Perspectives on the Manufacturer–Distributor Relationship:

How We Got Here and How to Move Forward Together

Dr. Richard J. George
Professor of Food Marketing
Haub School of Business
St. Joseph's University

PECK FELLOWSHIP YEAR 1 - 2010 REPORT
INTERNATIONAL FOODSERVICE DISTRIBUTORS ASSOCIATION

About International Foodservice Distributors Association (IFDA)
When U.S. consumers sit down to eat in one of the nation's nearly one million foodservice locations, the food on the plate—and possibly the plate and tableware—has been brought there by a foodservice distributor. IFDA is the leading trade association representing foodservice distributors throughout the United States and internationally. IFDA's members include broadline, systems, and specialty foodservice distributors that supply food and related products to restaurants and other food away from home foodservice operations. IFDA members operate more than 700 distribution facilities representing more than $110 billion in annual sales. For more information, visit www.ifdaonline.org.

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In 1986, the National-American Wholesale Grocers' Association (NAWGA) established an endowment in recognition of the achievements of retiring NAWGA President, Gerald E. Peck to support teaching and research if food wholesale management. Through time the Peck Fellowship has evolved to a series of three year appointments of Food Marketing Professors from Saint Joseph's University in Philadelphia, PA, to contribute to the understanding of distribution as it relate to food retailing and foodservice. The Fellowship responsibilities rotate every three years between the Food Marketing Institute (FMI) and the International Foodservice Distributors Association (IFDA). The current Peck Fellow, Dr. Richard J. George, recently completed a series of three one year research projects for FMI to better understand the future of food wholesaling. Now, Dr. George is undertaking a similar stream of research in support of the foodservice industry.

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INTRODUCTION

This study can best be compared to looking through a prism that breaks light up into its constituent spectral colors—the colors of the rainbow. Viewing the comments through a prism, one can see distributor shades of blue, manufacturer shades of red, broker shades of green, and the yellow of industry observers, combining these colors to make a rainbow for the operators. In the world of business, however, a rainbow is not a rainbow unless there is a pot of gold at the end of it. If there is no pot of gold, it is only something nice to look at and vanishes as quickly as it appeared.

As markets and companies recover from the "Great Recession" and rebuild their marketing strategies, one neglected issue is the design of the value chains for competitive advantage. The recent challenges and threats have left survivors reaching for the correct answer or a magic formula. During this search for answers, one must be careful not to regard the current models as fixed given the historical nature of the foodservice distribution channel.

Success in the foodservice channel is dependent on the presence of high levels of cooperation among channel members, as well as high levels of trust and integrity. Large power differences and low levels of trust and cooperation are a recipe for disaster. This report, based upon conversation with leaders in the foodservice industry, underscores the fact that current relationships can no longer be viewed as "business as usual."

An important determinant of the health of the foodservice channel will be the strength and dependability of relationships. Measures of relationship health include the following: trust, cooperation versus conflict, direction/degree of interdependence, and relative market power. As noted throughout the research and across the various channel players, transparency and trust are the key ingredients. What is needed is an atmosphere of openness and negotiation. It is not enough simply to pay for cases shipped. The new paradigm should focus on developing partnerships.

Part of the solution might be to engage in face-to-face planning and a sharing of expectations of what the partnership is going to deliver and who does what for whom. In addition, companies may want to set measurable goals based on a scorecard approach to what the partnership is achieving. The striking conclusion is that the time of yearning for yesterday's better days is past. The time for action is now.

This report describes the current relationship between foodservice distributors and manufacturers. In addition, suggestions are offered for relationship enhancement and for channel improvement in terms of both efficiency and effectiveness. The report is based on in-depth interviews with foodservice manufacturers, distributors, sales agents/brokers, and industry observers.

Please Note: The views expressed in this report, as well as statistics not specifically source referenced, represent the opinions of executives interviewed for this research.

Acknowledgements

I am particularly thankful to the executives of the various foodservice channel members who took the time to participate in the structured interview. Their knowledge and insights into the business were matched only by their passion for the industry. Several of the scheduled 45-minute interviews continued on past 90 minutes as animated executives communicated their commitment to ensuring that foodservice operator customers not only survive, but flourish. Their thoughtful responses provided valuable insights into the distributor/manufacturer relationship. Their views of the future provide the substance for a discussion of changes needed to enhance this relationship going forward.

Additionally, the outreach provided by the IFDA staff and executive board to key foodservice executives to participate in this survey provided the basis for a broad range of perspectives. The funding and support of the Academy of Food Marketing at Saint Joseph's University made this research possible. Finally, I offer a special thank you to my graduate assistant, Joe Reeder, for his dogged pursuit of information and integration of the many perspectives. Joe, together with Sarah Downs and Terri Breslin ensured that the research report was accurate and complete. Thanks to all.

Background

The foodservice/restaurant industry could easily be defined as a series of relationships. There are relationships with customers, financial backers, partners, and employees. All are critical. But somewhere at the top of that list has to be the relationship between the manufacturer and distributor, sources of not just products, but information, tools, and assistance with everything from marketing to menuing.

The aggregate foodservice industry share of the food dollar has almost doubled in the last 50 years (1955 = 25 percent, 2009 = 48 percent).[1] After a long period of growth, the industry now finds itself on uncertain ground.

According to Technomic, total foodservice retail sales equivalent for food and non-alcoholic beverages in 2009 was slightly less than one-half trillion dollars (actual = $499.83 billion). This represents a -6.1 percent real growth rate over 2008.

Further, Technomic forecasts a -1.2 percent real growth rate for 2010.[2] According to Moody's Investors Services, economic weakness combined with rising costs to consumers and businesses will create further difficulties for the restaurant industry. An increasingly competitive environment will add pressure to the restaurant business, as will food safety concerns. Against this backdrop, restaurant companies will face liquidity and refinancing risks. Obviously, operators are facing significant challenges, which will likely affect the manufacturer and distributor.

The current economic environment will likely result in consumers continuing to be more discriminating in their away-from-home food spending. A review of the following gives credence to this perspective:

- According to research from ConAgra, in the past year 75 percent of Americans have cooked more meals at home and they say they will continue to do so.[3]
- A study by the Coca-Cola Retailing Research Council of North America is focused on "growing sales by helping customers eat at home more." The goal is to move supermarkets beyond the "product provider" role to the go-to meal solution provider. The potential prize is an increase in food sales of 3.2 percent and an increase in total store sales of 2.2 percent.[4]
- More recent research by Packaged Facts found that half of respondents were more likely to eat dinner at home than they were three months ago, while 64 percent reported purchasing ready-to-eat or heat-and-eat food from a grocery store within the last month. The study predicts that supermarket prepared foods will grow to $14 billion (+7 percent) by 2011, largely motivated by consumers migrating away from restaurants during the recession in search of value and one-stop-shop convenience. In terms of total usage occasions, grocery-related prepared foods use leads both family and casual restaurant segments and trails only fast food/QSR.[5]
- Research by Price Waterhouse Coopers suggests that an enduring shift has taken place as a result of the Great Recession. Going forward, purchases will be more deliberate and purposeful. Conspicuous consumption will give way to more conscious or practical consumerism. Rampant deal-seeking will be replaced by more purchase selectivity and the use of shopping techniques and tools discovered during the recession.[6]

Anecdotally, we are hearing that shoppers are getting tired of trading down; however, they remain cognizant of today's economic realities and the need to balance that with personal desires to reward themselves.

The enduring question is: Will old spending habits return when the economy improves and unemployment eases? This will likely be a function of impact and duration of the recession and the

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[1] NPD Group/Eating Patterns in America, 2010.
[2] Technomic, 2010.
[3] ConAgra Foods, 2010.
[4] "Eating In," Coca-Cola Retailing Research Council of North America, 2010.
[5] "Prepared Foods and Ready-to-Eat Foods at Retail: The New Competition to Foodservice," *Packaged Facts*, 2010.
[6] "The New Consumer Behavior Paradigm: Permanent or Fleeting?" PriceWaterhouseCoopers, 2010.

price tag of the item. It will be hard to feed consumption cravings with tighter credit and homes that cannot be tapped for cash. However, food shopping and restaurant patronage may represent a "cheap indulgence."

In addition to the consumer-driven variables, higher food costs (wholesale and menu) and other factors, such as the following, will have a dramatic impact on the relationship among manufacturers, distributors, and operators:

- Customer loyalty to foodservice distributors/brands is eroding as restaurant operators are increasingly shopping around for better prices.
- In addition to managing food/waste costs, there is an increased focus on managing/cutting labor hours in the back-of-house at casual dining establishments.
- Chain restaurants have taken share from independents due to more aggressive pricing/promotions.
- Many foodservice distributors are willing to be more aggressive with pricing in order to increase share/build new accounts.
- Group Purchasing Organizations (GPOs) represent a challenge—and a potential opportunity—to both manufacturers and distributors.
- In an industry with already low margins, foodservice distributors have faced high energy costs that have been ratcheting upward. There is also the ongoing challenge of attracting, developing, and keeping good people.

These comments on the state of the foodservice industry are provided as a backdrop to underscore the significant challenges and changes taking place in this critical sector of the food marketing industry. This project is intended to complement the foodservice research done by organizations such as Technomic, The Hale Group, NPD, the Hartman Group, and others. The research reported here is based on interviews with key foodservice industry executives to examine the history and current state of the industry as it relates to the distributor/manufacturer relationship.

Research Design

In-depth interviews were conducted with 39 foodservice executives representing 34 companies and organizations between February and May 2010. Respondents represented the following foodservice classifications: foodservice distributors, foodservice manufacturers, sales agents/brokers, and industry observers. Respondents participated with an understanding that all comments would be treated with confidentiality.

Interviews were in the form of in-person, telephone, or electronic responses. The survey consisted of 13 questions, several of which were multi-part. Appendix A details the actual survey instrument.

Responses were captured via audio recording, transcribed, edited, and integrated by category of respondent into the report. Appendix B provides a list of executives that participated in the interview process.

In-depth Interviews

The contributions of the 39 executives who responded indicate that one's role in the foodservice channel definitely influences one's response. This is not necessarily a bad thing. As portrayed by the opening analogy, these perspectives are similar to looking through a prism that shows the different spectrums of light as the prism is turned. Together these perspectives provide a "rainbow" view of an industry designed to efficiently and effectively serve operators and their customers. Therefore, in order to give proper consideration to these dynamic colors of the rainbow, responses to each question will be presented by particular channel classification.

QUESTION 1

Specifically, reflecting on the distributor/manufacturer relationship during the first decade of the 21st century, how did we get where we are today? What is your view of the current relationship between distributors and manufacturers?

