FOODSERVICE MARKETING INSIGHTS

The Online Newsletter for Foodservice Marketing Professionals
From Franklin Foodservice Solutions and Dave DeWalt

Volume 2, Issue 8
August, 2004

IN THIS ISSUE:

REDISTRIBUTION UPDATE:
"Part 2 of John Tracy Interview"

FEATURE ARTICLE:
"Gimme Shelter"

A WORD ABOUT "SHARE OF STOMACH"

REDISTRIBUTION UPDATE:
"Part 2 of John Tracy Interview"

This is Part Two of an interview with John Tracy, President of Dot Foods. If you missed Part One, you can get it from the "Free Resources" section of my website (www.franklin-foodservice.com)

DAVE: Because Dot carries multiple manufacturers in most categories, you would seem to be "neutral" regarding which products you ship. At the same time, Dot has a large sales force and offers marketing program opportunities to the manufacturer.

Is Dot simply in the business of expertly fulfilling demand that is generated by the manufacturer, or is Dot in the business of influencing distributor demand for various manufacturers and brands?

JOHN: We are neutral in the sense that we make the products available to the appropriate distributors in multiple channels, and we do not try to provide an operator selling function or be the product experts technically. However, by selling the distributor on the value of our concept, and creating demand for products through our system, we are breaking down barriers for our manufacturers to sell product. These barriers typically include manufacturer's shipment minimums, long lead times, custom items with limited volume, and the distributor's lack of space to add product lines.

That said, our sales people are like others. If a manufacturer has created numerous barriers for the target volume (LTL orders) to move through our system, they are going to focus more on manufacturers that have less barriers in place for them to sell and influence our distributors.

The final point is that we have a variety of sales and marketing resources to help manufacturers access the market in a way they can't match on a direct basis. Our marketing activity including the most widely used web access to distributors in the industry (Dot Expressway), does a lot to influence demand. Most distributors have a good idea what they want; if not, our sales people will focus on the lowest-barrier manufacturer. Dot provides a manufacturer the opportunity to grow their sales through more customers in more channels, as opposed to just a logistics solution.

IMPLICATIONS FOR MANUFACTURERS:
This is a great clarification of a sticky topic. In our follow-up conversation, John said "it wouldn't matter even if I told our salespeople not to favor one supplier over another – it only makes sense that they'll sell what's easiest for them." When manufacturers place too many limits on who and what Dot can sell, they reduce the potential to take advantage of Dot's "marketing value" and new business potential.

Ideally, your redistribution program should be structured in such a way that you are comfortable "taking off the reins" and letting your redistributor sell all of the customers who fit your defined target criteria.

DAVE: If a manufacturer's price bracket structure is sufficient to cover the cost of shipping minimum orders, why does Dot need to earn this margin PLUS a redistribution allowance, when Dot's system is more efficient than the manufacturer's?

JOHN: We have never seen a manufacturer who has all of the cost to serve LTL orders (including Order Entry, Accounts Receivable, warehousing, transportation, and invoicing) in their price brackets. Almost all do not know the exact cost to serve each bracket, and most look only at transportation costs as a driver of their bracket structure. Price brackets primarily address the transportation cost difference, and even if it is more than that, we are providing sales and marketing support to grow a manufactures top line, which is much more than just cost to serve.

Ultimately, the marketplace determines what price an operator will pay, and thus what a distributor will pay. It is unlikely the marketplace will allow a manufacturer to arbitrarily set up prices within brackets without regard to the competition or create bracket pricing that has all the total cost to serve. This is one reason so many manufacturers have to deviate from their price list to get the business and why it is so critical for the manufacturer to understand cost to serve based on the size of the order and customer, regardless of what bracket or price they charge.

IMPLICATIONS FOR MANUFACTURERS:
As we've written before, there is a very strong relationship between price bracket structure and redistributor programs. But it's all meaningless without price discipline. If a manufacturer routinely provides truckload price exceptions on small orders, he cannot expect his redistributors to adhere to the price list, as they will lose volume.

Establishing bracket prices is further hampered by the lack of sophisticated accounting systems to capture all of the costs outlined by John. Manufacturers who make the effort to understand these costs, and have the discipline to enforce the resulting prices, stand the best chance of establishing a redistributor strategy and program with clear financial benefits.

DAVE: If a distributor who buys 10,000 lb orders from a manufacturer switches his business to Dot, he gains the benefits of faster turns, shorter lead times, responsiveness, etc., probably with no price increase. If the manufacturer makes lower revenue and incurs higher cost to put this business through Dot, how can he justify that decision?

JOHN: The issue you are raising above gets back to the challenge for everyone in the supply chain (including manufacturers, distributors, and Dot Foods) to understand their cost to serve. It is easy for Dot, or the manufacturer to pick out one customer or one instance that is less than perfect for either party. Far too much emphasis at times is spent on that one instance as opposed to looking at the entire program.

We don't deny that occasionally the distributors we serve elect to source a line from Dot Foods, even if they are above the target order size for that manufacturer. In most cases, we are able to show the manufacturer that these are aberrations, and are more than offset by the hundreds of distributors we serve that are buying far below the manufacturer's minimums.

We know, however, that in the long run no manufacturer (or no business for that matter) will sell anyone that lowers their revenue and raises cost. So if a serious case does occur, it will be corrected because if it isn't, the relationship will not survive for either party. The key is to have good communication as to what the target customer is and then review any exceptions to understand why and look at the cost to serve in that case.

IMPLICATIONS FOR MANUFACTURERS:
Many of the companies I work with express concern about this issue, whether it involves one large distributor, or several dozen. There is no doubt that a distributor will "be happier" if he can get your line from Dot with all of the benefits and no price increase, and it may feel like a win/lose situation.

