

SURVEY CONCERNING THE EU HORTICULTURAL FRESH PRODUCE SUPPLY CHAIN

STUDIUL PRIVIND LANȚUL DE APROVIZIONARE CU PRODUSE HORTICOLE PROASPETE ÎN UNIUNEA EUROPEANĂ

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Abstract

This paper presents recent evidence of supply chain developments in the horticultural fresh produce industry, based on a survey realized with the occasion of several documentation visits in European countries (France, U.K.). A number of success factors were evident, to varying degrees, in all of the companies visited. These included: continuous investment (despite increasingly tight margins), good staff (to drive the process of innovation and develop good trading relationships with key customers), volume growth (to fund the necessary investments and provide a degree of confidence in the future), improvement of measurement and control of costs (in the pursuit of further gains in efficiency), and innovation (not just the product offer but also the level of service and the way of doing business with key customers).

Key words: fresh produce, supply chain, retailer

INTRODUCTION

In the past the horticultural fresh produce industry has lagged behind the manufacturers of fast moving consumer goods in its approach to marketing, clearly resigned to the status of commodity traders. The ascendancy of the multiple retailers and the importance of their label products has elevate the fresh produce industry to a position where suppliers have a veritable opportunity to escape of the commodity decoy and take the fresh produce category out of the trading environment.

Total imports of horticultural fresh produce in the EU reached 13,926,758 tons in 2007, this accounts for an increasing of 7% respect to last year. Imports value was 10,940 million euros. According to Eurostat, imports of vegetables registered the largest increase of 2,422,401 tons, (19%). Potatoes, tomatoes, garlics and onions, represented 66% of the total. Fruit imports summed up an amount of 11,504,357 tons, with an increase of 5%. The main importing fruits have been bananas (4,673,315 tons), citrus (2,142,922 tons) and soft fruit (1,307,963 tons). In value, imports reached 8,867 million euros.

Main importing countries were UK (2,593,729 tons), The Netherlands (2,285,868 tons) and Belgium (2,037,679 tons), the latter two due to their conditions as entrance ports. They are followed by Germany (1,336,797 tons), France (1,333,392 tons) and Italy (1,201,541 tons). Spain reached 916,300 tons. Besides, with 31%, it has one the highest growth rates of the EU and the highest among the biggest EU countries.

The research upon which this paper is based involved structured interviews with staff members of some successful fresh produce suppliers – importers (fruit) and pre-packers – to establish how they understand the relationship between suppliers and retailers and to identify some examples of best practice in the industry.

MATERIAL AND METHOD

With the increasing need to assure consumers that the food they intend to consume is safe and nutritious, the food industry is moving away from the traditional means of buying towards a more direct and reliable means of procurement where buyers exert greater control over prices, quality and production methods. Development agencies worldwide are giving increasing attention to the concepts of supply chain management in seeking to address the growing income disparity

between smallholder farmers and the urban community. The papers address the following questions: do producers know what consumers want? How can farmers and traders coordinate their activities to meet the needs of the institutional market? How is it possible to introduce and implement quality assurance systems for horticultural producers? Also included is a summary of the policy recommendations that were proposed during the presentations and interventions to develop competitive agribusinesses and agro-industries within the horticultural sector.

The purpose of the research is that to evidence the supply chain developments in the EU fresh produce industry, based on a survey realized with the occasion of several documentation visits in European countries.

RESULTS AND DISCUSSIONS

A number of success factors were evident, to varying degrees, in all of the companies visited. These included: continuous investment, good staff, volume growth, improvement of measurement and control of costs, and innovation.

The role of horticultural fresh produce in the market strategies

The role of fresh produce in the strategies of the major supermarkets has changed dramatically over the past ten years. Understanding the factors driving the growing importance of the fresh produce category provides the key to understanding their approach to vertical co-ordination and the steady move towards fewer larger suppliers operating in dedicated supply chains for specific supermarket customers.

There are four key factors that have driven the transformation of the fresh produce industry in recent years:

1. Supermarket strategies
2. Food safety legislation and supply chain integrity
3. Rationalisation of the supply base

1. Supermarket strategies.

Fresh produce has become what retailers describe as a 'destination' category – fresh fruit and vegetables is one of the few product categories (along with fresh meat and wine) for which shoppers will switch stores. It is also one of the two remaining categories (along with meat) which is virtually all own label and thus over which they can exert considerable influence and control. As a result, over the past fifteen years, the fresh produce department has moved from the back of the store to the front and has doubled its shelf area in store and the growth has occurred without substantial growth in consumption volume, but with significant growth in expenditure. The search for competitive advantage and a point of difference between supermarkets coincided, in the early 1980s with the consumer's move towards an increasingly Mediterranean diet, driven by heightened awareness of (and concern about) health and nutrition.