FOODSERVICE DISTRIBUTORS

It is no surprise that the declining economy between 2006 and today has figured as the primary focus point. The reaction to the economic situation and its effects on the foodservice distribution system, however, are being dealt with in much the same manner across the board. All interviewed were in agreement about one thing, *"The old model no longer works, and a new model is needed."*

Each organization is trying to react in its own way and in a manner appropriate for its operation. The interesting aspect is they all have a similar perception about what is "broken" in the old model.

Erosion of "Trust" in the System

Every executive surveyed mentioned the word "trust" or "relationship" or both when talking about the evolution of the business. It is apparent that all perceive that there has been an erosion of that trust on both the manufacturer and operator ends of the business with the distributor caught in the middle. One source of the strained relationship appears to emanate from manufacturers that deal directly with customers on price. Another is the emergence of GPOs. The perception is that the leveraged purchasing power of these organizations has left the distributor with little or no pricing flexibility and hence little room for error. However, distributors still remain the conduit from the manufacturer to the operator, but with little or no perceived incentive provided to the distributor by either channel member.

"I'm sick of it," stated one foodservice distributor who feels the distributor is being asked to do the administrative work for the manufacturer without being properly compensated. In other words, the direct distribution mark-up is the only thing the customer is willing to cover. The manufacturer quotes the price, yet the distributor is still required to provide all the associated administrative functions, *e.g.*, food safety training, menu development, customer service, etc.

"You just have to be careful about who you pick (as a partner/supplier)," was another notable distributor comment. Once again, trust between the manufacturer and distributor is apparently being eroded by "direct quote" pricing, which puts the distributor in a model of "just deliver this!" Such a paradigm does not necessarily recognize the true "cost of service" to individual accounts.

The emergence of GPOs has also increased pressure on supply chain relationships. It should be acknowledged, however, that the creation of GPOs was a survival reaction of selected channel members to allow them to be competitive with the purchasing power of larger organizations.

Historically the purchasing power and leverage rested with the distributor. The distributor would evaluate his customer base, project the volume of sales it would generate, and leverage that volume with the manufacturers. This allowed for a certain degree of financial maneuvering in pricing, permitting financial buffers. It is important to note that these buffers were not greed driven. They were simply insurance for the bottom line against the many variables confronting the foodservice distributor. Volume shrink and spikes in variable costs all impact the bottom line; a mechanism is needed to accommodate these variables.

Historically the purchasing power and leverage rested with the distributor. The distributor would evaluate his customer base, project the volume of sales it would generate, and leverage that volume with the manufacturers. This allowed for a certain degree of financial maneuvering in pricing, permitting financial buffers. It is important to note that these buffers were not greed driven. They were simply insurance for the bottom line against the many variables confronting the foodservice distributor.

A major shift in distributor purchasing power was created by the "Chain Operator" effect. These chains specified the manufacturer, negotiated price and quality specifications, and then directed the distributor to purchase and deliver to specified locations at this price.

Initially this relationship was workable as the chains guaranteed predictable volume, were willing to negotiate a distribution mark-up that covered limited distributor services, and, to some extent, took responsibility for delivering on that volume. In the case of a shortfall of volume, the distribution price would be adjusted to cover the cost. If volume exceeded projections, the distributor would be expected to adjust price accordingly to reward the additional sales.

Even if a chain represented a significant amount of a distributor's sales, the distributor's independent customer base provided additional volume that complemented the chain's to create a profitable environment.

The emergence of GPOs, combined with the downturn in the economy, created a potentially disastrous *"perfect storm"* for the distributor. As manufacturers approached market-bottom pricing, the pressure increased for the distributor to reduce distribution costs, without reducing services.

Fixing the "Broken Model"

There are various opinions on how to fix the current supply chain, but two are constant: the desire to be competitive and the desire to bring value to the customer. Most of the distributors feel that the influence of *"large chains taking things into their own hands"* has handicapped the distributor's ability to optimize purchasing and distribution opportunities.

The general sentiment is that *"distributors need to be treated as customers by manufacturers."* Distributors bring a great deal of value to the supply chain in terms of consolidation of products, administration, service, and quality control. The value of the distributor and its function should be recognized in any new model going forward.

Driving Costs out of Distribution Operations

"The customer is very fickle. He wants one thing, says one thing, but does another," stated one distributor. Traditionally distribution costs represent about 6.5 percent of the cost of goods sold across all industries. Within that 6.5 percent is a very narrow margin for profit. Even if the distributor worked for free, the impact on the overall distribution mark-up would be nominal. The cost structure of most distributors is approximately 40 percent fixed and 60 percent variable cost, although this varies with volume, type of product, etc. Fixed costs like warehouse operations, cooling systems, and mainframe computer systems are difficult to change in the short run. Variable costs such as productivity, miles driven, and overtime hours paid can be impacted more immediately.

Distributors have been quite effective in *"squeezing out"* many of the costs, in large part a result of advances in technology. For example, enhanced communications have allowed for better inventory management and more effective delivery routing. The reality, however, is that often for every step forward other changes may create a step back.

Increasing fuel costs are an example of this. As noted, a distributor can have the most efficient routing package, drivers trained to get better miles per gallon, and various other efficiency improvements, but when the cost of a gallon of diesel increases by 5 to 10 percent, the distributor is faced with two choices: pass the cost on to the customer or take it out of efficiencies gained.

Distributor Private Label Products

Distributor private label products were discussed by many of those surveyed and two aspects were commonly raised. First there is the desire to bring value-added products to the customer through private label products. As a general rule, most of the private label products are produced by manufacturers that currently market similar products. Second, while the manufacturer is happy to have the private label business, he feels stress that its customer, the distributor, is now a competitor as well.

Private label brands of national scale distributors *"soon become the label."* While many of the manufacturers focus their marketing efforts on the operator end of the business, they still depend on the distributor to bring the product to market. If a distributor has a strong private label, the concern of some manufactures is that the distributor's sales force may push the distributor's product to the detriment of the branded offering. This perception has reinforced the manufacturer's feelings for the need to deal directly with the customer and circumvent the distributor.

Another concern expressed is that the proliferation of private label increases the number of SKUs that must be managed.

FOODSERVICE MANUFACTURERS

In many respects, the manufacturer executives surveyed expressed views similar to those of the distributor. Trust and relationships have been mentioned by everyone. The key difference is that manufacturers feel the business model of distributors has to change. All agree that distribution has an important role to play in a market that is fragmented.

The Changing Model

In the late 1980s and early 1990s, consolidated distributors and broadliners began taking over the "total" distribution role, offering customers *"one stop shopping."* Most of the manufacturers mentioned the development of stressed relationships as a result of this new dynamic. Some feel distanced from their customers; others feel a loss of control.

Some of the larger manufacturer companies began their own consolidated distribution operations. This was possible since their companies produced a broad range of products that were flowing through independent distributors anyway. This allowed them to "push" their brands and maintain direct contact with the customer.

Companies that were not large or diverse enough to do this needed to market through distributors. These manufacturers expressed concern with the lack of transparency in the distributor's pricing model. Earned income was a recognized practice and there was little or no explanation of what constituted the logistics mark-up. With the emergence of chains, some manufacturers began to reopen direct dealing with the customer, specifically on product-based pricing. The distributor was still utilized to deliver, but was circumvented on product pricing. This resulted in additional supply chain relationship friction. Stated one manufacturer: *"A combative or zero sum relationship evolved, instead of how do we work together to help customers grow their businesses."*

Adding to this stress was the case of larger manufacturers, some of whom would simply negotiate that a distributor carry only its products and drop a competitor's line of similar products.

These actions created a source of income for the distributors that was not directly related to logistics, but instead driven by pricing and discounts. One manufacturer captured this sentiment with this statement: *"The problem is the distributors believe the well is never dry and keep coming back with more schemes to increase their allowance programs such as . . . pay for sales meetings, . . . pay for national accounts."*

Not only did this inflict damage on the distributor/manufacturer relationship, it also made the distributor more dependent on earned income, *i.e.*, income not generated by operating efficiencies. This became a serious problem when the dynamics of the business started to shift to a "cost plus" basis for distributors serving chain accounts.

Adding Value to the System

Several manufacturers discussed their view that there is a need to bring *"added value"* to the system. While cost reduction and efficiency are critical, products and services that help the operator grow its business represent other significant opportunities. To some extent this has placed manufacturers and distributors at odds. From the manufacturer viewpoint, new items and packaging give the customer greater choice and marketability. However, these activities add SKUs to a system that already is dealing with thousands of SKUs in some cases.

Manufacturers still feel *"at the mercy"* of distributors. They *"believe"* that they have lost control of pricing and direct contact with the operator. They want to see improved communication with distributors and greater transparency. There was a sentiment that distributors should be paid for the services and value they provide to the supply chain and not just for speculating in commodities and offering manufacturers access to large accounts. While this appears to be the direction that most distributors are moving, the message seems not to have gotten back to the manufacturing community.

> The emergence of GPOs combined with the downturn in the economy created a potentially disastrous "perfect storm" for the distributor. As manufacturers approached market-bottom pricing, the pressure increased for the distributor to reduce distribution costs, without reducing services.

Group Purchasing Organizations

GPOs have become a bigger issue with manufacturers. In some cases they are perceived as *"ineffective and unethical"* in terms of honoring agreements with manufacturers. In general, GPOs are viewed—by some—as a quick fix for struggling independents, but lack the structure and direction to effectively accomplish what they are designed to do, namely, leverage buying power. One example was given of a GPO that works outside the agreed terms and pricing protocol with a manufacturer. Frustrated with the situation, the manufacturer said, *"We just simply had to walk away from them [the GPO]."*

SALES AGENTS/BROKERS

The views of sales agents/brokers complement those of their foodservice channel member counterparts, *i.e.*, manufacturers, particularly the ongoing concerns about developing trust and improved working relationships. Instead of industry growth, now the perceived battle is for market share. Comparisons with the food retail side of the business underscore broker concerns about the future of foodservice management by manufacturers.

Battle for Market Share v. Industry Growth

As noted by practically every respondent, until recently the foodservice industry has enjoyed significant growth. In effect, these were the *"best of times"* with *"share of stomach"* moving from food retail to foodservice. It might be argued that during these *"boom days"* almost any new product or new concept resulted in success for the manufacturer, broker, distributor, and operator. When the economy began to decline in late 2007, consolidation and unit closures began as over capacity was trimmed.

Consequently, there now are fewer operators, fewer manufacturers, and fewer distributors. Instead of industry growth, the challenge has become one of market share gain. This in turn is driving additional mergers and acquisition on the distributor and manufacturer level, not to mention the impact on operators of all types.

The Blurring of the Traditional Transaction

Brokers feel that over time, manufacturers have relinquished control to distributors in order to maintain sales levels. Published prices are no longer valid and distributors are able to negotiate earned income, which in many cases is the primary basis for a distributor's profit margins. This blurring of the traditional transaction has resulted in a lack of trust. The consequence of this and the increased influence of technology should encourage a return to transparency.

