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Summary report on distribution problems

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1. Introduction

The European food sector produces numerous traditional food products (TFP). Studies on food types such as ‘healthy’ food, ‘functional’ food, GMO-food and organic food already exists. However, few published studies are related to TFP and even less to innovations in those food production systems.

TRUEFOOD – Traditional United Europe Food – is an integrated European project within the Sixth Framework Programme for Research, Technology and Development. The aims of the project are to improve quality and safety of traditional food products, to support the marketing and supply chain development of traditional food products and to introduce innovation into traditional European food production systems, through research, demonstration, dissemination and training activities. The project consists of four scientific (consumer science, food safety, nutritional quality, risk assessment) and four industrial pillars (marketing and supply chain organisation, impacts of innovation, demonstration and training activities).

Work package 5 (WP5) is part of the industrial pillar of the TRUEFOOD-project. Four different institutions of three different European countries participate in this work package: Ghent University/Belgium (WP-Leader), Campden & Chorleywood Food Industry Development Institute Budapest/Hungary, Progetto Europa Regions Rom/Italy and University of Milan/Italy.

The aim of WP5 is to develop strategies to improve marketing and supply chain organization methods for traditional food products. Specific objective are:

- (i) Compare the functioning of different traditional food supply chains (meat, dairy, vegetables, beverages) within and across member states;
- (ii) Identify and quantify the determinants of bottlenecks and success factors that small and medium size enterprises (SME) active in the sector of traditional foods are confronted with;
- (iii) Compare food producers’ perspective on bottlenecks and on success factors with that of consumers;
- (iv) Develop a benchmark instrument relative to marketing effectiveness enabling traditional food companies to evaluate their current position;
- (v) Evaluate the feasibility and acceptability of possible approaches to improve marketing capabilities;
- (vi) Develop indicators to determine the overall chain performance;
- (vii) Analyse the potential impact of innovative distribution systems for traditional foods.

To achieve these specific objectives, WP5 is divided into four subtasks:

- Subtask 5.1** Determinants of bottlenecks and success factors of traditional food producers (i - iii)
- Subtask 5.2** Benchmark for evaluating marketing management capabilities of traditional food producers (iv - v)
- Subtask 5.3** Indicators of overall traditional food supply chain performance (vi)
- Subtask 5.4** Innovative distribution strategies for traditional food products’ (vii)

2. Aim

This paper is part of subtask 5.4 and a basis for the investigation of innovative distribution strategies for traditional food products. The aim of this paper is to summarize the findings of the national reports on distribution problems prepared by CCH and PEG. The findings of the

national reports are based on the experiences of consumers (WP 1), producers (WP 5.1+2) and other chain participants (WP 5.1) related to potential distribution problems for traditional food products. These three parts are the main building blocks of the concept (Figure 1). For this task not the whole supply chain but only the **distribution chain** is considered, including the producer (focal company), intermediaries of distribution, and the consumers. Intermediaries consist of wholesalers, retailers, distributors, and sales agents. The aim is to explore the problems between the three stages of the distribution chain.

Since managing the distribution chain is a relatively complex task. Many of the theoretical arguments about distribution chains revolve around cost. Managers have to take into account the trade-off between the costs of using intermediaries in order to achieve wider distribution. Often, the small company has no alternative but to use intermediaries, often several layers of them, while on the other hand large companies do have the choice.

In order to tackle this complex task in this work package the focus will be on following issues:

- Marketing management
- Supply chain management
- Innovation

These three issues are specifically investigated regarding their contribution to:

- Distribution
- Added value
- Convenience
- Labelling

of traditional food supply chains.