Changing the location of fresh produce within the retail stores yielded immediate benefits – some of them attribute a 50% increase in their fresh produce sales directly to the re-location of their fresh produce counter from the back to the front of their supermarkets – but inevitably resulted in problems over wastage, as retail managers lacked the knowledge to handle the increased volumes.

Pre-packing driven by retailers, not suppliers, substantially reduced wastage problems and enabled supermarkets, to introduce greater control over quality, presentation and pack size. Once retailers realized they could manage the category in-store, they were well placed to push ahead.

2. Food safety legislation and supply chain integrity

The 1990 Food Safety Act gave the process of vertical co-ordination, driven backwards from the retailer rather than forwards from the grower/processor further impetus, with the growth of own label increasing the need for improved due diligence and tighter supply chain control.

The 1990 Food Safety Act requires buyers to take all 'reasonable steps' to ensure that the food they receive from upstream suppliers is safe. It also means that upstream firms need to monitor

more carefully their food handling to satisfy their downstream customers. The critical word in the definition of due diligence is '*reasonable*'. This is sufficiently vague that it has encouraged retailers to take extraordinary steps to ensure the safety of products reaching them from their suppliers. If their desire to develop own label products had encouraged, them take a greater interest in what was happening upstream, the 1990 Food Safety Act compelled them to effectively take control, by instituting stringent quality assurance programs with their suppliers, with a particular emphasis on traceability. In effect, risk management became a key driver for greater co-ordination in the fresh produce supply chain. Retailers drew up codes of practice, covering all aspects of crop management and issued them to their suppliers.

The industry responded by developing a generic farm assurance scheme for domestic fruit and vegetables – Assured Produce – highlighting best practice in integrated pest, disease and crop management systems. Protocols have been drawn up for individual products, by growers and retailers (par example in UK the NFU-Retailer Integrated Crop Management Partnership) and are now established as the baseline industry standards for safety and quality. All of the major supermarkets now require all fresh produce to come from suppliers who are members of the assured produce scheme. A genuine (and visible) quality and safety culture is a '*must have*' for companies who supply the multiples.

3. *Rationalization of the supply base*

The search for improved supply chain integrity and greater consistency in the quality of fresh produce coupled with the need to squeeze costs out of the supply chain, through greater control (either directly, through grower/co-operative partnerships or indirectly, through pre-packers with their own grower networks) has resulted in the rationalization of the supply base, with retailers seeking to deal with fewer, larger, technically efficient and innovative suppliers.

The major supermarkets now deal with just a handful of suppliers in key product areas (potatoes, root vegetables, brassicas, salads, top fruit, stone fruit and soft fruit) and take every opportunity to pass responsibility (and associated costs) for quality control and procurement, storage and distribution upstream to their key suppliers, in return for which the chosen few are rewarded with volume growth. The latter is vitally important for suppliers, the bulk of who are privately owned and struggle to generate the cash surpluses necessary to maintain the level of investment in processing plants and new product development.

The race is on for retailers to find the best partners with whom to take on the competition. As a result, the power struggles between buyers and sellers that have characterized the European Union fresh produce industry for decades is being replaced by intense competition between chains. Whilst this will create opportunities for pre-packers and growers, it will also create growing tensions between supply chain partners, unless a way can be found to remove price as the key point of difference between suppliers (in the eyes of the retail buyer) and between retailers (in the eyes of the final consumer). It is here that innovation provides the key.

4. *Innovation*

Innovation drives value creation – new varieties (sweeter, juicier, crispier, improved visible characteristics etc), new formats (pre-prepared, mixed salads, stir-fry packs etc.), extended shelf life - and production efficiency (processing, storage, packaging and logistics technology). However, the shortening of product life-cycles and lead times for introducing new products and new technology, which reduce entry barriers – the process of commoditization - keeps the market moving on.