Comparisons with Food Retail

There is a sentiment among brokers that the foodservice industry is 20 years behind the retail side of the business. However, changes in organizational structure and staffing by manufacturers appear to be closing the gap. For example, the manufacturer CFO who is responsible for both the retail and the foodservice businesses asks why a $50 million piece of retail business is managed by a single broker and a $20 million piece of foodservice business is managed by 50 brokers. The benefit of regional and national brokers is derived from a fusion of talents and local market knowledge to create mutually beneficial relationships with the operator in mind.

INDUSTRY OBSERVERS

Survival of the Fittest

The changing business model is coming. The foodservice industry experienced extreme growth in a segmented environment. September 11, 2001, was the first "hit" the industry took in terms of changing consumer demand. This was temporary and the industry bounced back and quickly returned to a growth mode. However, this did initiate the change process that began when the economic situation worsened after 2005.

"Survival of the fittest" is the term used by everyone. The fit have survived and many of the less fit have ceased to exist. However, the biggest shift in the distributor/manufacturer relationship has been financial. The problem started in the late 1990s when much to the chagrin of smaller manufacturers, larger manufacturers paid distributors for exclusivity.

When money got tight and large manufacturers became more reluctant to pay for that exclusivity, the smaller manufacturers took advantage of the shift to start working contractually with distributors. Rebates, earned income, and influence peddling diminished to some extent and were replaced by distributors having to put a "value" or "price" on their services. It was noted in broker responses that today, more than 50 percent of volume is under a contractual basis with defined terms and conditions of service levels, pricing protocols, and financial terms.

QUESTION 2:

What will the foodservice industry look like going into the second decade of the 21st century?

FOODSERVICE DISTRIBUTORS

All of the distributors surveyed talked about one or more of the following issues: slower growth, selective consolidation among foodservice distributors, need for greater communications and transparency throughout the supply chain, and more definition/differentiation between manufacturer brands and private label brands. The watchword on everyone's lips was the Foodservice GS1 US Standards Initiative.

Foodservice GS1 US Standards Initiative

The current initiative includes 64 foodservice manufacturer, distributor, and operator companies that are working to adopt GS1 US Standards with a goal of facilitating clean and accurate data between these trading partners. The initiative is voluntary and is open to any supply chain member wishing to participate, and the decision to participate is made on a company-by-company basis.

The general sentiment by those surveyed is that initiatives like the GS1 US Standards Initiative will likely result in greater transparency, enhanced communication, and better customer service. Product information, country of origin, and other relevant data would flow with the product through the supply chain to the end user for companies that choose to adopt GS1 US standards.

The advantages include better inventory control, enhanced traceability, and more accurate and timely data that can benefit all supply chain participants. Another advantage is improved communications between the manufacturer and the distributor. One distributor summed it up best: *"We've begun to have more dialogue between the manufacturer and distributor than ever before."*

Minimum Growth/Selective Consolidation

Those interviewed feel that both the sluggish economy and current high levels of unemployment will show slow improvement, so growth will be very limited until 2015. Unemployment has reduced disposable income with notable cutbacks on dining out. The concept of *"too many [restaurant] seats"* currently in the market could lead to continued contraction in the industry. This potential contraction will result in slower growth. The consensus is that individual company growth can be accomplished only by gaining market share of the existing market.

There is also agreement that some distributor consolidation will occur. Because of fragmentation in the market, it is felt that this consolidation will be fairly selective. The recent trend does not indicate that large broadliners will acquire other large broadliners. A majority of the consolidation will be larger distributors acquiring specialty distributors or small regional distributors to increase specific market share.

Private Label Growth

The comment was made that there are two types of manufacturers, those that produce their *"power"* brand and those that produce their brand and private label. Most distributors feel their private label brands are *"in good shape,"* mainly because most distributors have aligned their private label with their business. Customers are now looking for better value along with like quality. Private label increasingly offers this option to the customer.

FOODSERVICE MANUFACTURERS

A New Way of Doing Things

The most discussed subject here was data sharing. To a great extent many manufacturers view their data on products and sales as proprietary. Distributors on the other hand have databases on all the manufacturers, but only for their geographical markets. Large retailers like Walmart and Kroger have already begun sharing scan data (not sales data) to evaluate market wants and needs more accurately. Both large and small manufacturers expressed that the real "gold" distributors possess is data and access to independent operators. Chain and retail data is for the most part available, but accessing and understanding independents is not.

The terms segmentation and niche are used to capture the need of manufacturers to develop more focus on specific products and categories. *"You can't be everything to everyone,"* was how one manufacturer expressed it. This relates to the financing models that are currently in use in terms of credit, cash flow, and receivables. Manufacturers feel they have little exposure as most of the business is directly with distributors, who normally pay on a timely basis. It was acknowledged that distributors have the most exposure on the receivables side, especially with smaller independents.

Both large and small manufacturers expressed that the real "gold" distributors possess is data and access to independent operators. Chain and retail data is for the most part available, but accessing and understanding independents is not.

Here the analogy was made of someone who has multiple credit cards, all of which are at the credit limit, and is only able to make minimum payments every month. This results in the distributor having to provide the working capital. Certainly on the financial statements, accounts receivables and interest income are both positive items; however, actual cash flow is minimized, leaving little room for contingency or default.

Manufacturers and distributors need each other and in the future will need to communicate, plan, and work together more closely to offer solutions to enable their customers to grow profitably. They will also need to work together on issues like payment terms and financing, with the goal of having a steady and equitable flow of cash throughout the system.

Thinner Margins, Fewer People

Traditionally the food industry has operated on narrow margins. This was acceptable in the high growth environment of the 1990s. Most organizations still have those old business models in place. Increased technology, digital communications, and real time data is rapidly turning most organizations' sales forces into *"dinosaurs."* If an on-the-ground sales force cannot generate enough income to pay for itself (and more), then it cannot be justified. As margins decrease, if they are to survive, sales and marketing departments likely will need to find ways to bring *"value, solutions, and fresh ideas"* to the supply chain.

> Manufacturers feel they have little exposure as most of the business is directly with distributors, who normally pay on a timely basis. It was acknowledged that distributors have the most exposure on the receivables side, especially with smaller independents.

In addition, a comment of interest was that the food industry needs to attract new talent to remain competitive with other industries. Young graduates do not view the food industry as "sexy," instead preferring high tech and digital companies for entry level employment.

SALES AGENTS/BROKERS

Continued Channel Member Brand Competition

As previously noted, today there appears to be a high level of mistrust among the players. Part of this mistrust emanates from the many instances in which distributors are now competitors to manufacturers. In essence, this places the manufacturer in a difficult position. While the foodservice distributor is their primary conduit to the operator, the manufacturers' nationally branded products are competing with the distributors' own private label. In many cases the same branded manufacturer is producing their own label for the distributor. However, this phenomenon has been the norm in food retail since the birth of supermarkets.

NATO – No Action Talk Only

As in most other industries, issues related to the upward spiral of technology continue to influence business models. As an industry, foodservice has been slow to adopt change. Currently there is very little data synchronization between trading partners. Despite the efforts in the late 1990s of industry studies encapsulated under "Efficient Foodservice Response" (EFR), the industry has made minimal progress in this area. These inefficiencies within product, pricing, and promotion, when combined with trying to keep pace with technology, have created uncertainty and an unhealthy situation including limited transparency and higher than needed inventory levels.

The thinking is that there are a lot of *"roadblocks"* to growth and that organizations complicate what should be a simple process. Most players talk a good game and want to do the right thing, but the demands of their own organizations overwhelm real behavior change. The current voluntary Foodservice GS1 US Standards Initiative is a possible solution being explored by a number of well-known industry companies.

INDUSTRY OBSERVERS

Change Is Needed Now

More collaboration is needed (within the parameters of pro-competitive antitrust laws), and the adversarial relationship between foodservice distributors and manufacturers needs to be addressed. Manufacturers want to be in touch with their customers and distributors need to recognize this and work with them to achieve this goal.

GPOs have *"muddied the waters"* further by burning both ends of the candle between the distributor and the manufacturer. Now mature distributor private label lines are also in direct competition with manufacturers. As a result, partnerships have deteriorated to RFPs (Request for Proposal) and in some cases, relationships have dissolved altogether.

QUESTION 3:

What impact will the continued consolidation at the manufacturer, distributor, broker, and operator levels have on the foodservice industry?

FOODSERVICE DISTRIBUTORS

A recent Kraft Foods/Cadbury acquisition (January 2010) was on the minds of many being interviewed. In this case, a major international company acquired another company in which it did not hold a core competency. The question was whether in the long-term, acquisitions outside of core competency will be successful.

The Impact of Manufacturing Consolidation on the Distributor

As previously discussed, the current amount of consolidation of distributors tends to be very selective and limited. Manufacturers, on the other hand, are seeing increased consolidation with some very large players acquiring businesses outside their traditional realm. Kraft is now in the chocolate business and Heinz is in the baking business.

With this consolidation comes restructuring, requiring the distributor to *"reshuffle the deck with regard to pricing, sales contacts, payment terms, and methodologies."* When a smaller manufacturer is acquired by a larger one, the acquiring company tends to structure the pricing and terms to its profit model and not the one previously used. This has great impact on the distributor. Why? Traditionally most distributors have made their money on the *"buy"* side of the business. Now larger manufacturers are dealing directly with the customers, establishing their pricing protocols and dealing directly not only with chains but with GPOs. One distributor noted, *"This puts the distributor in a very uncomfortable position."*

The Changing Role of the Broker

Most surveyed feel that brokers are not evolving quickly enough to remain competitive. The general opinion is that brokers are not adding value to the supply chain as they did 20 years ago. Traditionally, the broker was the *"go to guy"* on the ground to leverage purchasing and channel sales. Recent shifts in the industry have seen brokers assuming a more administrative rather than a proactive role. Some view brokers as a *"redundancy in the system."*

This presents an opportunity for brokers to reinvent and reinsert themselves into the system. As relationships change and headcounts on both the manufacturing and distribution side diminish with cost reductions, a broker who can provide *"value added"* services can bridge that gap. This will require a change in mindset.

Brokers still tend to be localized. As one distributor stated: *"The broker prioritized his customers based on proximity to his house."* Not surprisingly, when surveyed, brokers and distributors rarely articulate the same priorities.

The other sentiment was that brokers need to align with the distributor's customers. Distributors realize that they need to deal better with brokers than they have in the past and see the broker as a resource versus a redundancy. Likewise, brokers must take the next step on the evolutionary ladder and modify the way they do business to add value rather than add cost.