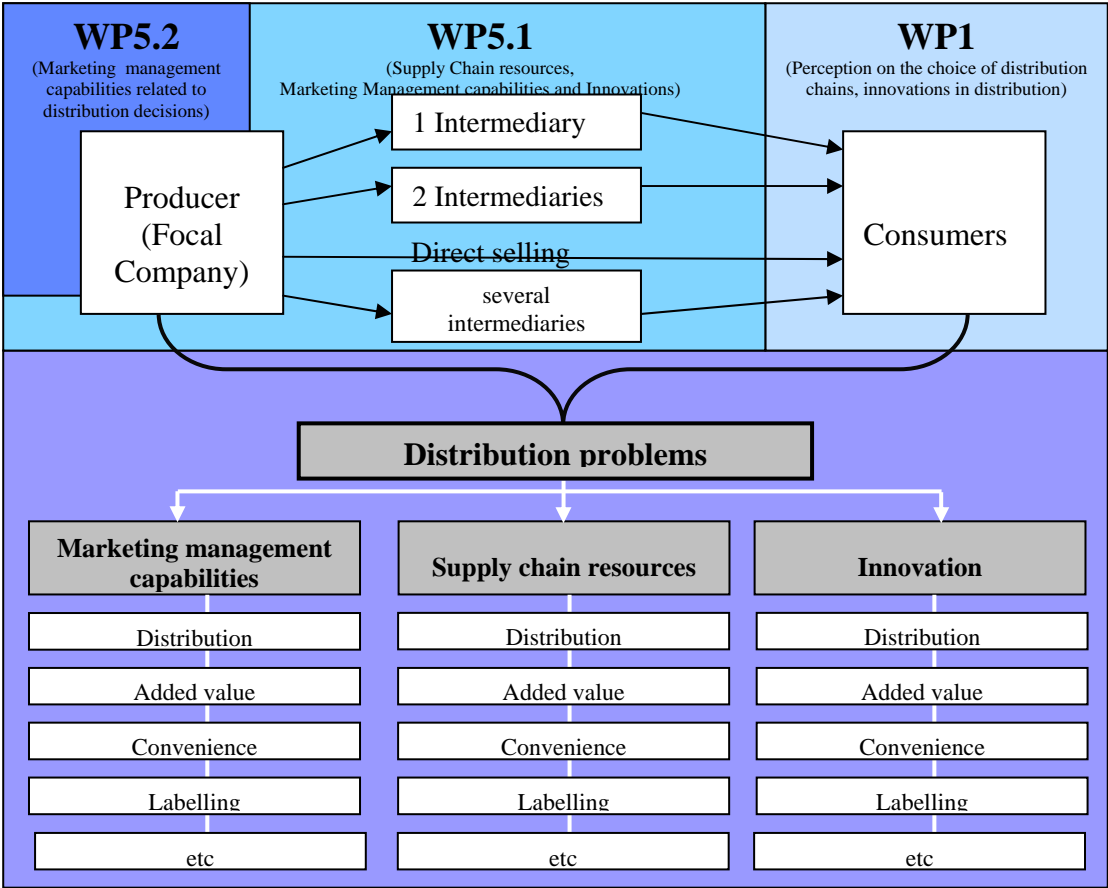


Fig. 1: Concept to tackle inventory and compliation related to distribution problems

3. The distribution chain

Distribution chains can have a number of levels. The simplest level exists, when there is a direct contact between producer and end-user with no intermediaries involved. The next level, when there is one intermediary (e.g. in consumer goods a retailer, for industrial goods a distributor). In large markets (such as larger countries) a second level, a wholesaler for example, is now mainly used to extend distribution to the large number of small, neighbourhood retailers (Kotler, 1991).

Figure 2 provides a detailed overview for the distribution chain of traditional food products, which will be explained in detail in the following sections.

