Agriculture and Agri-Food Canada
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Food Bureau
Bureau des aliments

THE FOOD MARKETING AND DISTRIBUTION SECTOR IN CANADA

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PREFACE

The food marketing and distribution sector in Canada is the first link in the demand chain and the final connection in the agri-food supply network that draws and provides food products from the farm to the consumer's plate. This large and complex sector includes supermarkets, grocery stores, restaurants and fast food operations, as well as wholesalers, distributors and brokers which link retail outlets and food processors and agricultural producers.

Although the food marketing and distribution sector includes auxiliary sub-sectors such as transportation and trading houses, the document will profile the food retail/wholesale (excluding alcoholic beverages), foodservice and food brokerage sub-sectors and their relevance to the Canadian food processing and agricultural sectors. The state of the food marketing and distribution sector in Canada will also be compared to global trends.

The document completes the Food Bureau's post-farmgate presentation of the food sectors, processing and distribution, in Canada. The food processing sector in Canada is profiled in the Food Bureau document, *The Canadian Food and Beverage Processing Sector   An Overview of Opportunities and Challenges at the Turn of the Century.*

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Également disponible en français.

EXECUTIVE SUMMARY

The food marketing and distribution sector ("the food distribution sector") is the critical final link in the Canadian agri-food chain between food processors ("processors") and agricultural producers ("producers") and consumers, and represents a significant part of the Canadian economy. Approximately 145,000 retail and foodservice establishments accounted for sales of $91 billion in 1997, [1] $24 billion of value added and over one million jobs. This sector also purchases over $50 billion of processed food products and $3 billion of raw agricultural products.

The food distribution sector is divided into the food retail and foodservice sub-sectors. The food retail sub-sector represents outlets (e.g. supermarkets) where food is purchased primarily for preparation "at home" while foodservice (e.g. restaurants) represents food that is prepared mainly "away from home." The food distribution sector also includes food wholesalers ("wholesalers"), foodservice distributors ("distributors") and brokers that supply and service food retail and foodservice outlets.

Consumers   the Customers of the Distribution Sector

Consumers drive changes in the food distribution sector and the rest of the agri-food supply chain in Canada. The most important demographic and economic trends are aging of the population, increased labour force participation by women, higher levels of education, increasing ethnic diversity, declining levels of disposable income, increasing nutritional awareness and smaller household size.

Today's consumers want more quality, value and convenience, and the Canadian food distribution sector must continue to adjust to these demands.

Structure of the Sector

Food Retail - Retail food outlets sold about $50 billion of food and non-alcoholic beverages ("food") in 1997. Most (91%) food products are sold in traditional food stores including supermarkets, and grocery stores and specialty food stores such as bakeries. A small but growing portion (9%) of food sales come from "alternate formats" – drug stores, warehouse clubs (e.g. Costco), mass merchandisers such as Wal-Mart, and gas stations.

Sales in traditional supermarket outlets are split between chains[2] and independent stores. All major Canadian supermarket chains are involved in wholesaling and retailing operations. Chain-owned warehouses supply not only the chain's outlets, but may also supply franchised stores and independent grocers.

Some independent grocers are affiliated with a wholesaler through a voluntary buying group. Voluntary groups, such as IGA, take advantage of, for example, economies of scale. Affiliated independents account for most of the sales by independent grocers.

Unaffiliated independents are true independent operators. They are primarily supplied through a variety of suppliers: cash and carry outlets of wholesalers, smaller wholesalers or, in some cases, by distributors.

About 25% of store inventory is delivered directly from the processor; the rest is supplied by wholesalers. Brokers act as processors' sales agents and currently represent 31% of the items

1. This figure includes alcoholic beverages

2. Statistics Canada defines a chain as 4 or more stores. In the US a chain is defined as 10 or more.

moving through wholesalers' warehouses to food retail or foodservice. Most of the other items are sold through the processors' own sales forces.

This sub-sector is quite concentrated; on a corporate basis, the top four firms account for 55% of national sales. Regionally, corporate concentration levels may be higher.

Foodservice - Foodservice sales [3] reached about $32 billion in 1997. Seventy-five percent of these sales are in commercial establishments. There are a number of segments within commercial foodservice, the largest of which include the licensed and unlicensed restaurants and quick/counter-service restaurants.

Non-commercial foodservice establishments sold $8 billion in 1997. They include hotels, institutions (e.g. hospitals), recreational facilities such as theatres and arenas, vending operations, and foodservice establishments in department stores.

As in the food retail sub-sector, foodservice is characterized by both independent and chain operators supplied by local, regional or national distributors (the foodservice equivalent of wholesalers). Unlike food retail, major foodservice firms do not integrate retail and wholesale operations.

Foodservice is fragmented. The top 10 firms account for only about 25% of sales but some segments are quite concentrated (e.g. the top 10 unlicensed restaurants account for 85% of total unlicensed restaurant sales).

Performance

The retail food sub-sector and foodservice compete for a share of the consumer's food dollar. In 1997, the retail food sub-sector accounted for about 65% of consumer food expenditures (including alcoholic beverages). Foodservice's share declined sharply in the early 1990s due to the recession and, in the opinion of the sub-sector, the introduction of the Goods and Services Tax. However, its share has recovered slowly since 1991. The growth of the "ready to eat," "convenient meal solutions" or "home meal replacement" market has further blurred the traditional line between the retail and foodservice sub-sectors.

Food Retail - In real terms, sales have increased by about 1.5% per year, mostly due to population growth. In this stable but mature market, retail firms can increase sales only by taking market share away from other firms or by selling more non-food products.

Because of this intense competition, efficiency improvements have occurred. However, sub-sectoral financial performance declined significantly between 1988 and 1996. Returns are generally lower than in the US. In contrast, after-tax profit margins and return on assets (after-tax profits as a percentage of assets) of the 10 largest food retail firms were significantly higher in 1996 than in 1988.

Food retail captured about 15% of total agri-food trading profits between 1988 and 1995. The 10 largest retail food firms recently averaged about 101% of the return on assets of the 10 largest processors, up significantly from 60% earlier in the decade.

Foodservice - Real foodservice sales dropped 15% between 1990 and 1991 and, although they are slowly recovering, they have yet to regain their pre-recession peak. Sub-sector employment has followed a similar pattern of expansion, decline and subsequent growth. Employment levels

3. Unless otherwise noted, foodservice sales include alcoholic beverages.

were about 13% higher in 1997 than in 1988. Foodservice's market share is somewhat underdeveloped compared to the US.

The cyclical trend in foodservice sales drives the performance of labour productivity, profit margins, return on assets and investment spending. Due to an emphasis on consumer value, real sales per hour have increased since 1988. Foodservice's return on assets averaged less than either the processing sector or the food retail sub-sector.

Food Brokers - In sales, food brokers have performed well in recent years. Their grocery volume has grown by 33%, from 22.5% of warehouse items in 1991 to 30.9% in 1997.

IMPACT ON THE REST OF THE AGRI-FOOD CHAIN

The changing structures and business practices in the food distribution sector have a major impact on suppliers (processors and producers).

Consolidation Recent acquisitions in the food retail and foodservice sub-sectors highlight the trend to increased consolidation in the food distribution sector. Many factors have inspired these mergers, not the least of which is increased buying power.

The Canadian food brokerage industry is also consolidating in line with the move to national procurement and centralized purchasing in the food retail subsector and foodservice. Many small- to mid-size regional brokers are expected to merge or align to form national operations.

Consolidation in the food distribution sector has an important impact on the rest of the agri-food system as more of the business of suppliers is controlled by fewer buyers. This may place greater pressure on suppliers to deliver quality products at lower prices.

Private Label One of the most influential trends to hit the agri-food system in recent years has been the growth of private or control label products. These products are owned and generally developed by retailers, but their production is outsourced to processors. Consequently, retailers are performing functions previously carried out by processors, including product development, packaging, marketing and advertising.

The impact on processors of the significant category share of many private label products is unprecedented. Retailers are assuming some of the functions of a processor, but with a very important difference: the retailer has primary access to grocery shelves. Although the success of private labels offers market opportunities for some smaller processors, it has strengthened the retailers' role within the agri-food supply chain.