If you are not comfortable accepting this situation as part of your overall redi program, perhaps there is an opportunity to convert the distributor's "happiness" to volume and profit growth for your line. Working with your Dot representative, the crux of the message could be "we're supporting you via our Dot program; let's talk about the new products, replacement of marginal competitors, and other growth opportunities enabled by our barrier-free redi strategy."

DAVE: Most accounting systems seem to lack the capability to truly reflect the cost avoidance associated with putting business through Dot. Does signing up for a Dot program require an "act of faith," or have you seen processes and systems that help a manufacturer "see" the cost offsets as well as the Dot allowance?

JOHN: We can help, and we have some tools to support that analysis, but the first key is for the manufacturer to commit internal resources to truly try and get to the true costs. Signing up for our program is hopefully a strategic decision with specific objectives, based on good business instincts and an understanding of costs. If the complete understanding of costs is not there, which it normally is not, there are usually excellent instincts on what is probably happening, as well as a plan to extend their reach by making the product more available and increase sales.

IMPLICATIONS FOR MANUFACTURERS:
Perhaps manufacturers were more willing to make the "leap of faith" in the past, but I see many working hard to quantify the impact of serving customers through redistribution vs. direct. The internal accounting issues will continue to be a stumbling block, until someone develops a way to capture the cost avoidance associated with redistribution, and reflect it in the regular financial statements.

When this happens (and I believe it will), a lot of the issues we've been debating will be obliterated and manufacturers will be able to focus more on maximizing the value of their redistribution programs.

Once again, I thank John for participating in this interview; it helped clarify my thinking and I trust you have found it beneficial as well. I welcome any and all of your comments.

Franklin Foodservice Solutions has been helping manufacturers solve the redistribution puzzle since 1996. E-Mail us (dave@franklin-foodservice.com) to receive a copy of our article "Does Your Redistribution Program Address These Realities?"

"Price is the reward you earn, and must collect, in exchange for doing the 'Other P's of Marketing' well.
-Robert Baker

THIS MONTH'S FEATURE ARTICLE:
"Gimme Shelter"

So we're visiting my folks a couple of weeks back, and at breakfast my Dad tosses the newspaper at me and says, "I see they indicted some of your buddies in the foodservice business…" And once again I'm stuck trying to explain the convoluted workings of the foodservice supply chain to the uninitiated!

In the classic supply chain model, goods flow downhill and each member of the chain adds value. The dollars flow back uphill, creating profit margin for each member in return for the value they added. But of all the links in the foodservice chain between the farmer's gate and the diner's plate, there is only one where the funds flow downhill, or backward, at such an alarming rate: between manufacturers and distributors.

I don't know what it is about the distribution business that makes distributors so dependent on subsidies from their upstream trading partners. And manufacturers certainly share the responsibility for creating this situation. But when this dependence leads to unsavory business practices, distrustful relationships, misleading of shareholders, and possible prison sentences, no explanation or excuse is adequate.

It seems that an enlightened distributor and manufacturer would want to work together to find a better way.

As an example, let's assume for now that a distributor must get \$.10/lb (or \$.50/case, or 7% of sales) from all of his suppliers to turn an acceptable profit. Instead of fighting over it, why don't we just acknowledge that it's so, provide it as a flat "distribution fee," and get on with building the business together? They're already getting it, and you're already paying it.

Instead, we have to go through annual negotiations for "label allowances," quarterly arm-twisting for "marketing programs," and daily games of "find the deduction" between Credit and Accounts Payable departments. It all creates a terrible administrative burden for manufacturers and distributors alike, and is the #1 source of mistrust and ill will for all.

I know, sitting here banging it out on my keyboard is the easy part. Figuring out how to make it work is hard. But I would pounce on the opportunity to help any and all manufacturers and distributors who want to truly fix what is truly broken in our business (and there are plenty of both reading this). If you have any reaction or would like to discuss this further, drop me a line and let's see where it goes.

"" I would enjoy working with Dave again as I have always appreciated his personal priorities and honest way of approaching business. " -National Sales Manager, Foodservice Manufacturer

---

AND FINALLY, A WORD ABOUT "SHARE OF STOMACH"

"Share of stomach" is a term that become popular in the food business years ago, but isn't heard that often these days. That's a shame, because I think it's a pretty compelling way of understanding the challenge food marketers face.

A look at the US Census website suggests there are 270 million Americans between the ages of 5 and 85. At a conservative average of 2,000 calories per day, that's 540 billion calories eaten every 24 hours in America by your target market. And if 50% are "away from home" occasions, that's a daily capacity of 270 billion calories.

Every day, you win when somebody chooses to use your bacon, pita bread, dill pickles, margarine, potato salad, baked beans and cheesecakes to satisfy a portion of that demand. And you lose if they just happen to find something else that day.

If anyone had the time, it would be fascinating to calculate the caloric value of your annual sales volume, and figure out your true "share of stomach" vs. the competition!

And who is your competition? More than just the guys who compete in your category. More than just the guys who compete in your channel. It's everyone who's trying to cram their OWN products down the same 270 million pie holes. And don't forget new products, as well as "dieting" and "doing without."

Look, I'm not trying to bum you out. Rather, I think it provides an interesting perspective when you consider that our industry works every day to fill what is essentially flat demand, and yet countless companies are able to thrive in this environment. So yes, strive for growth, but don't forget to appreciate the "share of stomach" you've already got!

Foodservice Marketing Insights is intended to share ideas and stimulate your thinking about current topics affecting your business. Your comments, criticisms, ideas and questions are all welcome, addressed to dave@franklin-foodservice.com