Working on the "Chain Gang"

The growing power of chain restaurants has had a great impact on distributors. McDonald's, for example, has worked for decades on a "system" of exclusive or dedicated suppliers in their supply chain. Growing chains are now placing similar demands on distributors not entirely dedicated to their brand. Independent operators are still abundant, but their margins are tighter. The attempt by GPOs to mimic the chains' purchasing power results in additional pressure on the distributor. Dealing with such organizations removes the purchasing leverage power that the distributor traditionally controlled. Distributors now find themselves in the position of having to *"invent a better mousetrap"* in terms of how they structure their services and pricing. As one executive said: *"My impression is people talk a good game, but we're not walking the talk and we need to take some big steps to get there."*

FOODSERVICE MANUFACTURERS

Consolidation

"Consolidation is healthy because it gets rid of the dogs and changes the margin structure for those who are in a better position," stated one manufacturer interviewed for this work. Almost everyone viewed consolidation as positive if managed properly. For manufacturers, consolidation will allow greater diversity in product line without the need for R&D dollars being spent. For example, the targeted acquisition of a specialty seasoning company by a spice company appears to be a good fit, bringing the company added diversity.

There was the sentiment that consolidation *"forces people to get better, to improve in order to be successful."* Everyone acknowledged the synergies that can be gained on the manufacturing side from consolidation. Points of contact are reduced. At the same time, more efficient collection and synchronization of data, and reduced sales and administrative overheads can be achieved. Consolidation can also lead to greater transparency within individual organizations, especially involving costs structure. It provides an opportunity for manufacturers to analyze where cost or pricing may be contributing *"dollars to subsidize inefficiency."*

Distributors will see greater consolidation at regional levels, in which smaller independent distribution centers will be taken over by *"Super Regionals."* The data that these larger organizations can capture, if shared with manufacturers, will be of great value to enhancing the supply chain. Just as consolidation within the manufacturing community provides more one-stop shopping for distribution centers, the same effect will be true for operators.

Most expressed concern about broker consolidation. The regional broker is still valued by manufacturing and viewed as a supplemental sales force. As large national brokerage firms emerge, there are two main concerns. The first is cost and the second is regional performance. With respect to cost one manufacturer stated: *"They want to charge me a million bucks. For that I can hire 15 people and do it myself."*

Just as consolidation within the manufacturing community provides more one-stop shopping for distribution centers, the same effect will be true for operators.

This is also an interesting contrast to previous comments in which manufacturer sales forces were being considered more and more obsolete. The other concern was the regional ability of a national broker. *"They might be doing well all over the country, but I have a problem with them in Indiana. How can I fire them just in Indiana?"* asked one manufacturer. Another said, *"If a regional broker brings value, they will not just survive, they will thrive."*

On the operator side, the situation is viewed more as survival of the fittest. Simply put, smaller independents are not consolidating, but are going out of business in numbers that will significantly affect this segment's market share.

SALES AGENTS/BROKERS

Opportunity for Greater Efficiencies

The consensus among brokers interviewed is that more consolidation at every level could help the industry reduce cost by becoming more efficient. The industry survivors could have more money to invest in their business to take cost out of the system. Continued consolidation could also make the foodservice business more transparent.

Brokers believe that manufacturer consolidation could result in stronger category ownership with fewer manufacturers in categories, and these manufacturers could dominate their categories. This may enable manufacturers to regain channel power and result in lower levels of distributor subsidization. The effect could be the requirement of greater efficiencies and true costing throughout the channel.

From a broker perspective, consolidation causes ripple effects. If Company A with one set of brokers is acquired by Company B with a different broker set, then who wins, who loses, and who keeps the line? This in turn could raise broker conflict issues with other manufacturers in the same product category. Competition now reenters the equation for the brokers, not just regional influence or exclusive sales channels.

Distributors obtain a new customer base. Remaining distributors will need to form competing alliances and/or engage in more specialization. At the operator level the result is less company/brand choice. It is healthy for the industry since it drives greater efficiency. However, the trade off is choice.

New Strategic Alliances

Brokers are moving toward large regional/national agencies, similar to what happened in food retailing 20 years ago. This in turn will create strategic alliances with manufacturers. The thinking is that the mergers will provide brokers with an expanded role in the channel as product and marketplace specialists, resulting in an improved foodservice distribution channel.

The consensus is that the recent broker consolidation is only the beginning, with individual market brokers merging into regional brokers. Currently, there is an urgency to merge that will be followed by a settling period. The next phase may more resemble the food retail model. In that model, it took a number of years for the "Big 3" national food retail agencies to develop and realize the benefits of efficiency and effectiveness. Like the smaller food retail agencies, the remaining brokers will need to reemerge as specialty brokers.

It is believed by many that operators will be fewer in total number, but that stronger regional and national chains will emerge. The surviving operators will become more efficient and will focus on high performance in their chosen segments. The consensus is that there are too many restaurants (over capacity) and that the current economic situation will purge those unable to change quickly. Those who are most creative, financially sound, and willing to change will survive.

Some view consolidation at the operator level to be more of a shift from independents to regional chains. With the shift to lower margin business as independents are diminished and chains start to dominate, the channel will need to strive for greater efficiencies. This scenario, when combined with trading partner disagreement over who owns the customer, produces a substantial barrier to developing mutually beneficial partnerships.

INDUSTRY OBSERVERS

Manufacturer Consolidation

Large manufacturer players have been watching a shrinking U.S. market, especially in terms of margin. GPOs, whose primary goal is to reduce margins in an already tight market, exacerbate this challenge. Multinationals have turned their attention and capital investment outside the U.S. market and into emerging markets where potential growth and margins are greater and competition is less fierce.

Smaller players are left to *"duke it out"* here in the U.S. Consolidation will continue to be a "survival" option to increase market share and diversify. The move is also being made to quantify and qualify services and value, not just focus on price.

Distributor Consolidation

Consolidation again becomes the watchword. Larger more regionalized distribution organizations are quickly replacing smaller distributors. This allows for synergies and reduction of redundant fixed costs. The question must be asked: *"Are they buying a business or just a client list?"*

Specialized or niche distribution will also find its way into the mix. As SKUs increase, more scrutiny will be placed on identifying more profitable higher volume products. The successful smaller niche distributor will be the one that offers gefilte fish, Korean noodles, nori, or a range of chutney at a regional level based on market demographics. In the end, distributors are paid for providing service, convenience, and value.

Broker Consolidation

Traditionally brokers are very local, with a few "powerhouse" regional brokers and no real national brokers. Those moving toward national coverage will try to reinforce their regional presence through the acquisition of smaller brokers. Private label will also have an impact on the broker. The previously discussed private versus brand label battle is well in progress, but the outcome is yet undetermined.

Operator Consolidation

The impact of the chains on the landscape of independent operators has been further amplified by difficult economic times. According to one observer, it is estimated that by 2020, only 35 percent of the market will be independents versus 40 percent today.

QUESTION 4:

Please identify specific challenges/threats/opportunities (to the foodservice industry in general or to distributor/manufacturer relationship, specifically).

FOODSERVICE DISTRIBUTORS

There are some interesting distributor views on the topics raised in this question. Margins, relationships with chains, and purchasing entities such as GPOs are still large issues. A new challenge is the role of government and government regulation. Finally, there are conflicting sentiments on private label products.

Challenges/Threats

"Right now the government is the only challenge growing," stated one distributor. There was an overall concern with increased government influence on business, not only from federal agencies like OSHA, DOT, and USDA, but also from a tax and labor regulation standpoint. This results in additional stress on small businesses with related added costs, not to mention the impact of healthcare and wage reform.

One distributor did not mince words regarding government regulation as a threat. *"I think probably the biggest threat out there is government regulation. We talk about food safety. If you travel to Europe, in Paris it's a $4 billion dollar market and there are perishable products that lay outside until mid-day and people go to the market everyday and buy it. The only thing I fear, quite frankly, is trying to stay on top of Washington, our legislators, and regulatory issues."*

The other most discussed challenge is with large chains and GPOs. The sentiment is that when manufacturers set product pricing with these organizations, pricing flexibility is eroded for the distributor who better understands the costs to serve a variety of different customers. This places a strain on the distributor/manufacturer relationship, as well as the distributor/operator relationship.

Another significant challenge and opportunity is the voluntary implementation of GS1 US standards. The standards may deliver significant benefits to all members of the supply chain, but it is anticipated that implementation will occur in phases, resulting in a period of time when distributors are working with a partial system.

Food safety is an important issue to all participants in the foodservice industry. The enhanced ability offered by GS1 US standards in terms of traceability, communications, and transparency in the supply chain will not eliminate all problems associated with a recall. However, it should make the distributor, who bears the greatest physical burden in retrieving manufacturer product during a recall, more effective and efficient.

For the most part private label is viewed as a positive innovation by distributors. However, this results in many *"like products"* being offered to the customer. The concern is that certain items, either branded or private label, could become "irrelevant."

Opportunities

The primary theme is differentiation of services, namely, how to standout as a distributor and remain price competitive. What is needed is better communication between distributors and manufacturers. As distributors reinforce their relationships with manufacturers, they can jointly identify and act on areas of opportunity. Category management offers a good opportunity, not so much in terms of reducing SKUs, but in getting to know and understand the customer better.

> Breaking down some of the traditional communication barriers and getting everyone in the supply chain "on the same page," working towards the ultimate goal of providing solutions and value for the customer will require mutual cooperation throughout the supply chain.

New technologies and potential implementation of GS1 US standards will provide tools for the distributor to reduce costs while maintaining or increasing service levels. Likewise, the current economic situation creates an environment for the pursuit of innovation. Simply put, innovations that reduce costs will be attractive to supply chain participants.

Finally, the changing demographics of the consumer and customer present opportunities. As Baby Boomers and Generation X grow older, their dietary habits change. In addition, members of Generation Y consume more meals away from home or take out than any other generation. Foodservice establishments have already begun changing menus and products to accommodate this. This is a critical link in getting to know the customer better in order for distributors to be able to innovate.

In addition, foodservice workers are changing as well. As one distributor remarked, *"Chefs now are 23, 24 (years old); they're not 50 or 60 years old anymore."*

FOODSERVICE MANUFACTURERS

Challenges/Threats

The two main challenges that everyone discussed are the ongoing efforts to drive down variable costs while maintaining service levels and improving the manufacturer/distributor working relationship. The latter is especially true with regard to the sharing of data and earned income issues. Breaking down some of the traditional communication barriers and getting everyone in the supply chain *"on the same page"* in working towards the ultimate goal of providing solutions and value for the customer will require mutual cooperation throughout the supply chain. Both distributors and manufacturers recognize their interdependence. However, few are able to act on it.

To some extent this can be influenced by the customer. It was noted that one large QSR (Quick Service Restaurant) chain forced manufacturers and distributors to work together and *"leverage their competencies."* Manufacturers and distributors need to take the initiative and do this on their own if they wish to bring value and remain competitive. Again this relates to the ongoing themes of trust and partnerships in the industry.