A major advantage of private label products is maintaining customer loyalty. Private label market share is expected to level off at around 30%. However, there may be more opportunities for Canadian retailers to sell private label in global markets. For example, Loblaws' President's Choice is currently sold in foreign markets, including the US and Latin America.

Private label is also prevalent in foodservice but is more "trade" than "consumer" oriented. Distributors' labels compete with processors' brands in areas such as ingredients, bulk packages (e.g. coffee) and in institutional catering (e.g. airline food).

Efficient Consumer Response (ECR) ECR allows distributors, processors and producers to cooperate and remove unnecessary costs and inefficiencies from the agri-food supply chain. The initiative includes many activities (e.g. Category Management,[4] Electronic Data Interchange [EDI][5] and Continuous Replenishment) designed to reduce the time and expense of inventory/ warehousing and to respond more efficiently to market demand. Foodservice's counterpart, Efficient Foodservice Response (EFR), was modelled after ECR.

Smaller processors may have to adopt business practices, such as EDI and case bar coding, that are better suited to larger firms. In some instances, brokers are providing this service. Eventually, suppliers that choose not to participate in ECR/EFR may lose business opportunities.

Despite the potential benefits, uptake has been slow. Efforts have focussed on the mandatory use of bar-codes and EDI standards with implementation targets set for May 1999.

Alternate Formats These non-traditional players provide much needed additional retail buyers for suppliers. However, alternate formats are especially challenging because many emphasize supply chain efficiencies and see groceries as a vehicle to increase store traffic.

Trade spending/Promotional allowances – This includes an array of potentially contentious incentives provided by processors to wholesalers/retailers such as "slotting fees" or "listing allowances." Some processors, especially small-sized, view slotting fees as a barrier to getting their products to market. Many processors question the efficiency of promotional allowances. Promotional allowances are not as prevalent in foodservice.

Home Meal Replacement (HMR) There is a growing demand for fresh or chilled, convenient, complete meals that are purchased in the grocery store and eaten at home. Examples include ready-to-bake pizza, chicken that is sold ready to heat and eat, and packages of pre-cut salads. Many grocers now offer complete meals ready to take home and eat. Suppliers must respond by suppling products that meet this need.

Consumer and Product Information Detailed knowledge of consumer preferences is leading to customized product offerings and more efficient product delivery. Suppliers would also be interested in such micro-marketing information and may consider forging new relationships within the distribution sector to develop and share such information.

Home Shopping Home shopping offers interesting potential as an alternate channel via electronic means such as the Internet. Home shopping could present an opportunity for processors to bypass the retailer, and fill some shopping orders directly from their warehouses or central depots.

Global Perspective

The demographic and technological changes that have caused Canadian consumers to become more value-focussed and Canadian firms to become more competitive are consistent with what is happening globally. As in Canada, food retail sub-sectors in other parts of the world (e.g. Europe) are highly concentrated. Also, while private label penetration is higher in Canada (25%) than in the US (20%), it is lower than in the UK (29%). Export opportunities for Canadian processors of private label products may exist in countries such as China and India as private label penetration increases.

4. Category Management is a method of retailing which analyzes groups of closely related products with the intent to achieve an efficient mix of products and profits.

5. EDI is the electronic transmission of business information.

CONCLUSION

The food distribution sector is playing an increasingly important role in the Canadian agri-food system by generating significant economic activity and contributing to the provision of one of the world's most affordable food supplies. The distribution sector has evolved from a passive sales venue to become an increasing influence in domestic and international food markets and in trading relationships within the agri-food supply system.

Increasingly, most processors have had to deal with retailers as branded product competitors instead of as vendors that sell their products. At the same time, suppliers are being asked to work more closely with retailers to examine and remove unnecessary costs from the supply chain. Meanwhile, fewer and fewer retailers result in fewer and fewer buyers; thus a more demanding business environment is created.

Opportunities will exist for suppliers that help the distribution sector respond to consumer needs by emphasizing value or react to the blurring of the interchannel competition between the food retail sub-sector and foodservice.

The Canadian agri-food system begins and ends with the consumer; the only constant is change. The distribution sector remains an important portent of these changes. Accordingly, suppliers must continue to acknowledge, understand and respond to these changes if they are to remain competitive.

INTRODUCTION

The food marketing and distribution sector in Canada, hereafter known as the distribution sector, provides the critical linkage within the Canadian agri-food system between the stages of food production (i.e. primary production, processing and assembly) and consumers (**see Figure 1**). This agri-food sector encompasses five separate but interrelated clusters or sub-sectors of services: food brokerage, food wholesale, food retail, foodservice distribution and foodservice.

In most cases, food products flow from food processors' ("processors") warehouses through intermediaries such as food wholesalers ("wholesalers") and foodservice distributors ("distributors") for final sale by food retailers ("retailers") and foodservice operators ("operators") to consumers. The retail and foodservice sub-sectors compete for a share of the consumer food dollar (including alcoholic beverages) with roughly two-thirds being spent in retail outlets for food that is mainly prepared and eaten "at home". The remainder is spent on items prepared "away from home" in commercial and institutional foodservice establishments.

The distribution sector is a major component of the agri-food system (**See Table 1 and Figure 2**). In 1997, it represented more than $91 billion in food and beverage[6] sales (**see Figure 3**) to consumers and provided over one million jobs. The sector purchased approximately $ 50 billion of processed food and beverage products and $3 billion of raw agricultural products. In the process, the distribution sector generated about $24 billion of value added economic activities – an amount equivalent to the combined value added economic activities derived from food processing and agricultural production in Canada.

Despite its significance, the role and impact of the distribution sector in the agri-food system has not always been evident or well understood. Today, the food distribution sector provides more than a sales venue for value added products in both the domestic and international markets. Its influence extends throughout the supply chain from the consumer to processors and agricultural producers ("producers"). As such, food distribution firms play an increasingly important role in interpreting and influencing evolving consumer preferences, as well as in the development of consumer products and services. In doing so, the distribution sector indirectly helps to shape the organization and competitive behaviour of the food processing and agricultural sectors in Canada.

A number of trends and issues are driving change in the food distribution sector in Canada. These issues include:

- the growing market share of non-traditional players,
- an increased blurring of competitive trade channels,
- major corporate mergers, acquisitions and evolving corporate strategies,
- the need to increase consumer value, and
- Internet shopping and consumer-direct retailing.

6. "Food and beverage" includes alcoholic beverages; "Food" refers to food and non-alcoholic beverages only; "Grocery" refers to all products sold at retail grocery outlets. Although the retail sale of food and grocery products is highly integrated, this study focusses on food products and wherever possible the data refer to food or food and beverage products.

On the consumer side, there is an increased emphasis on general wellness and health concerns, increasing consumer awareness, time pressures, declining standards of living, as well as powerful demographic changes including an aging population and emerging ethnic segments.

As an example of how the distribution sector has responded to changing consumer needs and trends, consider the evolution during the past century in the preparation of a food product such as a cake. At the beginning of the century, the food distribution system tended to market only the food ingredients such as flour, eggs and sugar which consumers used to prepare a cake at home. By the middle of the century, responding to the demands for convenience, more value added products appeared on grocery shelves, such as cake mixes which reduced preparation time by eliminating the need to mix most of the food ingredients. Today, distributors offer frozen and fresh-baked cake products as well as smaller portions such as single servings of cake.

Food distribution in Canada has changed dramatically since supermarkets and fast food chains first appeared in the post-war years. Historically, food outlets were the “final link” in a supply chain that “pushed” food items to a passive mass market. However, driven by the strong forces of demographics, income and technology, the distribution sector has evolved from simply a passive, downstream sales venue to become a key player and an increasing influence in domestic and international consumer markets and in trading relationships within the agri-food supply system. As consolidation continues within the distribution sector, the influence of large wholesalers, retailers and foodservice firms will undoubtedly increase.

