKET ACCESS OPTIONS FOR SMALL FARMERS: WHOLE FOODS MARKET, ORANGE COUNTY, CA

During a March 2007 seminar, Jeff Biddle, Whole Foods Market's produce coordinator for the Pacific region, and David Schaner, a farmer/roadside stand manager who sells fresh produce to a single Whole Foods Market store near his farm in Placentia, CA, shared tips on how small farmers and food suppliers can successfully enter the retail market.[74] Schaner is among more than a dozen Southern California farmers tapped by Whole Foods Market to supply produce. Since entering into a direct marketing relationship with a single Whole Foods Market store in Tustin, CA, in 2005, Schaner has boosted his annual revenue about 20 percent. Moreover, the in-store publicity received from point-of-sale material attracted new customers to his roadside stand.[75]

Biddle and Schaner point out that the most important first step for producers is to recognize that the typical retail buyer is an inherently conservative decision-maker, and can't afford to take chances. When one is moving large quantities of product, each additional penny or nickel per pound adds

70. *Maximizing Store performance via Trading Partners Collaboration*, Supermarket News webcast, June 2006.
71. Open letter to Michel Pollan from John Mackey, CEO and co-founder of Whole Foods Inc.
72. Ibid.
73. Ibid.
74. Remarks excerpted from presentation delivered at Southwest Marketing Network Conference, Flagstaff, AZ, March 2007.
75. "Relocated Tustin Whole Foods debuts," *Orange County Register*, August 29, 2007

up to a lot of potential loss. In addition, the daily life of a retail produce buyer is full of anxiety (e.g., weather problems, delays in transportation) and it's always a struggle to figure how best to manage inventory—whether to buy more to avoid running out, or to "short" the stores to save money. No matter what the decision, someone will complain when planned targets for profit margin or shrinkage reduction are not met. On the other hand, there is constant pressure to try new products.

So how can a producer expect to stand out and get his or her foot in the door? Biddle and Schaner recommend the following steps:

- Approach store-level department managers as an initial step in gaining market access, as this tends to be more effective than contacting buyers at a centralized distribution center (who are constantly barraged by prospective vendors.) Even at firms that generally embrace DSD, such as Whole Foods Market, Biddle notes some store managers are more open than others to DSD. Nevertheless, he encourages producers to keep "knocking on doors" even if they do not succeed with the first store contacted. Once a producer establishes a track record with a buyer for quality and reliability, buyers are usually willing to do what it takes to maintain a successful business relationship.

- Send food! Samples of food accompanied by a subsequent phone call are probably the most effective way to grab a buyer's attention, and e-mail solicitations are usually ignored. (Schaner developed his current retail business opportunity through a Whole Foods Market representative who had patronized his roadside stand and enjoyed his product.)

- Have information at your fingertips about

  - Pricing of your product
  - Pack size and packing material
  - How the product is cooled
  - Product quality standards
  - Special handling needs, if any
  - Delivery capabilities
  - HACCP certification
  - Liability insurance coverage (often mandatory)

- Make a point of mentioning organic certification or any humane or environmentally sensitive agricultural practices you follow. Biddle remarked that one produce supplier he worked with near San Diego boosted his sales by publicizing that he deliberately used production methods and barriers that would not harm the rabbits that visited his fields!

- Offer product demonstrations at stores and interact with customers.

- Be willing to open your farm to tours by retail buyers; buyers often become supporters after visiting a farm.

- Don't be embarrassed about charging what you need to make a living. You shouldn't lower the cost of your product just to make a first sale or enter the retail marketplace, because raising your price after giving an initial lowball figure can alienate a customer.

- Indicate your willingness to provide the retailer special services, such as deliveries, in-store product demonstrations, price look-up stickers on bulk produce, and value-added processing services.

DSD AND THE RED TOMATO DISTRIBUTION MODEL: STRATEGIES FOR MANAGING GROWTH

Growers may find DSD deliveries a marketing advantage when shipping to a small number of store locations. Growers with insufficient volume to supply a chain store distribution center may find that they can fill the needs of two to three stores through direct delivery. As growers scale up the number of stores they service with DSD deliveries they may find that DSD is no longer as feasible.

