FOODSERVICE MARKETING INSIGHTS

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

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IN THIS ISSUE:

WARNING TO READERS!
This month we're going to do something a little different. I've been thinking about and working on the issues around distributor trade spending for a long time. I'm in the process of building a framework for understanding why things are the way they are, as a means of identifying what could change to eliminate or minimize trade spending as a source of friction between manufacturers and distributors.

I'm using all three sections of the June Foodservice Marketing Insights to present my opening thoughts. If you're offended by straight talk about trade spending or hope I'll "take sides," you may want to stop reading. Otherwise, there will be a lot more to come, so hop aboard for the ride!

REDISTRIBUTION UPDATE:
"What's the Difference?"

For starters, let's compare the business models of a redistributor and a distributor, and see if we can find out "What's the Difference?"

A redistributor provides value to its downstream trading partners (distributors) as well as its upstream trading partners (manufacturers). The value proposition for a distributor is that the redistributor provides efficient access to a wide variety of manufacturer goods. The value proposition for a manufacturer is that the redistributor provides an efficient channel to the distributor marketplace, especially to small-order distributors.

Similarly, a distributor provides value to its downstream trading partners (operators) as well as its upstream trading partners (manufacturers). The value proposition for an operator is that the distributor provides efficient access to a wide variety of manufacturer goods. The value proposition for a manufacturer is that the distributor provides an efficient channel to the operator marketplace.

So far, so good. Now let's look at how each is compensated for the value they provide.

A redistributor typically has two main sources of income:

1. The gross margin on the sale to the distributor (selling price less purchase price)
2. The redistribution allowance paid by the manufacturer

While it's an oversimplification, let's consider the gross margin as "payment for value provided to the distributor customer" and the redi allowance as "payment for value provided to the manufacturer supplier." How does that compare to the distributor's business model?

A distributor typically has two main sources of income:

1. The gross margin on the sale to the operator (selling price less purchase price)
2. The trade/shelter/marketing/earned income, etc. allowances paid by the manufacturer

As with the redistributor, it would seem to make sense that the gross margin represents "payment for value provided to the operator customer" and all of the manufacturer trade spending represents "payment for value provided to the manufacturer supplier."

So What's the Difference?

THIS MONTH'S FEATURE ARTICLE:
"The Difference"

The difference, my friends, is in the approach that redistributors take in seeking compensation for the value they provide to manufacturers, vs. the approach taken by distributors.

The best redistributors take a sophisticated approach that begins with helping the manufacturer understand his total cost-to-serve for various order sizes. Once these numbers have been established to everyone's satisfaction, the redistributor figures out whether he can profitably take over service to a defined set of distributor customers, at an allowance level that is in the range of the manufacturer's cost-to-serve. Final negotiations will take into account pricing issues, pickup locations, etc., but the point is this: everyone understands that handling orders and getting products to market costs money. The manufacturer willingly pays the redistributor to take over these functions for a set of customers. Everyone agrees on the value being provided, and what it's worth.

It seems to me that many distributors take a very different approach to making a case for manufacturer compensation. For reasons which go beyond the scope of this newsletter (but which I'll articulate in the future), these distributors have developed the practice of offering a menu of "marketing programs" with fixed prices. The menu includes label allowances, food shows, flyer programs, DSR time, etc., etc., etc. And the menu is presented along with a VERY strong recommendation of what items the manufacturer should "order." And in case the manufacturer is considering eating light or skipping dinner altogether, there are tacit suggestions, thinly-veiled threats, or overt statements that the distributor will choke off the manufacturer's volume if he doesn't participate at the distributor's prescribed level.

There's the difference.

The sophisticated redistributor is proving his value by helping the manufacturer understand the cost of serving the marketplace. He does so by putting it in the manufacturer's own terms, based on the manufacturer's cost of doing it himself.

The distributor in our example is putting forth a menu of "services" which the manufacturer doesn't necessarily want, and which have a value which is at best hard to quantify. And he's making it clear that failure to play along will result in harm to the manufacturer's business. Distributors who take this approach behave as if they don't have anything positive to sell to the manufacturer, only "the absence of a negative!"

But is there a better way?

"Too many distributors are too busy re-inventing the past to look up, re-assess what customers really want, and invent better ways to give them just that."
– Bruce Merrifield

"This goes for manufacturers, too!" – Dave DeWalt

AND FINALLY, A WORD ABOUT "WHAT IF?"

What if the next time you sit down to negotiate the 2007 program with a major distributor, he says something like this:

"You know, there was a day when foodservice distributors could make a decent profit just by selling products at a higher price than we bought them for. Those were the days of CFS Continental, S.S. Pierce, and Pacific Gamble Robinson. There were only a handful of manufacturers seriously committed to foodservice, and operators were happy to get nationally-branded products packed in "foodservice sizes." We all did well, and we all got used to that system.

"But as foodservice grew, more and more foodservice distributors sprang up. And more and more manufacturers jumped into the marketplace. And those manufacturers wanted their products in every distributor in a marketplace, so they wouldn't miss any operator sales opportunities. And so we distributors had to compete on price on the nationally-branded products, so our margins shrank. Soon we had to do something new to remain profitable."

"So we pursued private label as a means of differentiating our products, and we began to "look upstream" for dollars from manufacturers to bolster our bottom lines. And somewhere along the way, perhaps because we'd never asked manufacturers to compensate us for providing an efficient channel to the marketplace, we began to speak to manufacturers in terms of "sheltered income" and "marketing programs." And relationships have been going south ever since."

"But no matter how we got here, the fact remains that we provide great value to the manufacturer by providing you with efficient access to operators. That value comes at an ever-increasing cost, and it only seems right that our suppliers should be willing to bear some of that cost in recognition of the value we provide. As a starting place for quantifying what that is worth, wouldn't it be interesting to figure out what it would cost you to serve all of your operator customers directly?"

"I know in the past we've twisted your arm about participating in food shows, providing flyer allowances, etc. But if we can agree on a distribution allowance that makes sense for both of us, we should also be able to figure out if there's a marketing program that works for you."

Maybe I'm dreaming, but it seems that if we could all start over from this point, manufacturer/distributor negotiations could take on a new and better tone. And there might come a day when manufacturers will sign up for distributor allowances not angrily, not reluctantly, but willingly, recognizing that they are making an investment in a valuable trading partner.

That's enough for now, but I've got a lot more in store. All I ask from you is that you let me know if I'm missing anything, or egg me on if you think we might be on to something here. And thank you for reading!

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