This profile provides an understanding of this sector’s current role within the agri-food system, its impact on the production and processing of agri-food products, and the changing relationships and global trends that will move the food sector into the 21st century. An awareness of, and fast response to, these trends and changes are keys for the competitiveness of Canadian agri-food products at home and abroad.

CONSUMER MARKET TRENDS

Demographics

Canada's population currently stands at 30 million people, nearly three quarters of whom reside in urban areas. Canadians are migrating from east to west – populations of Ontario, Alberta and British Columbia are expanding at the expense of other provinces. While the Canadian population is not expected to grow significantly in the coming decades, current birth and immigration rates will result in an annual increase of about 1.2%. Much of this growth will be the result of immigration, as Canada's birth rate is well below levels needed to sustain population growth.

The make-up of the population is changing in terms of age structure, ethnic diversity and the size and composition of Canadian households. The working population or "baby boom" is greying, the number of seniors has doubled from 25 years ago, and Canadians are living longer. The combination of reduced birth rate and growing life expectancy means that, by the year 2011, the median age of the Canadian population is expected to be nearing 40 years, and by 2016, about 44% of the population will be 45 years of age or older.

In the case of ethnic diversity, sources of immigration to Canada have changed greatly. Before 1961, 95% of immigrants to Canada were from the US and Europe. Asia and the Middle East have become major sources of immigrants to Canada, accounting for 56% of the immigrants who arrived in Canada between 1991 and 1996. Today, Central and South America, Africa and the Caribbean are also increasingly significant sources of new immigrants. Given the declining domestic birth rate, ethnic Canadians will represent an increasingly greater portion of the Canadian population and, accordingly, an increasingly important segment of consumer influence.

The average size of Canadian households has fallen, to the current level of 2.6 persons. This declining household size reflects an increase in the number of single-person, lone-parent and childless-couple families.

INCOME

Linked to these changes in the size and composition of Canadian families have been fundamental changes in the labour force. The participation rate of women has increased steadily – dual-earner families are as common today as single-earner families were in the 1960s. The number of families with more than one earner and family members with more than one job is also increasing.

The after-tax or disposable income of Canadian consumers has stalled since the early 1980s and has actually been eroding throughout the 1990s. Real per capita disposable income in 1997 stood at about 9% lower than its peak in 1989 **(see Figure 4**).

DEMAND

The distribution sector, together with the rest of the agri-food supply chain, face many challenges in meeting the changing needs for the products and services of a diverse and demanding consumer population. Gone are the days of homogeneous markets – today's vendors are targeting specific segments or niches within the population. This population diversity, combined with the fast pace of life and family time pressures, means the following:

- Consumers want additional convenience in the foods they buy – but not necessarily at the expense of value, taste or nutrition. Canadian consumers still enjoy cooking, even if it means assembling quick meals from partially prepared ingredients, and they want these foods packaged in sizes to match the needs of their family. Single-serving portions are becoming increasingly important.

- Consumers want service in the stores they shop in – this may include banking, dry cleaning, florists, rest areas and foodservice/take-out establishments located near the entrance for quick purchases.

- They also want to be able to buy food wherever they are or wherever they are going. Supermarkets will continue to account for the bulk of food purchases, and are actively competing against specialty and convenience stores for market share by offering fresh baked goods, fish, greater varieties of ethnic products, and by opening for extended hours. But non-traditional outlets such as drugstores, gas stations, discount stores and clubs are also selling an increasingly diverse range of food products.

- Restaurants and other foodservice operations will continue to play an important role in meeting consumer food demands. Despite a significant decline in foodservice's share of total food spending in the late 1980s, it has almost regained this lost share. But Canadian consumers will continue to search for food and menu ideas that both offer value for their dollar and support their keen interest in food. Canadian seniors are better-off financially and more physically active than ever before, and represent an expanding market opportunity for foodservice.

FOOD RETAIL / WHOLESALE SUB-SECTOR

The retail/wholesale food sub-sector is comprised of retail food outlets and associated wholesalers engaged in the sale of food and non-alcoholic beverage ("food") products that are purchased by consumers mainly for use in the preparation of food at home. The retail outlets represent the critical link with consumers in the agri-food chain and include a wide variety of formats and levels of service. Traditional retail food stores include establishments primarily engaged in the sale of food products such as chain supermarkets, convenience stores, independent grocery stores and specialty food shops. Non-traditional or alternative retailers include retailers such as warehouse club stores, department stores, drug stores and gasoline retailers, whose principal sales are mostly non-food products but which also sell food products.

Wholesalers are the principal links between processors and retail outlets. They provide a variety of services such as warehousing and efficient physical distribution of the product to retailers, either directly or through third-party service providers.

SIGNIFICANCE

The retail food sub-sector[7] is one of the largest in Canada. It is second only to automobiles and parts, and accounted for about 25% of total retail sales and 10% of all household spending in 1996. In 1997, Canadians spent some $50 billion on food and non-alcoholic beverages from retail food stores and outlets which employed about 400,000 people. At the wholesale level, sales of food products are the third largest trade group, following "other products" and "industrial machinery and equipment." This category employs an additional 98,000 Canadians.

During the past decade, annual consumer expenditures on food products have risen steadily, on average by about 3% (**see Table 2**). This rise is due to the combined effects of population increases, price inflation and consumer demand for enhanced value-added food products. In real terms, annual retail food sales have been growing by only about 1.5% . Population growth accounts for almost all of this growth. Consequently, this sub-sector is frequently described as a mature but stable market.

STRUCTURE

Traditional supermarkets and grocery stores account for most of the $50 billion of annual retail food sales in Canada (about 83% in 1996) (**see Table 3**). Other food stores include specialty food shops such as bakeries and meat markets. This is the second largest food retail group in Canada and accounts for about 8% of retail food sales. Non-traditional retailers (e.g. club stores such as Costco), drug stores and mass merchandisers (e.g. Wal-Mart) accounted for an additional 9% of sales in 1996. Their collective share of total retail food sales has increased by 3 percentage points since 1989. Since almost all households shop for food and do so frequently, selling food products often provides an excellent way of increasing consumer traffic within non-traditional food retail outlets.

Type of Outlets

There are about 36,000 traditional food stores in Canada consisting of chain supermarkets and convenience stores, independent grocery stores and specialty food stores (**see Table 4**). Most retail food sales occur within chain and independent grocery stores.

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7. Generally, retail food stores sell grocery products that represent food and non-food items. In 1997 grocery sales were an estimated $65 billion. The document may reference "food" or "grocery" as the context requires.

Four or more grocery or convenience stores under single ownership constitute a chain. In 1997, fewer than 80 chains operated nearly 8,000 chain grocery and convenience stores in Canada. These outlets accounted for 51% of traditional food store sales. Most chains owned fewer than 50 stores. Larger chains, including Loblaws, Provigo, A&P, Sobey's and Safeway, accounted for the bulk of chain sales. Chain supermarkets represented only 6% of traditional retail outlets but accounted for 45% of traditional retail food store sales. Convenience stores accounted for approximately 6% of retail food sales.

The independents' share of traditional retail food store sales was about 41% in 1997. Although their market share is similar to the chains', over twice the number of independent outlets exist in Canada. Independent grocers can be classified as affiliated or unaffiliated.

Affiliated or voluntary group independents group together to benefit from volume purchases from their sponsoring wholesaler. In many cases, the wholesaler is owned by a retail chain; thus, the distinction between the chain's corporate retailer and the independent franchisee may be fine. This group of independents, such *as Your Independent Grocer,* includes 5,200 stores that handled about 35% of retail grocery sales, or nearly $20 billion in 1997.

Unaffiliated independents are single, unaffiliated operating units. Such truly independent operations accounted for about $3 billion or 6% of traditional retail grocery sales. While their market share is small compared to the chains and voluntary group independents, this group is very large. Unaffiliated independents totalled more than 13,000 or about one half of the traditional grocery outlets in Canada.