Another challenge is improving category management. This will result in reducing redundant SKUs. It will also provide the opportunity for distributors working in concert with the manufacturing community to offer *"whole menu package solutions."*

GPOs were cited in almost every response as a challenge, as was earned income. Manufacturers feel that their efforts to reduce cost are canceled out along the supply chain by these two practices. Regarding GPOs, the comment was made that *"GPO's cut into margins, creating unhealthy relationships and stifling innovation."* While GPOs were originally created to leverage health care purchasing, the perception is that healthcare is a very different industry from foodservice in general. There is concern that the relatively narrow margins of foodservice make it difficult to apply the same collective leveraging as applied in other industries. As one manufacturer said, *"Anyone with a rolodex (electronic of course) is out trying to sign up operators for their loyalty programs. GPOs are driving the distributors nuts."*

Finally, there is concern about the future of independent operators. Chains or new independents may take their place, but this creates channel uncertainty and turmoil.

Opportunities

The goal of creating value through transparency, data exchange, and synchronization represent the greatest opportunities. Voluntary GS1 US standards are seen by manufacturers as a real catalyst for this opportunity. Previously issues of food safety, traceability, and general information flow have been isolated. Manufacturers had their pieces of the puzzle. distributors theirs, and so on. Those interviewed expressed that GS1 US standards application and leveraging will require a more unified approach to information sharing, AND will require much better defined business strategies and commitment by both the manufacturer and the distributor. One manufacturer captured the sentiment when he said, *"You won't be able to have a middle of the road strategy. If you are standing in the middle of the road, you're going to get run over."*

Some also anticipate a bounce back in "away from home" dining after three years of decline. The opportunity comes from purging the system in the past three years of many costs and redundancies. *"Those costs won't come back, but the diners will."*

SALES AGENTS/BROKERS

Challenges/Threats

A number of different ideas were expressed by brokers as challenges or threats to the industry in general or to the manufacturer/distributor relationship specifically. They include:

- Continued high levels of unemployment and less discretionary spending continue to plague the industry.
- There will be continued competition for "share of stomach" and market share in general.
- Manufacturers and distributors will be challenged to continue to provide service at a high level with reduced income and margin compression.
- Money is still being made on the buy, not on direct sales, reflecting the traditional practice of earned income. Some sales agents/brokers that were interviewed felt that manufacturers are paying multiple times for the same product to the operator.
- The trend has been for greater regulation on things like menus, calorie counts, and anti-trust issues.
- The retail mindset is driving foodservice manufacturers.
- Continuing trust issues emanating from the lack of sharing information and the absence of transparency will not abate unless these issues are addressed.
- There will be a continued weakening of the distributor/manufacturer relationship.
- There has been limited availability of capital to reinvest in businesses and innovation.

Other challenges and threats include increasing government regulation and legislation, alternative distribution options for specialized segments, and the consolidation of operators into more powerful buying groups such as GPOs. The net effect will shrink margins to distributors and manufacturers. Consumers will also enjoy new options—from Walgreens pilot program selling fruit, vegetables, and packaged meals, to Wegmans' or Harris Teeter's supermarket restaurants, to upscale food trucks. All of these options and other emerging formats will continue to blur the traditional definition of foodservice. Finally, concerns remain for realizing efficiencies and controlling costs and services related to getting product to the operator.

Opportunities

Opportunities include real partnering between the manufacturer and distributor, learning from other industries, and listening better to the consumer and the operator. Also, there is a need to focus on how to take cost out of the business by streamlining information from operator to distributor to manufacturer. Developing longer term strategic partnerships between manufacturers and distributors is critical. Finally, there are opportunities in adapting more quickly to the changing needs of the consumer and in becoming more flexible and efficient.

INDUSTRY OBSERVERS

The responses share the basic theme: *"Those that have survived are going to have to work together if they are going to continue to survive."* As reflected in the interviews, trust and building relationships will be the key. Interaction will be required by all parties across the supply chain as no one entity can succeed in isolation. Investment will decrease in the development of *"me too"* products and redundant SKUs.

QUESTION 5:

Specifically, how can manufacturers/brokers/distributors add value to the foodservice distribution channel?

For each channel member, the ability to bring "value" to the products and services they provide is deemed a critical task and is achieved in a unique manner by each player.

FOODSERVICE DISTRIBUTORS

The responses to this question were very similar. The sentiment is that distributors are much more in line with operators both in terms of understanding their needs and in terms of strategies. Distributors feel that both manufacturers and brokers need to get in *"tune with them,"* (*i.e.,* operators). Also, it is apparent that distributors feel the role of the broker needs to change, becoming more involved in understanding the distributor as well.

How Manufacturers Can Add Value

"We need the manufacturers; we can't do it without them." Overall, distributors express a genuine appreciation for the work of manufacturers. While suggestions for improvement vary, the common theme centers around improved communications and better understanding of both the distributor's and the operator's needs.

Other critical value-added activities included:

- Potential implementation of voluntary GS1 US standards as soon as possible, and
- Introducing new products that are truly innovative and that are aligned with the marketing strategy of operators.

How Brokers Can Add Value

The sentiment is that brokers may bring value to the manufacturer, but the value added for the distributor is minimal. As one distributor put it, *"They cost us money in the system because we really don't see the value; from the manufacturer they see some value because there's transparency on pricing."*

Most distributors want the broker to better know and understand the role of distributors and the challenges of distribution—resulting in better alignment between these two supply chain participants. The feeling is that brokers have become more administrative and less *"hands on"* in terms of dealing with the end user.

How Distributors Can Add Value

Many expressed a desire for enhanced communications, especially in terms of being a two-way conduit of information between the end user and the manufacturer. The distributor's sales force, with its rich operator data history, is seen as a valuable asset. Assisting with orders and inventory management, including distributor-generated or suggested orders, would bring more value to the system.

Other innovative services such as custom packaging, customized delivery, and offering new menu items and/or entire menu combinations, would bring value without significant incremental expense.

FOODSERVICE MANUFACTURERS

How Manufacturers Can Add Value:

"At the end of the day, the manufacturer needs to figure out what he is good at and focus on that," stated one executive interviewed for this study. While there certainly is the desire to make improvements up and down the supply chain, efforts need be applied where they have the most impact and where there is the most control over outcome. Manufacturers seem to feel they are in the best position to understand what consumers and customers want—and as a result feel they are in the best position to introduce innovative new products.

> If all this is orchestrated with the goal of satisfying the end user on quality, price, and service, everybody wins.

This perspective was recognized by distributors who feel they are being *"distanced"* from the customer. Outside of "customer" focused comments, distributors are looking for SKU reductions of marginal products.

How Brokers Can Add Value

Overall manufacturers want their brokers to know the product, know the market, and train the customer. To some extent manufacturers expressed a "comfort level" with the concept of regional and national brokers. The value a broker can bring is in generating volume through their relationship with the customers. In the words of one manufacturer, *"They've got to get back to selling."*

How Distributors Can Add Value

Strategic partnerships with the manufacturer is one of the predominant issues cited in this section. The value of distributors should not be limited to the "buy" side of the business, but rather in the ability to accommodate the flow of product from the manufacturer. Instead provide assortment, inventory management, and the ability to *"value"* or *"justify"* their services. Simply stated, *"What's more basic than the cost to serve to price paid?"*

Some expressed concern that distributors have lost some of their *"traction"* with large chains. Who really sells the product? The end user pays for everything, but how those costs are allocated up and down the supply chain is still very much debated.

SALES AGENTS/BROKERS

How Manufacturers Can Add Value

"Develop products that meet the needs of the operator, not simply the new product development mandate of corporate." Sales agents and brokers expressed the following on how manufacturers can add value:

- Understand how the operator functions.
- Develop better partnerships with understanding and acknowledgement of trading partner issues.
- Leave the sales and marketing to the companies that are supposed to do that, namely, the brokers and distributors.
- Recruit the best management talent.
- Invest in the best systems and technologies.
- Focus on brand establishment and brand identity.
- Train sales personnel effectively to respond to operator needs.
- Take out cost and minutia. Introduce fewer products that offer little in the way of differentiation. Provide greater ideation and innovation and better research aimed at new products for the customer.

How Brokers Can Add Value

On their own ilk, brokers stated:

- Become more efficient in reaching the operator and maintaining local knowledge.
- Make effective use of technology to communicate to manufacturers and distributors.
- Become more service oriented (consultative sellers of services).
- Add complementary product lines.
- Take a menu approach in addressing needs that are solutions oriented, rather than simply selling products.
- Become more sophisticated with technology and professional selling.

How Distributors Can Add Value

To add value, brokers felt distributors could:

- Become more open in sharing information with trading partners as well as more responsive to operators' demand for products.
- Reduce redundancy and cost of delivering to the operator.
- Eliminate non-value added activities, *e.g.,* food shows, *"ride withs,"* etc.
- Develop net pricing. Eliminate deviations and deductions.
- Decide whether the distributor is a logistics company or a sales and marketing company. Should distributors focus more on a redistribution model, moving product from A to B or do they need the whole sales and marketing side with fliers, food shows, merchandising assistants, etc.?

INDUSTRY OBSERVERS

Industry observers noted the following areas where industry players could improve:

- Distributors can add value and grow the business by focusing on their individual strengths and working in concert with operators to address their challenges and needs. Distributors must provide effective, cost efficient services that enhance the operators' ability to service the end user and reduce costs.
- Manufacturers must provide innovative and quality products. Brokers must be experts in their markets and know their products *"inside and out."*
- Operators must know their customers and do what they do best.

If all this is orchestrated with the goal of satisfying the end user on quality, price, and service, everybody wins. Simple to state, but challenging to accomplish.

QUESTION 6:

Please comment on advantages and disadvantages relative to the current distributor/manufacturer relationship, which appears to be oriented toward product-centric and transaction-based rewards.

FOODSERVICE DISTRIBUTORS

Responses to this question varied from *"it's not going to change"* by some, to innovative suggestions by others. One distributor talked about opportunities to shorten the supply chain by working together. Another stated, *"We as an industry have to make the changes. We all have to play our part and we'll all get the benefits out of it."* The distributors are all anticipating the benefits of standards implementation that provide the potential of additional transparency and clean and accurate data for all supply chain members.

In terms of product and inventory, some distributors are looking for a "pull" system of inventory that would allow them to improve inventory levels and cash flow. Admittedly, most distributors work on a "push" basis with their customers. The reluctance from the manufacturers' viewpoint to a "pull" system indicates they want to show growth through increased sales. One example is a manufacturer offering significant discounts in December in an effort to boost year-end sales. This creates a *"sales bubble."* Distributors, however, still view earned income as part of any business model going forward.

We as an industry have to make the changes. We all have to play our part and we'll all get the benefits out of it.