This is the situation in which Red Tomato, a Massachusetts-based nonprofit organization, found itself when it arranged direct deliveries of locally grown produce to 40 retail stores three times a week in the Boston and Philadelphia areas. Among the services Red Tomato provides to its partner growers are product consolidation, repackaging, and transportation to destination markets. At first Red Tomato viewed DSD as an excellent way for farmers to improve producer access to retail markets and get their foot in the door. However, as the demand for locally grown products increased and retailers wanted to expand delivery beyond the pilot stores, it became too expensive to continue.

In order to continue DSD, Red Tomato addressed the distribution needs of its growers by partnering with transportation service providers, and with retail firms making deliveries to local stores, independent truckers, and farmers who had space after their rural deliveries. Red Tomato found that piggybacking on existing transportation networks helped both parties. Shipping products through their business partners reduced Red Tomato's shipping costs and also improved the operational efficiency and revenues of the shipper by filling trailers that previously were partially loaded or that otherwise would return empty.

To determine if DSD is appropriate for your firm, consider your scale of operation—including labor requirements, transportation costs, and time requirements.

red tomato

Fresh produce. Fresh thinking.

Preferred Vendor and Vendor Certification Programs

As food safety assurances become more influential on purchasing decisions, supermarkets are seeking out food suppliers with track records of proper postharvest techniques, good quality control throughout the distribution process, and recordkeeping procedures that enable supermarkets to track food products to the source efficiently. To accomplish this and reduce the risk of inadequate service from suppliers, many retailers created preferred vendor programs, which restrict vendor selection to suppliers that meet prescribed quality, quantity, packaging, and delivery requirements. Suppliers who participate in preferred vendor programs must adhere to strict requirements in order to maintain preferred vendor status.

Some retail firms prefer to work only with vendors that have enrolled in a formal Vendor Certification Program (VCP). A VCP allows retail buyers to verify their food suppliers comply with acceptable food handling, product quality, and food safety standards.[76] Usually carried out by a third-party auditor, a good VCP starts in the field with a review of the harvest, handling, packing, and shipment practices followed by a grower for a particular food product, and tracks the handling and distribution process of the food product until it reaches its final destination. Some growers develop their own certification programs to monitor performance, which also becomes a marketing tool for prospective customers. These programs are usually verified by third-party inspectors.

The basis of many certification programs is a Hazard Analysis and Critical Control Point (HACCP) plan. HACCP is widely accepted as a means to prevent contamination at vulnerable points in the handling and distribution process where the possibility is greatest for accidental or intentional contamination.

Growers' documentation of their production schedules, handling practices, and adherence to food safety protocols is an essential component of meeting retail procurement requirements for traceback capabilities and preparing for possible recalls. These may include product production dates, use-by codes, daily or hourly production run codes, quantity-produced data, and metal detector verification reports. Carton information should also include the processor name, hour of production, expiration date, and plant ID number to help retail buyers trace products to their places of origin.

76. "Vendor Certification Programs: Improving Food Safety Through Performance Tracking," *Food Safety Magazine*, July 2006

A CASE STUDY OF VENDOR/BUYER RELATIONSHIPS: THE APPALACHIAN SUSTAINABLE DEVELOPMENT NETWORK

The Appalachian Sustainable Development (ASD) Appalachian Harvest brand of organic fruit and vegetables is supplied by 60 farmers in southwestern Virginia and northeastern Tennessee, many of whom had converted tobacco acreage to organic fruit and vegetable production. While this network does not claim to have a VCP, it pays close attention to the quality of products and the requirements of grocery retailer clients. Anthony Flaccavento, Executive Director of ASD, says, "If you mostly deliver what grocers want most of the time, they will work with you."

ASD sales are growing rapidly, with 2007 sales expected to reach $700,000, and 2008 sales projected at $1 million. Flaccavento noted that the relationship between ASD and its grocery retail clients had become easier over time. He attributes the improved relationship to ASD's proven ability to meet grocers' specific production, packaging, and shipping requirements successfully time and time again. Flaccavento projects consumer demand in 2007 for his network's production to be more than twice the volume of available supply and estimates that 25–50 growers need to be added to the network to meet current consumer demand. More information about ASD can be found at http://www.appsusdev.org/.