Chain supermarkets, with average annual total sales per store of $16 million in 1997, are much larger than either affiliated independents, which averaged $3.8 million in total annual sales per store, and unaffiliated independents, with annual sales per store of $0.25 million. Overall, the number of grocery establishments, excluding specialty stores, has declined by 15% since 1989. This rationalization has occurred exclusively within independent grocery establishments which declined by 30% during this period while the number of chain establishments increased by about 20%. Such rationalization has increased market share for chain supermarkets and large independents at the expense of smaller-sized independents. Therefore, although most retail grocery outlets are relatively small owner– managed businesses, increasingly the sub-sector is dominated by large retail/wholesale corporations. The majority of food retail firms are Canadian owned, with A&P and Safeway the two notable exceptions.

Responding, in part, to changing consumer preferences for increased food product variety, the number of items in the average Canadian supermarket has doubled from 9,000 to almost 18,000 between 1991 and 1996. Correspondingly, the average supermarket size has increased from 18,000 to 26,000 square feet during the same period – an increase of about 40%. Some supermarkets may be as large as 60,000 square feet and carry more than 25,000 items.

Composition

Chain supermarkets in Canada are similar to US counterparts on the basis of grocery sales per store, but capture a smaller percentage of total retail grocery sales (about 45% vs. 60%). On the other hand, independent stores represent a greater percentage of grocery sales in Canada but operate much smaller stores in terms of average total grocery sales than their US counterparts. This structural difference may be attributed in part to the greater incidence of franchising in Canada resulting in more "independent" operators, but perhaps more importantly, due to definitional differences. In Canada, a chain constitutes ownership of four or more stores; in the US a chain is 10 or more stores. However, the structure of the retail food channel (share of sales of traditional vs. non-traditional stores) in both countries in terms of share of sales among supermarkets, warehouse stores and other types of outlets appears quite similar.

The Canadian retail sub-sector has often been characterized by industry observers as being overstored (population per store) by a factor of more than two to one compared to the US. Conflicting explanations of this observation range from the Canadian marketplace being less efficient than the US market to Canada being more competitive. However, a comparison of recent supermarket densities in major Canadian and US metropolitan centres does not readily support this characteristic. **Table 5** indicates that Canadian cities are widely dispersed among the rankings of US and Canadian markets (see Table 5). In addition, alternative measures of population per retail store also indicate comparable ratios between Canada and the US.

According to a major industry association survey in Canada and the US conducted on behalf of the Canadian Council of Grocery Distributors and the Food Marketing Institute, Canadian grocery stores are described, on average, as being much smaller and not carrying as many items as US supermarkets. However, comparisons of this type are difficult and the results are sensitive to many factors, such as the types of formats included in the survey, the impact of sales of non-food items (e.g. alcoholic beverages in US retail outlets), and the weighting of the results by share of sales instead of the number of stores.

Buying Groups

To maximize volume purchase rebates offered by branded product processors, most retailers and wholesalers in Canada organize into buying groups to jointly buy brand-name products. The volume rebate received by retailers and wholesalers on purchases usually increases as the volume of the purchase increases, typically up to a maximum of 10% of sales (although most rebates are less than the maximum rate). Therefore, each member of the buying group, regardless of its level of purchases, benefits at a level commensurate with the total volume of the buying group. For example, if the total volume of the buying group's membership qualified for a 5% discount on the purchase price, each member would receive a share of the value of this discount based on its proportion of the buying group's total sales. The major buying groups are: United Grocers Inc. (members include A&P, Metro Richelieu, Overwaitea, Thrifty and Sobeys); IGA (including Agora and H.Y. Louie), and Safeway; and Distribution Canada Inc. (members include independent non-affiliated grocers). Presumably due to their significant corporate buying power, Loblaws and Provigo do not belong to buying groups. Sobey's recent acquisition of Agora may change the group membership.

Supply Channels

Food products flow to the supermarket shelves from both domestic and international supplier sources through two principal supply channels (**see Figure 2**). About 25% to 30% of store inventory is delivered directly to the retailer by the processor and is known as direct store delivery. Perishable and easily damaged goods such as cookies, snacks, bread, meat and dairy products are delivered in this fashion. Soft drinks are also shipped directly. The remaining products generally move through food wholesalers' warehouses and then to food retail outlets.

Food products are sold to food wholesalers and retailers by either the processors' own sales force or by food brokers representing processors. About 31% of the products moved through food wholesalers are sold by food brokers on a commission basis. Most food brokers in Canada have lines that they take title to and operate on a buy-sell basis.

Typically, food wholesalers buy, take possession of and resell products supplied by processors. Food wholesalers may be wholly owned by a food retail chain (e.g. National Grocers), a cooperatively owned group (e.g. Federated Co-Op), a voluntary wholesaler with which retailers affiliate (e.g. IGA) or an independent that serves non-affiliated or independent retail stores, such as smaller locally based specialty wholesalers. Regardless of the type, food wholesalers perform similar functions; mainly buying, warehousing, transporting goods and the associated data processing and accounting services. In addition, they may provide a variety of business, financial and technical services for retailers.

Most major Canadian grocery retailers operate wholesale and foodservice divisions and are active in more than one province or region. Only two retail wholesale firms operate on an essentially national basis –Loblaws and Agora (although Agora does not operate in British Columbia and Loblaws has just recently entered the Quebec market). Corporate wholesale divisions of retail wholesale firms supply corporately owned stores, as well as affiliated or franchised independents operating under various banners, and unaffiliated independent and foodservice accounts.

Co-ops such as Federated, Interprovincial and Co-Op Atlantic are distinct in that their wholesale operations are owned by the retail members. For example, Federated Co-Operatives Ltd., the largest co-operative in Canada, provides centralized wholesaling to about 300 locally owned retail co-operatives across Western Canada and northwestern Ontario. In turn, the co-operatives' retail members are owned by an estimated 900,000 individual co-operative members.

Corporate Concentration

By most accounts, the retail food sub-sector in Canada is characterized by high levels of corporate concentration.[8] After the recent major acquisition activity in the industry, the largest four retail grocery firms now represent about 55% of national all-channel grocery sales – up from 45%. The top eight firms represent about 70% of such sales. In most regions, over 70% of sales are accounted for by the top three firms. In Quebec, the top two companies (Provigo and Metro Richelieu) share about 70% of sales. The US is not as concentrated, on a national basis, with eight companies controlling about 35% of the national grocery market, although its retail food sub-sector continues to consolidate at a rapid pace. However, in most US regions, the level of concentration is consistent with the Canadian situation, with three to five firms controlling the bulk of grocery sales.

Due to the high level of integration between the retail and wholesale operations of most large Canadian grocery firms, retail and wholesale sales are not usually reported separately by food retail wholesale companies. Thus, it is very difficult to readily determine the extent of concentration in the wholesale food sub-sector in Canada. But it is believed that this sub-sector is characterized by a degree of concentration comparable to the retail sub-sector.

Generally, the food wholesaling sub-sector in the US is much less concentrated than in Canada. The leading 10 wholesale firms in the US accounted for about 15% of total wholesale sales but within the general line of wholesalers, the eight largest US firms accounted for about 44% of sales in 1992. Moreover, there is much less integration into retailing by US wholesalers. In the US, most major food wholesalers, such as Fleming Cos. and Supervalu, are not major retailers. But like the US retail food sub-sector, the wholesale sub-sector in the US is also consolidating rapidly.

CONDUCT

During the past decade, the food retail/wholesale sub-sector has evolved to better respond to consumer demand. Previously, this sub-sector tended to reflect the traditional supply chain system, powered by the processor push. Now, the supply system is evolving to a demand chain, driven by consumer demand.

Within the traditional supply chain approach, processors were able to develop strong brand loyalty through comprehensive and expensive marketing programs. Processors were also responsible for conducting most ongoing market research on consumer needs and aggregate retail trends. Retailers relied on processors to determine what goods to sell and, in many instances, at what price.

8. Due to the integration of wholesale and retail operations, firms' market share is reported on a corporate basis (i.e. total firm sales/total value of grocery market in Canada).

However, factors such as increasing competition in the retail grocery marketplace, flat food sales, consolidation within the retail/wholesale grocery sub-sector, new store formats and private brands have changed the traditional relationship between food processors and retailers.