Another suggestion is for the distributor and manufacturer to work together to develop "multi-use" items; for example, one SKU or product that could be used in multiple menus by the operator. This would reduce line items and create line items with higher volume, hence greater efficiency for the distributor. What the distributor does not want is multiple, slow moving, specialized items.

It is also felt that the manufacturers have a great deal of data including historical sales numbers, price fluctuations, raw material costs, etc., that could be shared with distributors. An effort could then be made to jointly develop cost reduction strategies with the goal of better servicing the end user, thereby increasing volume and profit.

FOODSERVICE MANUFACTURERS

"Transaction based rewards are just merely a way of driving a brand and customer loyalty by paying them!"

As one supplier said, *"The key to success is to get food to people faster and to lower inventories."* This reinforces the distributor's role as a service provider to manufacturers and to operators. However, most of the manufacturers are still in favor of fostering cooperation and strategic partnerships with the goal of mutually growing the business with the distributor.

SALES AGENTS/BROKERS

A key challenge cited by brokers is changing the mindset of *"how can I buy at the lowest price?"* Another significant challenge is getting the best product for the operator; not simply selling the cheapest product. Some brokers feel that distributors focus too heavily on price, which pressures manufacturers to reduce their costs and can potentially "cheapen" or devalue the brand in the marketplace. There is no easy answer.

Going forward, providing cost effective solutions to the customer represents the ideal solution. Some brokers feel this is a very inefficient and redundant industry with a lot of waste. Trading partners need to align their efforts. However, as noted repeatedly, this is hampered by the lack of trust in the system's partnerships. If trade relationships cannot be based on a true partnership, then at least a mutually agreed arrangement is required. Also, currently there is little market research to determine customer needs.

INDUSTRY OBSERVERS

Currently, it is estimated that 50 to 60 percent of all transactions are contractual. This has changed the landscape to a more predictable and transparent environment. Manufacturers now have set financial understandings and pricing. In a contractual setting, distributors are paid purely for consolidation and logistical services. Chains negotiate their supply chain based on the "whole picture."

QUESTION 7:

Is there any interest or merit in changing the focus of the system from procurement and the "buy" side to the operator and the ultimate customer, the consumer?

FOODSERVICE DISTRIBUTORS

There are two distinct points of view regarding this issue:

- Those who are happy with the current procurement system with monies being generated from manufacturer rebates and discounts, and
- Those who believe greater contact with the customer and shifting to a pull inventory system is the best and only way to go forward.

The common sentiment is the *"fear of the unknown and how do we do it?"*

Some feel the starting point is with the manufacturer as they have *"a great deal of valuable data and don't even realize it."* Distributors feel that they are only using the data collected by the distribution center (DC) for inventory control and not really looking at what the operators want and need. They feel the manufacturer could provide this information if the right methods of communication are used.

> Establishing trust is dependent on the behavior of all of the parties involved.

A couple of distributors are actively testing this "pull" type method, where the focus for generating profit is on per case mark-up rather than on the buy side. Both manufacturers and distributors admitted there is risk because of the *"transparency"* with the customer associated with this strategy. They also noted that while the chains are much more understanding and open to this, GPOs still maintain some traditional mistrust of how distributors determine prices and generate profit. This is certainly an obstacle to full implementation and will require a great deal of honest communications to establish a trust relationship.

The majority of distributors surveyed favor changing to more of a pull system and greater contact with customers. The technology is there to do this, but everyone struggles with the question of how to implement it and what to do with the data when it's collected. One distributor is testing a methodology that provides demographic information within a five-mile radius of the operator to assist in deciding which menu items best suit that area.

Those in favor of a stronger, customer-driven pull system also caution that consumers are *"fickle."* *"They will tell you in a survey they want healthier menus and more nutritious food, then turn around and purchase the opposite."*

On the positive side, one distributor feels that working more closely with manufacturers to understand products is critical. The example given was a milk-based sports drink that the distributor felt would be very sellable to schools, daycare, and other markets for children and young adults. The product was developed, launched, and enjoyed great success.

Finally, one distributor who was very favorable to pull versus push, stated, *"I want to fulfill that need more efficiently at a lower cost more than anyone else in the world."*

FOODSERVICE MANUFACTURERS

The "buy side" remains the traditional vehicle for creating margin; however, the focus has to change to the consumer. As one manufacturer put it, *"As far as the focus shifting to the consumer, the industry isn't there yet although it is certainly feasible that the market will eventually dictate this movement."*

Once again the "level of trust" among organizations has become the issue. Those relationships can be dictated by top management, but in some cases remain *"confrontational."*

Establishing trust is dependent on the behavior of all of the parties involved. One manufacturer example involved a request to a sub contractor to produce a particular product. The manufacturer submitted an RFP and stated it would be good for three years. The potential sub-contractor laughed and stated, *"You'll take the lowest bid and ask again in a year."* After assurances that this would not be the case, the RFP was submitted, accepted, and has now been in place for eight years without a request for resubmission.

Some manufacturers are concerned about larger distributors using *"pricing brackets"* based on volume. They feel this erodes the price competitiveness of their products with smaller independents. As one manufacturer put it, *"If you are going to enhance margins, you have to sell the whole picture, the big picture."*

SALES AGENTS/BROKERS

Brokers expressed interest in changing the focus of the system from procurement to a focus on the customer, but brokers generally feel that over the years distributors have controlled the system resulting in an "adversarial" relationship with manufacturers. Instead of simply driving the manufacturer's price down, brokers believe the supply chain needs to think about what is best for the operator and that this message needs to be driven back up the channel. However, the consensus is that the industry is too fragmented at this time to effect this change. Going forward, technology will play an important role in deciding this issue.

(Industry observer perspectives were addressed in response to question #6.)

QUESTION 8:

How can manufacturers and distributors enhance their operator focus?

FOODSERVICE DISTRIBUTORS

Manufacturer, Treat the Distributor as Your Customer!

The concern about manufacturers bypassing the distributor and forging deals directly with the customer only to have the distributor renegotiate another deal remains a source of frustration or, as one distributor put it, *"a vicious circle."* Distributors want manufacturers to treat them as the customer, trust them to manage the operator, and keep the communication flowing. It was also felt that both parties need to understand the operator's needs better. Manufacturing and logistics need to work together and realize that the operator is everyone's customer. Therefore, everyone needs to be working to enhance the operator's business by more than just reducing costs. A good summary by one distributor: *"Stop saying whose customer it [the operator] is! It's everybody's customer."*

We can't dictate to the operator what to buy. They know their business better than we do. Each of us needs to concentrate on what we do best.

Understand the Customer's Operations and Needs

One distributor commented that *"pushing case sales"* cannot be the priority. Both the distributor and the manufacturer need to understand how the operator works and their needs. Distributors are in a good position to understand these issues as they are in direct contact, weekly or daily, with the operator. The distributor needs to become more proficient at communicating the *"why,"* not simply the *"what,"* and then work with the manufacturer to craft a solution.

Manufacturers and distributors need to connect more frequently and efficiently with the operator, to get into their establishments and understand how they function. For example, operators are moving toward a smaller footprint for their businesses, resulting in less space for inventory and quicker inventory turns. *"The distributor has got to be able to help them with that."*

One distributor summed up the situation, *"We can't dictate to the operator what to buy. They know their business better than we do. Each of us needs to concentrate on what we do best."*

FOODSERVICE MANUFACTURERS

The manufacturer needs *"to be on the street"* to understand customer needs and their competitive environments. The goal should then be to design and produce well-researched, innovative products with an understanding that these products have limited lifecycle and new ones need to be in the pipeline.

Distributors need to be more customer-centric by stocking and fully supporting the new products of their manufacturing partners. This is how they will get the operators *"back on board."*

SALES AGENTS/BROKERS

Brokers felt that manufacturers need to better understand operator's needs, become open to making products that are responsive to those needs, and do more comprehensive research and product testing. The manufacturer must have a better understanding of the challenges facing operators and have a better market segmentation focus to successfully make and develop products that the operator wants.

Many of the manufacturer comments are applicable to the distributor as well. Distributors should not try to be all things to all people. *"If you are good in schools, become great in schools. If you are good in Mexican, become great in Mexican, etc."*

INDUSTRY OBSERVERS

Most agree that the 80/20 rule is in effect in the foodservice industry with approximately 80 percent of the volume produced by 20 percent of the accounts. This however does not mean that the remaining small accounts do not need attention. The challenge is to reach this smaller segment of the market and be responsive to their needs, without them becoming a distraction. Distributors and brokers can play a key role here, both in terms of service and communications. This is especially true for distributors as they are in touch on a daily or weekly basis with every customer.

QUESTION 9:

Question 9A: What makes a manufacturer "best in class"?

FOODSERVICE DISTRIBUTORS

Distributors felt that best in class manufacturers were *"forward thinking"* and had a focus on innovation—including in terms of supporting the distributor. Developing quality products, insuring on-time delivery, and working with the distributor to better service the customer as the end result were all top of mind. Distributors also felt it would be helpful to develop measurable standards of improvement and find ways to apply manufacturer market information to improve the supply chain and create synergies and efficiencies and *"becoming more interested in the customer's success beyond product sales and pricing."*

FOODSERVICE MANUFACTURERS

The fundamental attribute to being best in class as a manufacturer is to have a strong knowledge of the operator and what the operator needs. Manufacturers should also drive innovation in product development and make sure products are high quality and sellable.

Another attribute is to be *"deliberate"* and know how to act with the customer and distributor. *"If you are meeting with the distributor's Quality Control representative, make sure you have your own QC person there who is comfortable talking about the microbiology of your product."*

Another manufacturer had an even simpler suggestion, *"Just make sure your products do what you say they will do."*

Finally, be prepared to customize product if the demand is sufficient.

SALES AGENTS/BROKER

Brokers felt best in class manufacturers should present a solution management approach, designed to solve the market's needs versus simply selling products. Those who are best in class encourage strong trading partner relationships, are effective communicators, and are good listeners. Also cited was the need to:

- Develop innovative new products based on consumer insights and R&D,
- Provide a differential advantage and execute their strategic objectives,
- Provide needed leadership, ideation and innovation, and

- Above all, be efficient, have the right SKUs, be in the right categories, focus on brand establishment and identification, develop strong brands, have world-class talent, and focus on core competencies.

One observation was: *"Pick your strategy and execute it brilliantly."*

INDUSTRY OBSERVERS

Industry observers shared the following best in class comments for all four channel members:

- Understand your organization's position and do what you do best.
- Each organization has its role to play and must also understand its limitations outside that role. Again, trust and relationships come to the forefront. If you are doing right by your distributor and your distributor is doing right by you, then let the manufacturer *"sweat the new innovative products"* and let the distributor concern himself with *"getting them to the operator."*
- Let the operator make sure the end user gets the complete positive experience.
- Know who your customers are and what you are to them.

Question 9B: What makes a sales agent/broker "best in class"?