Product innovation is limited in the fresh produce category, but the difference in retail margins between raw and semi-prepared produce is substantial: the choice is between a 25% margin on raw carrots at 29p/Kg and a 25% margin on processed (washed, sliced, diced, shredded) at 89p/Kg. With consumers demanding more of the latter, it is easy to see why retailers are looking for innovative suppliers with the ability to invest in processing capacity and professional product development programs, along similar lines to the branded food manufacturers. Innovation has been a major factor driving the growth of own label in other key sectors, such as chilled ready-prepared

meals, and supermarkets are keen to exploit value creating opportunities wherever they can, particularly if it provides them with a point of difference against their competitors.

Innovation is difficult to achieve and exploit in a sector which offers low margins for suppliers and in which the rewards for first movers on new products (varieties, preparation, and packaging) are limited and short-lived. Moreover, it is likely that the growth in value added fresh produce is heavily dependent upon economic growth. Investment in processing facilities may be thwarted as we move into recession, when the growth in value added (prepared) salads etc. is likely to slow down markedly. Given the importance of growth and the fact that most of the growth has been in value-added products, investing in product innovation (and processing capacity to deliver them) is the only way in which fresh produce suppliers can break out of the commodity trap.

Dedication is a high-risk strategy but a feasible one for relatively small companies, but for larger businesses it is simply not an option. Technical excellence and innovation becomes even more important for those companies seeking to supply all of the major supermarkets – if retailers cannot have exclusivity they expect an irresistible offer.

Characteristics of fresh produce suppliers

The good firms are getting better – building relationships, developing systems, improving service levels and management skills – but the challenge to achieve year-on-year growth remains: margins are squeezed as volume goes up but prices are cut, yet the need to invest is ever present and privately owned firms in a highly competitive market need profitability to fund it. Even the best ones are finding it difficult in a market that is oversupplied. So what makes a good supplier and what are the characteristics of those that are growing their business in such a demanding and highly competitive environment? This section is focused on the criteria which the supermarkets use for assessing their suppliers, across the whole of their business not just fresh produce, and provide examples of best practice from the companies interviewed in this study.

The implementation of Efficient Consumer Response (ECR) and Category Management (CM) programs by the major retailers over the past few years has resulted in a fundamental examination, by retailers, of their suppliers. This process not only enabled supermarkets to identify those suppliers best equipped to implement ECR and CM, it also enabled them to identify the level of commitment from their fresh produce suppliers, which in turn assisted them in their rationalization of the supply base and the search for technical excellence and competitive edge in the fresh produce supply chain.

Factors which supermarkets regard as key indicators for the development of successful partnerships in the fresh produce supply chain:

- Pro-active relationships across all aspects of the business;
- Complete electronic integration;
- Information sharing;
- Innovation (supply chain management, new marketing strategies, new product development)
- Strategic relationship with customers;
- Financial stability ;
- Supply Chain Management;
- Cost Management (analyze, positive action, feasibility).

The role of market information

What becomes clear from the list of ‘success factors’ outlined at the beginning of this section is the need for size and sophistication. There is a distinct lack of market research in the horticultural fresh produce industry that struggles to break out of the commodity trap. Yet product knowledge is one of the few areas where suppliers can (and should have) an advantage over their customers. Small-scale fresh produce companies need to wear big company clothes and tailor them to their budget – market knowledge is one of the few remaining sources of countervailing power.

The high degree of inter-dependency which has been established between some suppliers and their retail customers reduces the risks associated with information sharing. With competitive

prices at the core of their respective marketing strategies, open access to cost and market data is a must.

It is perhaps significant that in the case of those companies who appeared to be doing the most in terms of market research and recognized the considerable benefits from so doing the Managing Directors had previous experience outside of the fresh produce industry, bringing with them experience from an fast moving costumer goods environment and a clear marketing focus to their strategic management. Moreover, effective market research does not have to be outsourced, at a cost that may prove difficult to justify. With the right people and the right level of motivation, cost-effective market research can be done in-house.

Strategic orientation of companies/organizations

This is a particularly difficult characteristic to measure and is closely linked to the expression of a (shared) strategic vision. It is essentially concerned with the people factor and the degree to which suppliers comprise the sort of people with whom the retail customer (and most notably the buyer) feels happy working. Culture is concerned with the ethos of the business and the attitude of employees (including senior management) to customer service, whilst structure is concerned with the way in which suppliers choose to communicate with their customers, at all levels of the business.