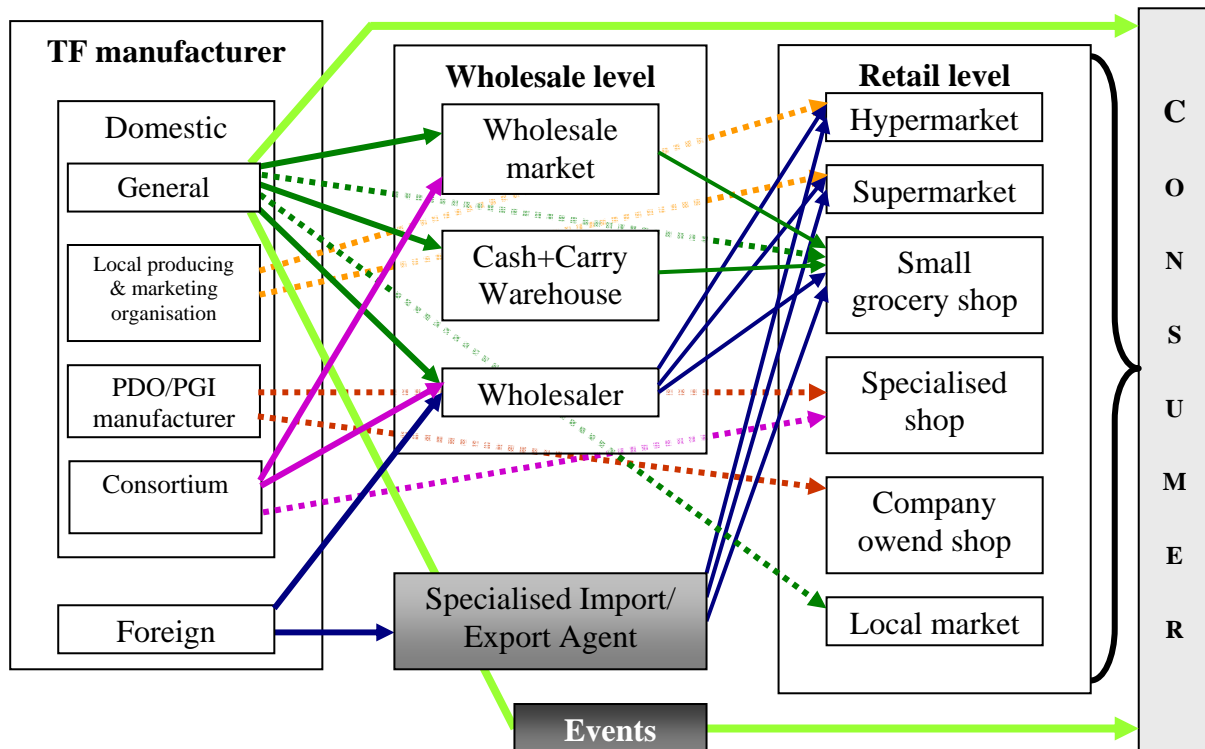


Figure 2: Distribution chains in the traditional food sector

3.1. The manufacturer level

At manufacturer level there is first a separation into domestic and foreign traditional food manufacturers. The **domestic** level is further divided into traditional food (TF) manufacturers in general and three special forms of organisations. **Local producing and marketing organisations** organise the production, packaging, selling, and marketing for a group of local producers. This type of organisation is typical for fresh products and is a solution particularly for very small TF manufacturers, which is supported by the EU.

PDO/PGI manufacturers produce products according the rules of the European label for 'Protected Designation of Origin' (PDO) or 'Protected Geographical Indication' (PGI).

A **consortium** is an association of manufacturers. It bundles specific tasks, such as marketing management, for their members.

Under **foreign** level all traditional food manufacturers are included who enter the domestic market through import. The foreign traditional food manufacturers enter the domestic market either through a wholesaler or by a **specialised import/export agent**. The latter is not necessarily a wholesaler, he/she is not buying the product, but is arranging contracts, deliveries etc. This specialised agent can be situated either in the country where the product is sold (domestic) or in the country where the product is produced (foreign).

3.2. The Wholesaler level

There exist three types of wholesalers in the traditional food market, namely the usual wholesaler, cash-and-carry warehouses and wholesale markets. The **wholesaler** collects products from different manufacturers and sometimes processes them further by e.g. slicing and final packaging. At **cash-and-carry warehouses** and **wholesale markets** the manufacturers or their representing organisation (consortium or local producing and marketing organisation) are offer their goods which are then sold by the retailers, often without any invoice or recipe.

3.3. The retailer level

The retailer level is more diverse than the wholesaler level. **Hypermarkets** are stores with more than 4000 sqm sales floor and the widest choice of grocery and non-grocery categories. **Supermarkets** have a sales floor between 100 and 4000 sqm. **Small grocery shops and specialised shops** have less than 100 sqm sales floor and service staff is always present to provide aid to the consumer. **Company owned shops** are integrated in the plant area and products are sold directly from the company to the consumer. Examples for **local markets** are fresh markets and farmer markets hold at periodic times, such as daily or weekly.