Conclusion

With retail establishments of all sizes, from national chains to independents, seeking to carve out a piece of the natural and organic food pie, food manufacturers who can deliver products that meet their standards at reasonable prices will find a ready market. How can this benefit smaller scale food producers and processors? They may find it cost effective to produce packaged food items for a private label program, and let the retailer bear the financial burden of promoting and advertising the merchandise. Moreover, as private label programs for organic and natural foods become more widespread, some retailers, following the lead of such independent operators as Dorothy Lane Market, may try to distinguish themselves from competitors by involving smaller scale, local businesses in their private label programs. The local businesses then could share "personal stories" with consumers through promotional materials and appeal to consumer desires for local origin and authenticity.

The waning importance of national brands and neighborhood full-service supermarkets in the food marketplace and the rise of increasingly fragmented and diverse consumer shopping patterns offer exciting new opportunities for the smaller scale niche producer and manufacturer of food products. The rapid rise in Hispanic, Asian, and African-American consumer purchasing power, coupled with widespread consumer interest in gourmet and specialty food items, potentially benefits the smaller scale food producer and processor that can supply products that appeal to consumer desires for variety, innovation, authenticity, and freshness.

At the same time, health, nutrition, and environmental issues are becoming increasingly important to consumers who seek to purchase goods in accordance with their social values. Food producers and processors who can provide assurances of environmental stewardship and food safety can be expected to prosper. Retailers of all sizes seek suppliers that can deliver reliable volumes of high-quality, nicely presented food products that satisfy the concerns of environmentally and health-conscious customers. If demands for volume, supply availability, and consumer-ready packaging can be met, local smaller scale food producers and processors can play an integral role in today's rapidly diversifying food supply chain. Whether their participation involves producing branded food products for specialty retailers that use local origin as a consumer "hook," or supplying customized/exclusive food products to a retailer's private label program, smaller scale food producers and processors have many options for filling an important niche in the retail food marketplace.

The U.S. grocery sector is a mature market and, as such, its growth rate is limited to the growth in U.S. population. Consequently, one of the new frontiers in the grocery sector for increased sales and profits and reduced expenses is in the arena of data collection, accuracy, and exchange. Improvements to information transmission throughout the supply chain are expected to lower warehousing, distribution, and marketing costs.

Gains in sales are facilitated by more efficient collaborative relationships between suppliers and supermarkets from the adoption of data collection and data synchronization technologies. Leading supermarkets and suppliers electronically capture and analyze near real-time data throughout the supply chain, giving supermarkets the ability to quickly modify product offerings, quantities, package sizes, and other product attributes that consumers prefer. Collaboration between supermarkets and suppliers assists supermarkets' efforts to consistently merchandise a high-quality product mix that accurately reflects consumer desires at the store level. Food producers and manufacturers with proficiency in electronic data collection, sharing, and synchronization, and that collaborate with buyers, have a marketing edge in the grocery sector of the new millennium. Over time, as the collaboration between supermarkets and suppliers increases and the cost of technology declines, compatible forms of electronic data transmission will become even more critical.

Accurate evaluation of customer demand and precise tracking of inventories ensure that supermarkets have the right product on the shelf. Simultaneously, supermarkets will limit inventory stored in back rooms and distribution centers to precise levels sufficient only to prevent running out of stock, and will collaborate with vendors. Market leaders in the grocery sector are already committed to the Information Age, and require vendors to collect and record information about food products from the time crops were planted or animals raised through final delivery.

Product knowledge alone, however, is not sufficient in today's market. Suppliers must also be sensitive to the market demand for their product and know how the supermarket or consumer intends to use the product. Suppliers that develop this capability will be able to respond more quickly to shifting consumer preferences and retain a marketing advantage in the rapidly changing grocery sector.


WHOLE PANTRY
Hand-Stuffed Green Olives with Jalapeños
DR. WT. 5 OZ (141g)
2.99
Nutrition Facts
Dolmas
365 ORGANIC
Organic Mixed Mediterranean Olives with Roasted Red Peppers
NET DR. WT. 5.3 OZ (150g)
2.69
365
Large Ripe Pitted Olives
Jumbo Ripe Pitted Olives