During the past decade, as the result of heightened consumer awareness on value, retailers have reviewed their operations and responded with innovations that would provide consumers with more choice, greater convenience, better quality or lower prices. Technology has allowed retailers to collect information on new consumer trends. For example, as an initial response to increasing consumer emphasis on value, retailers have scrutinized the main costs that they face and control (e.g. variable costs of labour and stock). Consumer information will be increasingly applied to improve competitiveness through micro-marketing (e.g. matching store-level expenditure patterns and consumer profile data).

Alternate formats

In response to changing consumer trends and retail strategies, new food retail formats (e.g. warehouse clubs) have appeared, along with the introduction of food products in non-traditional outlets (e.g. mass merchandisers). These formats draw consumers from the traditional supermarket by offering lower prices and one-stop shopping convenience. Traditional chain and independent grocers must now increasingly compete in food categories with mass merchandisers, warehouse clubs, deep discounters, drug stores and other outlets in which food is not the main line of business. Such non-traditional formats capitalize on high inventory turnover, low markups, reduced real estate costs, minimal customer service, narrower product variety and direct delivery of goods. Gross margins in these formats may be as low as 8% to 11% compared to typical supermarket margins of 20%.

Although it is not a major player in the Canadian food retail sub-sector, Wal-Mart is estimated to be about the third largest grocery retailer in the US. Some analysts expect it to be the largest grocery retailer in the US by the turn of the century with a 10% share of the food market. Wal-Mart has recently added refrigerated food products to some of its Canadian outlets, which has led to speculation that it may intensify its food retail efforts in Canada in the future, at least within its current department store format.

Private label[9]

The marketing of private and control labels has been an effective product strategy for retailers and a source of their increasing influence. Private label has been around for decades. In the past, product development and marketing were the exclusive domains of processors. Increasingly, retailers are assuming and controlling the valuable and potentially lucrative functions of product development, package design, marketing and advertising by outsourcing production of high-quality, value added products with a distinct price advantage over national brands. Consequently, the major retailers now exercise significant influence and control about 20% of the food product and brand development in Canada.

As competition heightens, retailers such as Loblaws have become aware that selling brands under private labels have three advantages: increased margins and profits, more effective bargaining with processors, and strengthened retailer image and consumer loyalty. Retailers also acknowledge the potential of exporting these private label products. For example, Loblaws' President's Choice products are sold in the US, Hong Kong, the Caribbean and Israel.

9. Also known as "own label," "store brand," "control label products," "retailer brand," "corporate brand" or "exclusive brand," private label products are "owned" and/or licensed exclusively by retailers, wholesalers, cooperatives, restaurant operators, foodservice distributors or caterers for distribution in their segment of the marketplace.

The market share of private labels (excluding random weight meat, produce and random weight dairy products) in Canada increased from 14% in 1986 to about 25% of grocery sales in 1997; it is expected to level off at about 30% in the medium term. The increased popularity of private labels during the early 1990s was partly due to the recession. Evidence indicates that private label market share is inversely related to disposable income. However, this relationship has weakened over the years. The quality of private labels is constantly improving and Canadian retailers have skillfully developed their private label products and now offer a range from modest generic, price-oriented, average-quality commodities to upscale, luxury items that are differentiated by high quality. Consequently, a majority of consumers today believe that private labels are equivalent in quality and value to national brands.

Private label penetration has also been bolstered by technological advances and comprehensive point of sales data that provide major retailers with a competitive edge over processors in deciding which new products to introduce and in identifying poor-performing products. More consumer brand buying decisions (often estimated as being upwards of about 80%) are made at the point of sale, which reduces the effectiveness of mass media advertising by national brands and confers an additional advantage to retailers. Customer loyalty plays a major role in retailers' strategies. Typically about 20% to 35% of food store customers in North America generate 70% to 85% of a retailer's profits. Current strategies emphasize meeting the needs of this customer and encouraging repeat shopping and increased spending. Private label and electronic data information are key components in knowing and keeping this customer. These products are critical to the retailer's ability in differentiating itself from the competition and as a key component of customer loyalty.

Efficient Consumer Response

For years, customer knowledge was the sole domain of the processor. This was gleaned from focus groups and consumer research. This task has switched somewhat to the retailer but the processor is also expected to take an active interest in customer preferences and efficiently respond to the buying patterns in an individual store. This relationship forms the basis for implementing the Efficient Consumer Response (ECR) initiative, not only in North America but worldwide. The retail food sub-sector is the first link in the demand chain but it may also be the most important, as it is the beginning of the information flow from consumers to production.

In 1992, a major US industry study determined that discounters and competitors such as Wal-Mart could charge lower prices not because of preferential processor prices but because their logistics were more advanced. As a result, their distribution costs were lower than competitors' by up to 2% of sales. Given the intense levels of competition within the retail food sub-sector between traditional and non-traditional grocery firms, to maintain or increase profits, retailers had to focus on reducing costs within the distribution system. Subsequently, ECR was launched by the Canadian grocery industry in 1993. An ECR steering committee composed of processors, distributors and brokers was established to lead the initiative. The industry thus falls in line with other efficiency initiatives and re-engineering approaches (e.g. just in time [JIT] delivery) implemented by industries such as automobile manufacturing.

In general, ECR aims to reduce the external system costs that result from the interaction of processors, wholesalers and retailers in the agri-food supply system by improving coordination among these entities so that they may more efficiently respond to diverse consumer demand – in essence, eliminating unnecessary costs and inefficiencies in the supply chain.

ECR involves a set of enablers or non-proprietary business practices to facilitate a mutual benefit among trading partners in the supply chain. This initiative envisions the following measures:

- management of inventory levels as well as product offerings in a way that reduces inventory levels and ensures the right mix of products and profits through category management[10];
- implementation of continuous product replenishment programs to improve service to consumers by reducing the frequency of out-of-stock products;
- the promotion of cross-docking stock (e.g. assembling store deliveries from carriers right on the warehouse dock rather than by drawing from stock inventory) which increases the efficiency of product flows at warehouses; and
- uniform and transparent supplier pricing policies to discourage stockpiling by wholesalers and retailers.

The critical first step will be the efficient communication of consumer demand through the supply chain. This step will require the implementation of universal bar coding of individual products, and eventually product cases and case pallets. Concurrently, the use of compatible information technology among the system's sectors will need to be implemented.

At the outset, in Canada, the annual savings from implementing ECR were estimated to be a minimum of $3 billion. In addition, the sector initially estimated that ECR could reduce the time it takes to move food products from processor to consumer from the current 104 days to 61 days and, in the process, reduce consumer prices by 10%. However, at this time, the level of benefits is expected to be considerably less than the $3 billion and cannot be directly allocated between individual supply chain players. Moreover, the implementation of ECR will undoubtedly involve system costs as well as system benefits and, in some cases, the incidence of costs and benefits may not be equal for each party in the supply chain. This situation may mean that ECR will be implemented in a step-wise fashion with the initial emphasis only on "win-win" actions.

ECR emphasizes the change from supply to demand based marketing or from a supplier push to a consumer pull. ECR will also affect the way the industry measures its performance. The sector will move from using volume (e.g. gross revenue, gross margin, sales per unit) indicators as measures of performance to measures that will focus on:

- customer satisfaction;
- product replenishment times;
- yield (% of product wasted, sold at full price, etc.);
- reliability (forecasting, JIT delivery); and
- financial measures based on returns on assets and activity based costing.

Based on pilot projects, the potential impact of ECR is significant. For example, a continuous replenishment program pilot project with Quaker Oats and Agora reported significant efficiency and service gains. Retailers and processors have made major progress in identifying the enablers and technical elements of the ECR initiative as well as recognizing that a critical mass of participation will be necessary to achieve significant gains. To date, however, progress in ECR implementation has been limited.

10. Category management is a method of retailing which analyzes groups of closely related products with the intent to achieve an efficient mix of products and profits.