3.4. Direct sale

Direct sale embraces the direct contact between the food manufacturer and the consumer, without any intermediate (light green arrows in Figure 2). The food manufacturer is delivering his/her products by own means to the consumer. Mainly direct sale is restricted to an area of 20km around the production area. **Events** are a special form of direct sale. These events relate to product specific festivals, village festivals and other kinds of gastronomy festivals.

3.5. Distribution channels

The distribution channels (**arrows** in Figure 2) can be divided into short and long chains. The distance can be measured by the transactions between the manufacturers and consumers. This means, the more intermediaries between the manufacturers and consumers the longer is the distribution chain. The **shortest** distribution chain (light green arrows in Figure 2) is direct sale. A distribution chain were the food manufacturer is selling directly to the retail level can be called **medium** distribution chain (dashed arrows in Figure 2). A distribution chain can be stated as **long** (solid arrows in Figure 2) when all levels of the distribution chain are involved, namely the food manufacturer, the wholesaler, and the retailer.

4. Distribution problems

Distribution problems of traditional food producers will be described related to supply chain management and marketing management in traditional food distribution chains. First related problems are discussed, which are followed by possible solutions for the problems.

4.1. Supply chain management

Distribution problems related to supply chain management refer to:

- Logistic problems
- Availability of selling points
- Value added
- Financial aspects

These items and their possible solutions will be explained in detail in the following sections.

4.1.1. Logistic problems

The traditional food manufacturer needs to choose the **best fitting distribution channel** for his product. Short distribution chains (direct sale) have the advantage of direct contact with the consumer and less transport and logistic problems. In medium and long distribution chains several intermediaries are involved, which can increase logistic problems in the case of low collaboration between the intermediaries. Such logistic problems can be improved by installing route-planning and transport traceability systems, such as radio frequency identification (**RFID**) or **GPS**. The first allows the tracing and assurance of continuous supply of food from the manufacturer to the consumer. Route-planning systems or software using GPS allows the selections of the ideal route of distribution as well as fast correction of the delivery schedule in case of changes.

Especially in short distribution chains **own transport** can be a barrier for the food manufacturer if he/she does not possess of sufficient means for own transport, since it is very costly to maintain or to rent. Another logistic problem appearing for the traditional food manufacturer is **seasonality**. This refers to peaks in storage and transport capacity the food manufacturer has to cope with. The costs for transport can be decreased through **joint delivery** or **joint contracting** with a distribution service provider.

Furthermore, there is the problem of the concentration process in the retail sector. Recently retailers implement a **backward logistic system** including the construction of retailer owned depots, where the goods are collected and subsequent delivered to the stores. The costs are transferred to the food manufacturer, as he/she has to pay for the service of transport. In this way, no benefits or profits are passed to the food manufacturers, which in return can not afford investments necessary for improvements and R&D. Some food manufacturers reacted to this system by searching for other distribution channels than via such retailers.

The **information exchange** between food manufacturers and customers (wholesalers, retailers) refer to another supply chain related distribution problem. The information exchange needs to be improved in order to improve order handling, lead time, and customer complaints. There exist several **specific information technology** systems on the market, already affordable for SMEs. Those systems are internet based tendering systems, where customers can submit an offer, or virtual market systems, which are based on an electronically database offering stock management and the search for stock. Another specific information technology system is the electronic closed-access database and information sharing systems. This is an internal data platform between a certain group of supply chain members.

Finally, **traceability and quality/safety assurance** along the (distribution) chain are of increasing importance for the retailers. Particularly the traceability of the transport of imported bulk and unpacked fresh foods is problematic for the retailers. Another problem is the assurance or proof of product origin in the case of food crises for small shop owners why buy their products at cash-and-carry warehouses or wholesale markets without an invoice. A solution is the use of **EAN 13 or EAN 128 bar codes** according to the EC 178/2002 regulation. The latter provides more data for identification of the food than the first, including quantity, shelf-life, and transportation, which can be registered in the logistic system. For the assurance of food quality and safety assurance it is recommended to use standards which cover the whole distribution chain, such as the International Food Standard (**IFS**) and the standard of the British Retail Consortium (**BRC**).