As with the other key characteristics identified as being of particular significance by retailers, all those companies interviewed in this study made reference to the importance of good quality staff, which most found difficult to attract and even harder to keep, given the limited career opportunities in a tight margin industry with a unattractive image for young graduates – a problem which the fresh produce industry as a whole needs to address.

All of the companies interviewed in this study had structured their businesses into account management teams, and in some cases these teams were run as strategic business units – independent profit centers with a strong customer focus. Such a structure enables suppliers to handle issues relating to exclusivity or dedication, even with a mixed customer portfolio, and facilitates the process of cross-functional alignment between customers and suppliers, which all those interviewed regarded as an important means of developing customer relations.

Despite the progress which all those companies interviewed had clearly made in terms of structuring themselves to meet their customer needs more effectively, there was a common perception that retailers had made little progress on their side to develop genuine category management teams, better equipped to break out of the trading mentality. Many of those companies interviewed expressed skepticism over the retailers' approach to partnerships, pointing at the central role of the buyer which has changed little in recent years, and the policy of rotating buyers on a regular basis, which makes it difficult (and costly in terms of the time it takes to develop an adequate level of mutual understanding between buyer and account manager) to build long term relationship.

Cost control

As demands from retailers on their fresh produce suppliers become increasingly exacting, the capability to measure the cost of increasing customer service is essential for those suppliers who seek to meet those demands – at a profit. All the companies in this study had invested heavily in recent years in IT systems which gave them more accurate costing, although every one of them recognized that their remained scope (to varying degrees) for improvement.

Measurement and control of costs go hand in hand and good measurement is often associated with core competence. Logistics is one function that many suppliers regard as a cost, yet some regard it as a core part of an integrated business and a genuine source of profit.

The EU, food supply chain is regarded by many as one of the most efficient in the world, yet there is still room for improvement, not least in the level of standardization. Retailers have gone to extremes in recent years to differentiate themselves from their competitors and, it would appear, make it increasingly difficult for suppliers to service several retail customers. As the rationalization

of the supply base continues and retailers become increasingly dependent on fewer larger players, so supply chain efficiencies will become increasingly driven by the suppliers, who are best placed to identify the costs of operating parallel systems.

Innovation

In a highly competitive market such as horticultural fresh produce, characterized by over supply and a commodity orientation, innovation is the only long term source of competitive advantage, which is why retailers place so much emphasis on selecting suppliers who demonstrate a desire and an ability to be innovative – not just in developing new products, but in all aspects of the business. The lack of product innovation is a feature of commodity markets. In the fresh produce industry, it is also a result of the proliferation of entrepreneurial (often family owned) businesses, in which the injection of creativity and an open mind – essential ingredients for innovation - is often lacking. The companies in this study who demonstrated the clearest understanding of the benefits of market research – an essential ingredient for innovation in the marketing mix - were run by people with experience in other sectors.

CONCLUZIONS

Consumers have a greater choice of top quality produce, all year round, and retailers have set out their stalls - to make fresh produce a destination category, attracting new customers in the battle for market share and generating handsome margins through predominantly own label product lines. Yet the trading environment from the suppliers' perspective does not reflect the success which retailers have had at store-level and the pressure on suppliers' margins is intense.

There are very few companies of the size and sophistication and with the resources and strategic orientation necessary to compete for both portions of the profit. What is also clear is that in order to compete in the value-added portion of the profit, suppliers need to build collaborative trading relationships with their customers, not least to gain a measure of strategic insight into the retailers' perspective on the future growth areas, but also to lock customers into innovative, but often high risk, investments.

The future is bound to see a steady move away from traditional commodity trading, with its emphasis on price, towards integrated supply chain partnerships, with much greater emphasis on value added and return on investment to all members in the supply chain. At the grower/pre-packer interface, the need for further volume growth will mean further rationalization of the supply base with the largest and most professional growers being rewarded with whole-crop marketing agreements on a cost-plus basis, which in turn will lead to much greater product differentiation and market segmentation.

The next decade will see a continuation of the process which has led thus far to a substantial increase in the scale, scope, sophistication and strategic importance of the fresh produce industry in the EU.

It is evident that the dominance of food retailers in food supply chains around the world is growing and it is surely only matter of time, at least in developed countries, before retailers around the world recognize the opportunities to drive value not volume in the fresh produce category, opportunities which are currently being exploited successfully by EU retailers and driving the future of the horticultural fresh produce industry in the EU.

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