FOODSERVICE DISTRIBUTORS

Many of those surveyed are critical of the brokers as being *"too administrative."* To be best in class requires the broker to define their role and act on it. Brokers need to be transparent and not try to be all things to all parties. The general sentiment is that brokers need to engage and better understand the distributor, advise the DC, and be the recognized product *"experts."*

FOODSERVICE MANUFACTURERS

Manufacturers felt that best in class brokers need to:

- Know and understand the product and the company they represent,
- Stay close to the operator and jointly develop strategies to grow the business for both the manufacturer and the operator,
- Be transparent and communicate regularly and clearly, and
- Execute an aggressive sales strategy.

SALES AGENTS/BROKERS

Brokers felt that a best in class broker needs to:

- Know the market. Be the problem solvers, customer service, and strategic growth planners,
- Hire and develop *"world-class"* talent who are totally focused on the operator,
- Offer additional/supplemental services that support its core competency of being the front line contact to the operator,
- Embrace technology and accountability to trading partners,
- Invest in training for product, customer, and market knowledge,
- Deliver on promises and provide inspired leadership,
- Be strong enough financially to invest in technology and the development of a professional sales organization, and
- Execute well.

Question 9C: What makes a distributor "best in class"?

FOODSERVICE DISTRIBUTORS

The simple answer from distributors is to know your customers and bring value to them, and always be ready to innovate to reduce costs. As one respondent said, *"Be open-minded to see the inefficiencies."* All the distributors recognize the need to bring value to the customer and the supply chain overall. Exchanging best practices was also discussed, as well as the ability to communicate both up and down the supply chain. Many of the comments are philosophical and focused on the mentality or culture of the distributor rather than technological tools.

One distributor's comment is notable: *"I was at a seminar and was asked what's most important, your vendors, your customers, or your employees? Well, your vendors and customers don't get the care they need unless your employees are important."*

FOODSERVICE MANUFACTURERS

Best in class distributors are those who are service oriented to both the manufacturer and the customer. The best distributors will *"work the peripherals with the operator"* with the goal of helping them grow the business. Also cited was the focus to creatively shrink fixed costs and introduce more efficient ways to provide their services, *e.g.,* offer night time delivery or invisible delivery.

SALES AGENTS/BROKERS

Brokers felt best in class distributors need to:

- Provide service reliability,
- Be open to innovative products and work closely with manufacturers and brokers to develop skill sets that will enhance the operator's competitiveness in the market,
- Listen to the operator,
- Treat employees and vendors with fairness and honor agreements,
- Be honest and ethical and be characterized by a system of on time, complete orders and fill rates, and
- Design a *"strategic"* as well as a *"tactical"* agenda.

Question 9D: What makes an operator "best in class"?

FOODSERVICE DISTRIBUTORS

Distributors felt that best in class operators know the business and develop an intimate knowledge of their customer base. Perhaps best stated by one distributor, *"You can't turn a hamburger joint into a steakhouse."* The best in class operator also offers quality, service, and value to the customer and retains customers while growing market share. Other members of the supply chain must recognize that the operator is the one who ultimately turns *"product into cash"* and sends that cash back up the supply chain.

The issue of customer service was also mentioned. One distributor felt everything was turning into the QSR business with little time for interpersonal reaction with the end user. Another felt that those establishments that offered the personal touch and made an effort at personal interaction were moving in the right direction.

FOODSERVICE MANUFACTURERS

Manufacturers felt that best in class operators have a clear vision and understanding of the customer base and what the customer wants both in terms of menu and services. One executive stated it succinctly, *"Staying true to what you are good at."* In addition, operators need to demonstrate flexibility and have the ability to respond quickly to changing markets. Winning operators do not view the supply chain solely in terms of "price," but in the services, benefits, and resources it can provide to help operators grow their business.

SALES AGENTS/BROKERS

Brokers felt best in class operators are open to dialogue with trading partners that may result in new ideas and concepts. Additionally, they should honor commitments and embrace technology, consistently deliver their message, and be recognized for adapting and meeting customer (consumer) needs.

At a minimum, a best in class operator should provide outstanding customer service and real customer value by having strong management, innovation, price-value to customer, and menu enhancements.

QUESTION 10:

What role does the manufacturer's agent/broker play in the channel? What will this role look like in the future?

FOODSERVICE DISTRIBUTORS

In response to this question, there are two divergent views: those who see the role of the broker evolving, and those who find little justification for the broker's role. For the latter, in the current environment brokers are not viewed as bringing *"value"* for distributors and continue to be viewed as an imposed, necessary evil and additional cost.

The Changing Role of the Broker

Expressed views were that today, brokers are still mostly localized and seem to be little more than glorified order entry people. Some stated that brokers do not meet the manufacturers' needs because of their localization; they are in one market, but not another. Distributors view them as administrative in function and not very good communicators. For example, some distributors offer a financial incentive to large suppliers to provide the supplier's entire product to the distributor's total customer base with the stipulation that no other broker can get involved.

The general sentiment is that those brokers who will survive in the future are those who become better at dealing and communicating with the DC. They also need to be product experts who supplement both the distributor and the manufacturer sales forces. They will need to be more *"on the street"* dealing with product technical matters, tastings, training in food preparation, etc.

Brokers who remain localized will have to partner with one or two distributors, using them as the conduit to get their product to market. This will require relationships and trust, along with a closer working environment with the DC.

Evolution of the "Super Broker"

Logically, brokers or brokerage firms that represent national brands need to have access to markets on a national level. Their role will, to some extent, become a sub-contracted sales force for the manufacturer. They can still deal locally with distributors, but will be viewed much in the same way that a large manufacturer's sales agents are perceived today.

FOODSERVICE MANUFACTURERS

It is evident from the answers to this question that manufacturers have a greater appreciation for the role of the broker than distributors. One common thread is the need for the broker's role to change. The recommended change is to take on more of a *"product expert"* and consulting role for the manufacturer. In this role a broker could be a valuable supplement to a manufacturer's sales force or extension of that sales force. The manufacturer's sales force would then take on more of a technical and training support role with the brokers.

As one manufacturer stated, *"It's incumbent we give them more intellectual capital to work with . . . teaching them what goes on in our test kitchens, and giving them information as it relates to solving culinary and food science type problems for the operator community."*

The broker's expertise and knowledge is also valued both in terms of regional influence and industry experience regarding innovation. *"I think they could save us a lot of time from running down roads that other manufacturers have tried and were not successful."*

Private label again emerges in this conversation and the broker's role of reinforcing the brand has been mentioned. The overall strategy of private label was discussed and one large manufacturer stated that brand success depends on the category you *"play in."* For example, in the breakfast category, the perception is that *"kids in college want to eat what they had in their pantry back home."* Admittedly, strong front of house brands are able to take this position. Back of house items, such as trash bags, aluminum foil, etc., will be under much more "value" pressure from private label.

SALES AGENTS/BROKERS

Brokers feel their role should be to focus on the operator and push ideas up the channel by becoming an effective communicator between trading partners. In that role, they become the recognized authority or product specialist. The broker must become an extension of the manufacturer and be totally integrated strategically. In the future, the role of successful brokers will be in one of the following categories: regional, national, niche (*e.g.,* seafood), or conflict brokers.

"Standing pat is not a strategy," stated one respondent. Brokers are responsible for communicating the message from the manufacturer to operator. It is less about deal making and negotiating, which has become the manufacturer's function. It is more about providing real tangible value to the operator. An agent should be almost indistinguishable from the manufacturer. With the exception of financial and logistical issues, the broker should manage the product channel from the back of the plant to the operator.

While most want the evolution of the broker to happen immediately, all recognize that it will probably take five to ten years before everything settles. Channel members need to realize that brokers and agents do not scale up very easily. One broker commented, *"There has to be a level of patience that a lot of folks don't seem to have."*

INDUSTRY OBSERVERS

Observers felt that brokers need to be less administrative and more customer and product knowledge focused. A broker needs to be more than just a vehicle for taking orders. Brokers need to be proactive in guiding, consulting, and communicating across the supply chain.

QUESTION 11:

What will be the impact of the digital economy, GS1 US standards, and data synchronization?

FOODSERVICE DISTRIBUTORS

Everyone is anticipating in these areas, and everyone has some idea of how they are going to use them, but everyone is also very guarded about the cost and initial accuracy. Certainly, once implemented by companies choosing to adopt GS1 US standards, certain costs are likely to be driven out of the supply chain, but many have concerns about the price tag associated with it. Many of those surveyed feel it will take a longer time than anticipated to get these innovations in place for their companies and that once in place, the actual innovation and application of value begins.

Food Safety and Product Recall

Of those interviewed, there was broad recognition of the value that GS1 US standards and clean and accurate data can bring to food safety programs and to the execution of a recall of product for the companies using the standards.

If one looks at the lack of uniformity in data currently exchanged and determines the financial impact of a recall, then the noted changes would be welcomed.

With clean and accurate data, nutritional information, ingredients, and allergens can all be easily accessed and provided to customers. This will assist sales people as well by providing a quickly accessed reference point that can be used by operators who want to meet the special dietary needs of certain consumers, *e.g.*, those with gluten intolerance.

However, the greatest benefit will be in handling product recalls, currently a very labor intensive process. *"Small operators can't be bothered going through their pantries looking for a product they may have received,"* said one respondent.

With data standards and other "linked" systems, when a recall is initiated, the manufacturer can determine that the product is in distribution centers 1, 2, and 3. Distribution centers 1, 2, and 3 can now determine that the product was shipped to customers X, Y, and Z. Such knowledge will also include the amount of product, ship date, and other critical data.

FOODSERVICE MANUFACTURERS

Manufacturers interviewed were generally very positive about voluntary GS1 US standards adoption and data synchronization. Terms like *"good, terrific, and a wonderful opportunity"* are used. Most, however, are prudent regarding the *"how to"* portion of any implementation. This caution is tempered by the potential gains in transparency and cost savings that are anticipated from it. One manufacturer said it best, *"Foodservice transaction costs are about double what they are for retail. That's largely due to lack of synchronization of data."*

SALES AGENTS/BROKERS

Brokers feel these innovations will provide transparency in transactions and a seamless system for those companies that subscribe to the data pools and work on a trading partner-by-trading partner basis to increase data efficiencies. To paraphrase, everything will become more transparent: *"The cream will rise to the top."* This is likely to create a demand for greater accountability and greater pressure to perform. As a result, the channel should become more efficient and more objective/results-oriented.

Some expressed that voluntary adoption may be slow. Because of capital intensity, so many producers, suppliers, and users view technology as another added cost.

Its effectiveness will depend on how many trading partners actively participate. The potential benefits across the supply chain are potentially significant. One broker commented, *"These are non-proprietary, non-competitive issues that … should be on the top of minds of every company out there."*

INDUSTRY OBSERVERS

There has been an overall positive response to these initiatives from industry observers, especially from a standardization and cost savings point of view. Again, like the distributors and manufacturers, observer answers were guarded, but expressed the need for openness and a sharing of information for voluntary standards adoption to be successful.