4.1.2. Availability of selling points

The traditional food manufacturers face several problems related to the availability of selling points. For most of the food manufacturers the sale via **specific shops** amount only a little part of the total sales. Furthermore, these sales are restricted to a local or regional level. Especially in Hungary there are no such dedicated delicatessen shops or specific cheese or butcher's shops available, where a wide selection of traditional food products is permanently offered for sale for

consumers interested in premium quality, specialty foods. In contrast, most of the small and medium sized traditional food manufacturers are not able to supply the requested amounts of goods to the **large retailers**, since the food manufacturers have only a restricted production capacity due to their size.

Possible solutions are the **cooperation** with and supply of specific shops and gift shops in **tourist areas, local restaurants**, specific shops with a **wide permanent selection** of traditional food products, and the introduction of **specific shops or stalls into supermarkets**.

4.1.3. Value added

Value added in the distribution chain relates to further processing at the wholesaler/retailer level, such as **slicing** and **second packaging**, and to increased **convenience** for the consumer. Often there are poor agreements between the food manufacturers and the subsequent levels of the distribution chain, decreasing the sales outcome of the traditional food product. The problem can be solved from both sides. At the **supermarket/hypermarket** level the fresh traditional product could be **cut or sliced and packed** in front of the consumer. **Specialty corners** in the shop allow a wider accessibility of the traditional food product for the consumer. At the food manufacturers side there is the possibility to produce (frozen) **ready to cook/bake products**, which are delivered to and finalized by high equipped **small outlets** in the metro, on the street or in market halls. These small outlets possess refrigerators and high performance air circulating ovens.

4.1.4. Financial aspects

Supply chain related distribution problems in regards of financial aspects refer to the general lack of financial resources faced by SMEs. Though, another problem is the lack of understanding the benefits of **supply chain management** and the lack of willingness of **sharing costs, benefits and risks in** the agri-food supply chain. These lacks weaken the position of traditional food SMEs in comparison to the strong position of the **concentrated retailers**. Through the improvement of **joint activities** between traditional foods manufacturers the position can be strengthen in comparison to the position of the retailers and costs can be reduced.

4.2. Marketing management

Problems related to marketing management in the distribution chain refer to:

- Labeling
- Publicity
- Convenience
- Market segmentation

These items and their possible solutions will be explained in detail in the following sections.

4.2.1. Labeling

There are two main problems related to labeling in the distribution chain of traditional food products. The first is the **misleading use of labels of origin**. Some food producers or retailers use a label indicating the domestic origin of the traditional food product although a domestic supply is not possible due to season or climatic circumstances. Those products are imported and labeled misleadingly labeled as domestic products in order to sell them to a higher price. This is lowering the trust of the consumers in the reputation of the domestic traditional food manufacturers. The second problem is related to the **low knowledge and awareness of labels** of consumers.

A possible solution for the first problem could be the **implementation and use of voluntary assured/labeled schemes**, which are supported by the EU and are supposed to protect the

reputation of the traditional food manufacturers. Solutions for the low knowledge and awareness are discussed under the following section on publicity.

4.2.2. Publicity

Often the food manufacturers advertise and promote their traditional food products only on a **local or regional level**. The manufacturers do **not use media** such as TV, radio, national journals and national newspapers to promote their products, which is often due to the lack of financial resources. Furthermore, the **use of the internet** by traditional food manufacturers is very limited yet.

Approaches to increase the **publicity** of traditional food products are:

- attachment of flyers with the story of the product
- map with the place of origin (as used e.g. in the wine sector)
- picture of the main ingredient on the product label (as used in the Hungarian meat sector)
- use of national characters as marketing aid (flags, colors)
- Campaigns to raise awareness of PDO/PGI/TSG product labels
- Establishment and improvement of regional labels or umbrella labels
- Use of the new Guideline Daily amounts (GDA) - label to meet the requirements of health information of the consumer

Furthermore, the traditional food producers should try to **cooperate with institutions**, such as tourist agencies, the ministry of economy and transport, etc. to achieve support for national and international public relations.