Efforts have focussed mostly on the development of bar-code and EDI standards. Virtually all retail food products now carry bar-codes that may be accurately scanned in retail stores and the industry has committed to the launch of EDI transaction sets (e.g. purchase orders and invoicing) in May 1999. Target implementation dates have also been set for the barcoding of product cases and pallets.

An ECR industry scorecard initiative has been introduced to measure the state of ECR readiness and its related progress. It is unclear if the progress to date in the Canadian industry is ahead of or behind the US industry, although the industry's sense is that more progress has been made in Canada, particularly in the area of bar coding and category management. Some observers believe that implementation of the ECR initiatives may not result in lower prices for consumers but may help to maintain prices and market share for traditional retailers.

Sector-wide embrace of ECR has been delayed as players assess the costs and benefits associated with each initiative. The remaining initiatives tend to be more proprietary and ECR may need to be embraced as a package rather than piecemeal.

Flat sales, low inflation and declining real disposable income have focussed retailers on efficiencies. The leading retailers are quickly acknowledging the importance of ECR based on activity based costing and value chain analysis. Some retailers are making major investments in information technology and embracing data mining to drive marketing strategies and customer loyalty programs. Also, the increasing presence of mass merchandisers in food sales in Canada may be the catalyst to widespread adoption of ECR.

The ECR initiative demands communication, cooperation and integration rather than isolation and suspicion. In doing so, ECR is dramatically changing the way the agri-food sector does business and transforming the fundamental buyer-supplier relationship.

Home Meal Replacement[11]

A common view is that time is the currency of the 1990s and the millennium. Increasingly, busy consumers and households are looking for convenient and easy ways of preparing meals. However, consumers still want to eat at home even though they may not have the time, the inclination or the ability to prepare home meals.

A recent survey indicated that most Canadians enjoy grocery shopping but speed and ease of preparation are important considerations in deciding what foods to buy. Other research indicates that most Americans would like to have dinner ready in 15 to 30 minutes. Today, consumers want more fresh than frozen, "meals" rather than ingredients, and they want these from their supermarket, but with the convenience of fast food. The manifestation of this trend has become known as home meal replacement (HMR), meal solutions and, recently, consumer solutions.

In much the same way as the 1992 US study on the distribution efficiency of Wal-Mart galvanized the sector's movement on ECR, another US study entitled "Foodservice 2005: Satisfying America's Changing Appetite" focussed the retail sector's attention on responding to these changing consumer trends. This study, stunningly, forecasted that virtually all incremental growth in the food sector in the US would be captured by foodservice. The authors reported that supermarket operators would need to respond by pursuing prepared foods or suffer significant losses in their market share of stomach.

11. Home Meal Replacement (HMR) or Convenient Meal Solutions (CMS) refers to meals that are fully or partially prepared outside the home and eaten at home. Selections include fresh, frozen and chilled items.

Retailers have recognized that this trend represents an opportunity to increasingly transform supermarkets from purveyors of ingredients to meal solution planners and, eventually, food preparers. Retailers are advantageously positioned to respond to this trend due to the high frequency of visits by shoppers, their expertise with private labels (since fewer HMR products may be branded) and their significant buying power. Retailers have responded along two fronts: offer prepared or almost prepared meals (fresh or frozen) which consumers take home and reheat, or complete preparation of the product and/or fully prepared cooked meal ingredients (e.g. meat loaf, potatoes, vegetables) which are already heated and ready to be assembled in the home.

Regarding the first approach, leading companies would emphasize adding value to the food shopping experience by marketing meal solutions and de-emphasizing meal ingredients. Many supermarkets will shift space allocation from packaged goods aisles toward a larger selection of fresh prepared, “nearly ready,” takeout and eat-in options.

Canadian grocers are responding along the lines of the second strategy by introducing new formats such as Oshawa/Agora’s IGA Marketplace. The increased popularity of fresh and chilled prepared foods could challenge the frozen and canned categories in the ongoing battle for retail space and involve the development and refinement of alternatives for sourcing and transportation of products with a shorter shelf-life.

The recent Canadian Council of Grocery Distributors retail operation survey indicated that the number of prepared food sections in Canadian grocery stores has grown, and close to three quarters of US grocery retail chains increased their shelf-space allocation for prepared foods/meal solutions. Canadian grocery retailers increased their share of dollar sales from prepared foods threefold from 2% to 6% between 1995 and 1996. In comparison, prepared food sales represent about 10% of US retailers’ sales. In 1996, frozen dinners and entrées saw a 16% increase in sales and a 13% increase in volume.[12]

In 1995, retailers in Canada provided only about 2% of total prepared meal sales (US retailers accounted for about 5% of total meal sales). Approximately 5% of meal occasions in Canada typically involve take-in products; thus, the industry must carefully understand and interpret what this trend means to consumers and what it will mean to the supermarket business. The HMR trend may mean a continuum of products from nearly homemade to ready-to-heat to take-it-home.

HMR represents a strategy to increase market share at the expense of foodservice companies. However, this opportunity is not without challenges. Shrinkage, significant labour costs, training, in-store investment, the requisite change in corporate culture (i.e. selling food is not the same as selling groceries) and performance measures have presented major challenges for HMR. Sourcing is also a main concern in the demand for meal solutions. Potentially, retailers have several choices for home meal solutions:

- prepare the products in-house, which could result in dedicated staff, packaging and new equipment for cooking and display, as well as significant training and investment costs;
- out-source to a central commissary operated by small local processor or caterer which entails new logistical concerns such as transportation, timing and new equipment to maintain product integrity;
- set up their own central commissary, which would entail capital investment in addition to the other factors previously mentioned;

12. Western Grocer (A.C. Neilsen), Jan/Feb 1998.

- develop their own private label meal solutions, which would involve contracting with processors, developing specification guidelines, maintaining and enhancing product quality;

- source directly from the processor, which makes the retailer dependent on the processor to maintain branded product quality (less than 10% of prepared food is provided by branded processor to retailers in Canada); or

- develop alliances with operators (e.g. Loblaws and Mövenpik Restaurants).

Retailers are also concerned about the extent to which incremental HMR will cannibalize in-store sales rather than decrease foodservice's share of stomach. A recent US study indicated that, on average, HMR-type foodservice operations by retailers resulted in a 2% net loss. A similar situation may exist in Canada. Undoubtedly, the sub-sector is encountering a significant learning curve with respect to this strategy.

Given the intense attention paid to the lucrative potential of HMR, many players are vying for this market. Supermarkets have felt this competitive pressure from a proliferation of mealtime options and alternative formats that have encroached on their packaged goods business. Traditionally, the difference between "retail" and "foodservice" has been based on food prepared "at home" versus "away from home." However, this distinction is becoming increasingly blurred as retail deli departments move into fast food items such as prepared chicken and prepared pizza and as restaurants market almost ready-to-eat meals that are "prepared" at home. Given these new forms of competition spawned by changing consumer trends, this sub-sector blurring is expected to increase.

Trade Spending/Promotional Allowances

Trade spending or promotion allowances includes a wide array of incentives/payments provided by processors to wholesalers/retailers to promote and/or list their products. Such rebates, allowances and discounts refer primarily to funds paid by processors for volume purchases, promotional efforts on behalf of the product and favourable purchase terms. Essentially, rebates reduce the purchase price of goods and increase the gross margin available to wholesalers/ retailers. In some instances, incentives are offered by processors; in other cases, the food wholesalers/retailers require such payments. For example, major wholesalers/retailers typically charge slotting fees to offset one-time costs associated with the introduction of new products, such as tagging (entering an item into the warehouse system) and the inherent risk of allocating valuable shelf space to a relatively unproven product. The value of slotting allowances can be quite significant depending on the product and the retailer/wholesaler.

The Food and Consumer Product Manufacturers of Canada (FCPMC) estimated that, in 1991, trade spending accounted for about 19% of sales generated by processors. FCPMC also estimated that about 70% of food products at that time were sold to wholesalers/retailers at a sale or discounted price in Canada. Allowances and revenues from processors were estimated to represent about 0.6% of sales for the average retailer in 1991. These allowances are significant given that grocery retail margins are about 1%.