QUESTION 12:

How do we build a model based on customer intimacy and strategic partnerships?

FOODSERVICE DISTRIBUTORS

It is generally agreed that the old model of *"protecting"* one's financial turf in product pricing has created an atmosphere of distrust in the industry. Those distributors who want to build a model based on trust know that overcoming this will not be easy. Transparency is regarded as a key element to accomplishing this.

As one distributor said, *"It is not so much financial transparency as the customer knowing how you get paid and what you get paid for."* This will be a critical step in moving toward strategic partnerships.

In the past, many dealt with the attitude, *"You bid on my business, I'll give you a three-year contract; the lowest price wins."* There needs to be an atmosphere of openness and negotiation to build strategic partnerships.

From the distributors' viewpoint, manufacturers who previously paid for performance now need to focus on developing partnerships. *"We need to move away from that and actually concentrate on selling product. Collaboration fosters trust."*

FOODSERVICE MANUFACTURERS

"The speed of the leader determines the rate of the pack and you've got to have one or two leaders that drag everybody into this."

Most manufacturers are positive about this concept and have some pretty clear ideas on getting back in touch with their customer base, to *"personally meet the customer, and not just interact on your computer screens."*

Manufacturers also expressed that the distributor needs to be more open in terms of access to the customer. This will require honest face-to-face planning and a sharing of expectations of what the partnership is going to deliver and who does what for whom. As with any goal, it must be measurable; successful partnerships must be based on a scorecard approach to what the partnership is achieving.

One manufacturer suggested that the following dialogue is needed. *"Mexican sauce is 10 percent, we're going to jointly execute it (a strategy). Here's what I (the manufacturer) am going to invest, here's what you (the distributor) are going to invest and at the end of 3 years your share in the marketplace is going to be 15 percent. That's where we are going to build the business model."*

Everyone involved will have to *"want to do it"* and foster an environment of *"trust."* One respondent believes that there will be a positive benefit if *"everyone works together to understand each other's cost of doing business and how to minimize it."*

SALES AGENTS/BROKERS

Brokers felt it is about trusting your trading partner. It's about mutual gain, not *"I win, you lose."* Brokers expressed the following sentiments:

- We need to break down barriers and to reestablish trust,
- No model can be developed until trust is present,
- There has to be codependency, a longer-term point of view, and building a relationship that includes the operator,
- Quarter-to-quarter plans that change on a whim are destructive,
- Select the right partner; establish a strategy that both sides win on, so that there is enough mutual profit,
- Invest in talent and technology to be as efficient as possible and think and act strategically,
- Strategies must start at the operator and work backwards, rather than from the manufacturer going forward,
- The process needs to begin with the most sophisticated segments, for example, the big multi-concept users, and
- The more transparent we become the greater the opportunity to develop more intimate and strategic partnerships.

IFDA and the IFMA play a large role in this process. These respected trade associations must continue to realign themselves to become the vehicles for change. They are in the best position to promote the sharing of mutual issues in the industry. Working in concert, IFDA and IFMA can identify the problems and help create dialogue so that supply chain participants can work to solve these challenges together.

INDUSTRY OBSERVERS

Two insightful comments came from industry observers. The first is that *"Trust is built on performance."* Second, *"We need to take a deep breath and go back to the future."*

Observers felt it would be helpful for supply chain members to reflect on the trust relationships that were the hallmark of the industry 30 years ago. It's not going to be a *"big bang,"* said one observer. Instead, it begins with one or two initiatives that show results. There will be an opening up of communications and cooperation when the fruits of these results are realized.

QUESTION 13:

What role(s) should industry associations play in improving the foodservice distribution channel?

FOODSERVICE DISTRIBUTORS

The consensus is that organizations such as IFDA, IFMA, the Foodservice Sales & Marketing Association, and the National Restaurant Association should play three predominant roles.

Engaging with Washington, DC and Regulations

Everyone feels a major role of trade organizations is to represent the interests of the industry on Capitol Hill. The objective is not to simply oppose legislation or regulation, but rather to propose common sense solutions that improve the industry, and help companies in the industry thrive as an important element of the nation's economy. In order to do this well, these organizations must know and understand the needs of their constituents, what the industry wants, what it needs, and perhaps most important, what the organizations can effectively do. Distributor engagement through IFDA has remained strong, even in a weakened economy.

The objective is not to simply oppose legislation or regulation, but rather to propose common sense solutions that improve the industry, and help companies in the industry thrive as an important element of the nation's economy.

Leadership

Many distributors speak of the need for trade organizations to take a leadership role. By clearly setting objectives and paths to reach them, time could be saved, and greater teamwork and cohesion would result in industry initiatives that can improve the overall supply chain for all participants. Leadership also includes being a watchdog for the industry on the legislative and regulatory fronts.

FOODSERVICE MANUFACTURERS

Like their distributor counterparts, manufacturers feel the major roles for industry associations should be leadership, government lobbying on behalf of the industry, and enhancing communication among all players. The leadership of the industry associations will be essential in helping facilitate standardization for those companies interested in, for example, GS1 US standards.

From a leadership standpoint associations need to present *"platforms that everyone can work together on."* Obesity was cited; *"How do we help the industry in general address this and other social issues?"*

The economic crisis had an adverse affect on industry association membership and participation as many manufacturers engaged in *"survival mode."* However, that is changing as the associations redefine their roles and the future becomes brighter. Perhaps one manufacturer said it best, *"I predict that in the next year many manufacturers will come out of their caves and return to the industry associations and also begin marketing and advertising again in a big way. They will realize that the storm has passed, the sun is shining, and it is time to shout from the mountaintops once again."*

SALES AGENTS/BROKERS

Trade organizations can be a strong industry voice on Capitol Hill. Associations need to take a strong advocacy role with the governing agencies to limit interference or regulations that do not really benefit the consumer. They need to be more proactive on research and education, bringing together major players and provide a forum to address common key issues.

Their whole goal is to help manufacturers and distributors collaborate better by learning to speak each other's languages. That's why this thing is so incredibly important.

While a collective voice for the industry is needed, trade organizations also must act as an advocate that the industry can use to get their point of view expressed without companies being identified and possibly targeted.

The trade associations are also under similar stresses that the industry players are experiencing. As electronic communication supplant the need to attend the traditional association meeting, there needs to be a new association model that addresses this world of high tech and limited time.

INDUSTRY OBSERVERS

Observers felt that industry trade organizations can provide leadership, become early adopters of innovation, and be ambassadors for change. Clearly trade organizations are in a position to establish platforms and represent the industry. One observer captured this sentiment: *"Their whole goal is to help manufacturers and distributors collaborate better by learning to speak each other's languages. That's why this thing is so incredibly important."*

APPENDIX A

Appendix A provides the survey instrument used with foodservice industry executives to solicit perspectives on the current and future relationship between distributors and manufacturers.

In general, reflecting on the foodservice industry, during the first decade of the 21st Century, how did we get to where we are today?

1. Specifically, reflecting on the distributor/manufacturer relationship, during the first decade of the 21st Century, how did we get to where we are today? What is your view of the current relationship between distributors and manufacturers?

2. What will the foodservice industry look like going into the second decade of the 21st Century?

3. What impact will the continued consolidation at the manufacturer, distributor, broker, and operator levels have on the foodservice industry?

4. Please identify specific challenges/threats/opportunities (to the foodservice industry in general or to distributor/manufacturer relationship, specifically).

    • Challenges
    • Threats
    • Opportunities

5. Specifically, how can manufacturers/brokers/distributors add value to the foodservice distribution channel?

    • Manufacturer
    • Broker
    • Distributor

6. Please comment on advantages and disadvantages relative to the current distributor/ manufacturer relationship which appears to be oriented toward product-centric and transaction-based rewards.

7. Is there any interest or merit in changing the focus of the system from procurement and the “buy” side to the operator and the ultimate customer, the consumer?

8. How can manufacturers and distributors enhance their operator focus?

    • Manufacturer
    • Distributor

9. What makes a manufacturer/broker/distributor/operator “best in class”?
    - Manufacturer
    - Broker
    - Distributor
    - Operator
10. What role does the manufacturer’s agent/broker play in the channel? What will this role look like in the future?
11. What will be the impact of the digital economy, GS1 US standards, and data synchronization?
12. How do we build a model based on customer intimacy and strategic partnerships?
13. What role(s) should industry associations’ play in improving the foodservice distribution channel?

APPENDIX B

Appendix B provides a list of foodservice industry executives that participated in interviews:

Rick Abraham	Foodservice Sales and Marketing Association
Mark Allen	International Foodservice Distributors Association
Jeff A. Braverman	Hawkeye Foodservice Distribution, Inc.
Dan Cassidy	KeyImpact
Bob Crawford	Perkins
Jim Cremins	Pate Dawson Company
Rich Ferranti	Rich Products Corporation
Randy Habeck	Admiralty Corporation
William C. Hale	The Hale Group, Ltd.
Mark Hayden	ConAgra Foodservice
Mark Hayes	Heinz North America
Thomas J. Henning	Cash-Wa Distributing Co. of Kearney, Inc.
Cara Johnson	Labatt Food Service
Boyd F. Jordan, III	Reinhart FoodService, LLC
Phil Kafarakis	McCormick & Company, Inc.
Jack Kelly	KG Associates
Blair Labatt	Labatt Food Service
Paul Lloyd	Ecolab, Inc.
John R. Martin	Martin Brothers Distributing Co., Inc.
Bill Mathis	Glazier Foods Company
W. Kent McClelland	Shamrock Foods Company
Maria Morgan	General Mills, Inc.
Pat Mulhern	Monarch Foods, Division of US Foodservice
Daniel A. Murphy, Jr.	Islandic, USA, Inc.
Larry Obergfell	International Foodservice Manufacturers Association
Tony Odorisio	Food Broker (retired)
Scott Panton	Perkins
William McFall Pearce	Performance Foodservice
Caroline Perkins	The Foodservice Content Company
Larry Perkins	Perkins
Larry Pulliam	Sysco Corporation
Herb Reichenbach	Reichenbach Associates
J. Michael Roach	Ben E. Keith Foods
Steven Scales	Campbell Soup Company
Al Silva	Labatt Food Service
Mark Spliethoff	Kellogg's Food Away From Home
Malcolm R. Sullivan, Jr.	Pate Dawson Company
Bud Taylor	Innovative Concepts
Roger Toomey	UniPro Foodservice, Inc.

INTERNATIONAL FOODSERVICE DISTRIBUTORS ASSOCIATION
1410 Spring Hill Road, Suite 210, McLean, VA 22102
(703) 532-9400   Website: www.ifdaonline.org