4.2.3. Convenience

The distribution chain of the traditional food products can not ignore the facts of **changing lifestyles** of consumers, a trend towards **healthiness** and to increase **quality requirements**. The consumers of nowadays are more restricted in their time spent on preparing and consuming foods. Furthermore they are more concerned about their health and the quality and safety of the food products. In order to meet the consumer requirements on increased needs of convenience traditional food manufacturers should try to find **alternative/innovative distribution channels**, such as tie-in-sales or specific home delivery services. Tie-in-sales are cooperative sales, where products are combined needed for a certain meal or dish. Other approaches are the use of modified atmosphere packaging to increase the shelf-life and the association in product marketing organizations. The latter do the sorting and packaging of the traditional food products of a certain group of manufacturers. This approach is limited to few organizations and products yet. The use of modified atmosphere packaging is more accepted by the consumer than e.g. frozen food or microwaveable food concerning traditional food products (result of WP1).

4.2.4. Market segmentation

Most traditional food manufacturers do **not focus** on segmenting and targeting their markets. The main reasons are lack of awareness and the lack of financial resources. Nevertheless, there are **good examples** for the success of investing in market segmentation, such as the organic producers, which achieve premium prices due to that. Another **barrier** for conducting market research and segmentation is the attitude of the owner of the traditional food SME. In most of the cases he/she is responsible for the marketing strategy as well. However, most of the owners face several barriers:

- Lack of appropriate state-of-the-art systems for market research
- Lack of understanding the importance of market segmentation
- Conflict between traditionality of product and new developments and requirements of the market

- The “traditional” view of the company owners

At last the traditional food manufacturer usually can choose between two **market segment strategies**:

- Aggregative strategy (cooperation between several manufacturers – allocating risks and benefits among a larger number of subjects) or
- Selective strategy (e.g. niche market)

5. Innovation

In this section the main innovations described in the previous parts of this paper are summarized. The main innovation in respect of **supply chain management** is the use of information and communication technologies (ICT) in order to reduce costs. Such ICT systems are RFID, GPS, and data exchange systems with closed- or open access.

For **marketing management** it is important that the company owner or the marketing responsible person is open towards the needs and requirements of the consumer. These persons should apply market research and –segmentation in order to achieve knowledge about recent consumer needs and expectations. Furthermore, the publicity of traditional food products can be raised through efficient labeling and using voluntary assured/labeled schemes, which are supported by the EU, to protect the food manufacturer’s reputation.

Furthermore, **distribution strategies** exist in European countries. In some countries they are already developed. In other countries they are in the implementation phase. These distribution strategies are mainly not yet used for traditional food products. These strategies are:

- Box scheme (direct sale, home delivery of basket with fresh foods, mainly used in the organic food sector)
- Networks of food manufacturers, retail coordinators and private households (supporting genuineness and ethic foods, often used for organic products)
- Subscription farming (consumers act as shareholders, thus have impact on the decision of the farmer/food manufacturer)
- Email-selling (not very often used yet, due to lack of competences for efficient set up of a mailing selling system and consumer avoidance of not-in-contact shopping. The project SME-NET developed a system where no special hardware (e.g. computer) is necessary, but where the food manufacturers can use a public internet access to enter electronic closed-access databases)
- Tourist facilities (such as restaurants and specialty shops)

6. Conclusion and future research

The traditional food sector faces many different distribution problems. In some EU-countries the traditional food distribution chains face fewer problems than **in other EU-countries**. The first can be used as good examples for those who face more problems. In addition, it is worth to consider **other sectors** than the traditional food sector in order to get ideas for possible solutions of distribution problems. Good examples are the wine sector and the organic food sector. Nevertheless, the aim is also to explore **truly innovative distribution chains**, not used anywhere yet.

Therefore, based on this compilation, a **brainstorm guide** will be developed, with the aim to explore innovative ideas for distribution strategies together with traditional food producers.

In the subsequent step **innovative distribution strategies** are selected based on the results of the brainstorm sessions. The chosen strategies will be described in detail and tailored, integrating also the findings from WP1-4 as well as the previous stages of WP5.

References

Kotler, P. (1991). *Marketing Management*, Prentice-Hall.