Aside from concerns that trade promotion monies may be simply subsidies to wholesalers/ retailers, allowances are challenged by processors in the hope of introducing a more efficient method of trade promotion, responding to consumer preferences and not wholesalers/retailers' demands. Currently, supermarket chains may forward buy (i.e. purchase products in bulk in advance of sales to obtain volume discounts or other trade allowances). These products are then warehoused for use as demand rises. These practices create production inefficiencies[13] for processors and excess inventory in the system. However, wholesalers/retailers argue that forward buying provides a competitive edge for supermarkets against mass merchants and wholesale clubs that do not forward buy to the same extent as supermarket operators. Trade studies report that a well-managed forward-buying program could result in a 3% to 4% increase in grocery retailer gross margins.

Processors may also set the stage for this situation by focussing on trade promotion instead of advertising to increase market share. Generally, consumers will respond more quickly to a price promotion than to an increase in advertising spending. Interestingly, a major cereal processor recently decided to reverse its decision to reduce trade spending in light of significant declines in market share.

The elimination of forward buying would be complicated. It is believed that its elimination would result in improved logistics which would benefit all wholesalers/retailers; however, not all wholesalers/retailers currently engage in forward buying. Thus, wholesalers/retailers involved in forward buying would lose their relative advantage because the benefits would be distributed system-wide. This is another example of the difficulties caused by piecemeal implementation of ECR.

According to a recent AC Neilsen promotion spending study conducted in the US, processors and retailers in the US demonstrated significantly divergent views on the effectiveness of such spending, with effectiveness varying from 30% to 90%. It is expected that this would also be the situation in Canada. Based on US trends, annual trade spending in Canada is estimated to be $300 to $400 million.

Generally, most trade spending is directed to food wholesalers which are expected to share such payments with retailers. Non-traditional retailers such as Wal-Mart and Costco, which do not usually operate through food wholesalers, do not explicitly receive such allowances and instead require the lowest net price for goods purchased from processors. This issue remains particularly sensitive in processor and retailer relations.

PERFORMANCE

The retail food sub-sector competes with foodservice (commercial segment only) for the overall food market. In 1988, the retail food sub-sector accounted for about 70% of consumer expenditures on food products; by 1997, this proportion declined slightly to 67%.[14] However, expressed in real terms, the share of the retail food sub-sector increased from 69% to 70% during the same period, indicating that, on a volume basis, the share of food products sold through retail outlets increased by about 1%.

13. These inefficiencies may be overstated in the case of food products, due to the fluctuations of agricultural production and the economies of batch production.

14. The retail food sub-sector has a 60% market share of food and beverage products; in this case only food products are considered.

Given that the past decade has been characterized by declining real disposable incomes, low rates of inflation and intense interchannel competition (e.g. traditional grocery stores vs. non-traditional outlets such as mass merchandisers, gas stations and warehouse clubs), between 1988 and 1996, aggregate retail supermarket net profit margins[15] declined from 1.2% of sales to 0.8% (see **Table 6**). Accordingly, the sub-sector average return on assets declined significantly from 6% between 1988 and 1991 to 1.4% between 1994 and 1996. Capital investment expressed as a percentage of sales declined from an average of 2% between 1988 and 1992 to 1.5% between 1992 and 1996.

However, the 10 largest grocery firms, which dominate the sub-sector, demonstrated above-average performance. Both net profit margins and return on assets[16] were significantly higher between 1995 and 1996 than between 1988 and 1992 (**see Table 7**). Deloitte and Touche reported a similar trend based on its examination of the financial performance of six major publicly traded Canadian grocery firms between 1991 and 1997. During this period, earnings, margins and return on assets for these firms improved significantly. The *Financial Post s* food store index outperformed the general merchandising retail index between 1988 and 1997, but not the overall Toronto Stock Exchange 300 index.

Comparison with the US

Compared to US supermarkets, Canadian food retail firms are less profitable, generating lower gross margins and net profit margins. Between 1992 and 1996, the net profit margin in US operations averaged 1% of sales versus 0.4% in Canada (**see Table 8**). The gross margin in Canada is generally 1% to 2% less than in the US, allegedly due to the higher cost of distribution in Canada.

Based on the sub-sector’s major benchmarking survey conducted by the Canadian Council of Grocery Distributors (CCGD) and the Food Marketing Institute (FMI), Canadian supermarkets have made improvements in efficiencies. These are reflected in the increases in average inventory turns (sales divided by value of inventory) between 1988 and 1996, increasing from an average ratio of 16.2 between 1988 and 1992 to 17.7 between 1992 and 1996. Real sales per square foot increased by about 23% between 1991 and 1996. Canadian operations also appear comparable to US benchmarks in terms of sales per square foot, inventory turns and sales per labour hour.

As another illustration of food retailing in Canada and US, the performance of the largest retailers, Loblaws and Kroger respectively, was benchmarked. (**see Table 9**). Although Loblaws’ sales between 1991 and 1997 were, on average, only 40% of Krogers, the average performance of the two firms is similar in terms of reported profit margins, return on assets and inventory turns. The sales per square foot and average store sizes were also comparable in 1997.

Wholesale

Since the leading Canadian grocery firms integrate retail and wholesale operations, a description of the financial performance of the wholesale sub-sector is difficult beyond the observation that, in 1994, the average trading profit margin of Canadian wholesale operations was comparable to major US wholesalers. However, inventory turns have improved since 1991 and the industry average, in this regard, exceeds the performance of major US wholesalers such as Fleming and Supervalu. Based on recent data from the CCGD and FMI survey, the number of cases shipped per total labour hour in Canada was about 80% of the US value. Again, care must be taken to ensure that the profile of the distribution centres is comparable. The US wholesale sub-sector provides for more specialized wholesalers (e.g. frozen products) which generally carry fewer items

15. Net profit margins represent profit after tax expressed as a percentage of sales.

16. Return on assets represents net profits as a percentage of value of total assets.

and hence tend to be more productive than more general line wholesalers which are more prominent in Canada. Real inventory levels in the Canadian wholesale sub-sector increased by about 3.5% between 1994 and 1995; however, this growth slowed to about 1.5% between 1995 and 1996, perhaps as the result of the sub-sector's focus on reducing stocks.

Comparison Within the Agri-Food Chain

Much discussion in the Canadian agri-food system has focussed on the relative performance of the retail sub-sector compared to other sectors in the agri-food system. While such comparisons are not straightforward, some observations can be made. In terms of total trading profit,[17] the retail food sub-sector generated about $15.5 billion between 1988 and 1995 – an amount slightly greater than foodservice ($13.5 billion) but much less than the level of trading profits generated by the food processing sector ($32 billion) or the agriculture sector ($45 billion) (**see Table 10**).

Regarding financial performance, the average return on assets generated in the retail food sub-sector between 1988 and 1996 was 3.12% versus 4.10% in food processing and 2.89% in foodservice. A similar comparison to agriculture is difficult due to inconsistencies in the year-to-year valuation of farm and non-farm assets. During the 1994 to 1996 period, the gap in the relative performance of the retail food sub-sector and the food processing sector widened even further, with the return on assets of retailers declining to 1.4% while that of the food processing sector was 3.6%, leaving a difference of about 2% – double the difference between 1988 and 1996 (**see Table 6**).

However, a comparison of the performance of the largest 10 firms in the retail food sub-sector and the food processing sub-sector indicates that, based on the average return on assets between 1988 and 1992, the 10 largest retail food sub-sector firms averaged about 60% of the return of the largest 10 food processing firms; however, between 1995 and 1997 they averaged about 101% of the processors' returns. Interestingly, among the large retailers, the trading profit margin improved since 1988 while it remained relatively stable for the large processors. This observation may indicate that retailers have been successful in obtaining operational efficiencies, but not necessarily by "squeezing" the prices of, at least, the largest processors. In addition, the food retail firms increased operating efficiency in terms of inventory turnover from 13.6 in 1988 to 14.7 by 1997 while the processing firms' inventory turnover declined somewhat (**see Table 7**).

GLOBAL PERSPECTIVE

The demographic and technological changes that have led Canadian consumers to become more value-focussed and Canadian firms to become more competitive are also occurring globally. Retailers around the world have responded by consolidating through mergers and acquisitions and by developing private label products.

In Germany and the UK, the top three grocery retailers accounted for about half of the entire market. The US and Japanese markets are less concentrated (the top three account for 20% and 9%, respectively), but on a regional basis this level is higher. Sales growth in all these markets is very small, but unlike in Canada and the US,[18] Western European and Japanese retailers are expanding to other countries and even other continents. As a result, within the US for example, three of the top nine retailers are wholly or partly foreign-owned, while the largest convenience

17. Trading profit is earnings before interest, taxes and depreciation. Trading profit is being used as an example of the share of profits distributed throughout the agri-food system.

18. With the exception of Winn-Dixie (US), which has a small chain in the Bahamas.

store chain, 7-Eleven, is owned by Ito-Yokado of Japan.[19] Western European retailers are the most “transnational”; France’s Carrefour is active not only in other European countries, but also in Asia and South America.

Private label penetration is somewhat higher in Canada (25%) than in the US (20%)[20] but lower than in the UK (29%).[21] Private label is highly developed in Western Europe; for example, all of Marks & Spencer’s food business is conducted under its own brand, St-Michael. The presence of private label products is usually the sign of a relatively sophisticated market. Also, such products are generally found only in markets where branded goods are in wide distribution. Therefore, in countries such as Japan and Taiwan, the market for private label has experienced double-digit growth in the 1990s, while in countries such as China and India, private label is not present at all.

ECR is not just a North American initiative but has implications for doing business worldwide. The global demand for value has driven ECR activity at various stages of development throughout the world. Trading agreements such as NAFTA and the presence of ECR veterans such as Wal-Mart and Carrefour in developing markets are expected to spur the growth of ECR worldwide. Therefore, ECR has also become an exporting issue (i.e. technology demands, on-line transactions, bar coding, pallet coding).

In their efforts to attract customers, retailers are diversifying the services they offer their customers. Some retailers offer financial services (like Loblaws in Canada), many offer “loyalty” cards[22] and others even sell gas (especially in the UK and France) and pagers (like Spencer's and Nanz in India).[23] This approach is a further indication of the increasingly tight competition in the retail food sub-sector, with retailers using aggressive marketing techniques to gain competitive advantage.

IMPLICATIONS FOR THE AGRI-FOOD SYSTEM

Consolidation

The re-engineering and cost controls that began for Canadian food retailing in the 1990s will continue and perhaps intensify. In the absence of price inflation, retailers will continue to control costs and consolidate because they will be unable to pass on additional costs through increased prices to consumers. Analysts expect that in the medium term the retail/wholesale food sub-sector will be dominated by even fewer firms in Canada.

Consequently, significant buying power will continue to rest in the hands of major food retail/ wholesale firms in Canada. This leverage to some extent has been offset by the increasing presence of non-traditional retailers but processors and producers may face greater pressure to deliver quality products at lower prices. Further consolidation and the corresponding mergers or acquisitions also mean that processors and producers may need to reforge new relationships in the medium term.

19. Euromonitor, p. 17.

20. *Grocery Marketing*, March 1997, p. 6.

21. Euromonitor, p. 219.

22. Using these cards, the shopper accumulates points based on the amount of groceries purchased. Points are redeemed through vouchers, Air Miles, discounts, etc.

23. http://www.expressindia.com/fe/daily/19971121/32555193.html

Efficient Consumer Response

The implementation and success of ECR will demand the forging of stronger and more cooperative relationships among producers, processors and the distribution sector. The roles and relationships between retailers and suppliers must change. The production, processing and distribution sectors must share information, become partners and form strategic alliances to succeed. To attain the requisite critical mass, smaller processors must also implement ECR initiatives. Eventually, those processors that choose not to participate with the proper information systems may compromise future business opportunities.

ECR strategies have helped the grocery retail sector to reduce stock and use shelf space more effectively; as a result, processors' performance will be scrutinized more closely. More and more products will be evaluated and their listings maintained on the basis of per unit contributions to profits, as determined by activity based costing,[24] rather than simply on sales volumes or gross margins. Thus, products may no longer remain on the shelf simply because of promotion spending.

Private Label

Due to the significant benefits of private labels for retailers, the increasing penetration of private label products should continue, albeit at a slower pace. Private label products mean that for processors their customers have now become their competitors. Private label products represent a continuing competition to branded processors. This will require processors to respond with appropriate strategies, such as cost control and value improvements. However, branded consumer goods companies may continue to have some interest in private label production to use excess capacity, exploit economies of scale, solidify relationships with retailers and eliminate competitors. For some small processors, private label production may be the only way to break into a new area.

Alternate Formats

Emerging retail channels may demand further adaptation in the supply chain. Wal-Mart is a prime example of this phenomenon. This growing channel influences product sourcing, packaging and movement throughout the food supply system.

Alternate formats and channels introduce another competitor into the food market, as well as another market for manufactured food products. Warehouse club stores (e.g. Costco) offer an example of how non-traditional retail food channels can influence the supply chain. These formats tend to source directly from the processor and often have specific package and size requirements. Price is a key sourcing factor.

Home Meal Replacement

The HMR initiative will demand new strategic alliances and category management relationships between retailers and processors, as they shift their core activities from grocery distribution toward meal ingredient marketing. This shift will represent a major challenge as well as opportunity for processors. For example, US grocery processors believe that the biggest, most important and potentially most profitable challenge focusses on who will be the primary supplier of meal solution products sold through retailers.

Both retailers and processors must strive to re-establish and maintain contact with consumers. This means developing the selling mentality focus of the consumer pull-type system as opposed to the buying approach of the supply push system. Improved relationships between retailers and processors will help achieve this goal. By combining point-of-sale retail data regarding consumers'

24. Activity based costing measures value added based on all costs.

buying habits with processors' skill in product development, product innovation should be more efficient and profitable.

Consumer Information

In today's complex competitive environment, it becomes particularly important to have more detailed consumer information. Retailers will develop sophisticated databases that allow the tracing of consumer purchases as well as analyses of demographic and behavioural data. Such information will help retailers and suppliers market more effectively and create more successful category management strategies. For example, data from shopper loyalty programs used by some retailers indicate that a small group of customers represent the bulk of a store's sale base. Strategies to target or at least maintain these customers would be critical to increasing profit levels.

The apparent breakdown of traditional mass marketing means that development of detailed consumer knowledge may be the next competitive strategic advantage. Assisted by unprecedented information technology, data mining, although not currently practised by retailers, may eventually provide new and lucrative insights into customer preferences. Such relationships could lead to increased customized product offerings in stores and be tied to demand-side initiatives in terms of product forecasting, ordering and replenishment.

Processors and producers, too, would be keenly interested in such micro-marketing information and approaches which could potentially provide a clearer and truer picture of consumer demand. Since the source of this information would lie with retailers, suppliers might need to consider forging new relationships within the distribution sector to develop, cost share and utilize such consumer information. In the process, retailers and suppliers both acknowledge that the balance of power within the agri-food system will eventually rest with the consumer.

Electronic Shopping

The electronic highway and telemarketing may reduce the need for traditional food retail outlets and promote "go direct" programs from processors. Home shopping is among the future trends that loom on the horizon for food marketing. Bypassing traditional distribution systems would permit direct communication with consumers by processors. While information technology in the form of scanning, bar-codes, etc., is changing the way products flow through the supply system, this technology might also change the traditional face of food retailing. Estimates are that by 2005, 10%-20% of US food sales will be done by electronic shopping from home via the Internet.

Combined with an aging population, homeshopping could eventually reverse the trend toward megastores and reduce expensive real estate investment in large grocery outlets. To downstream suppliers, it could present the opportunity to bypass the retailer, filling shopping orders directly from a warehouse or central depot. National brands tend to gain a stronger advantage in this scenario than the competitive private labels which are associated with a retailer banner.

FOODSERVICE

The foodservice sub-sector, hereafter referred to as foodservice, provides consumers with food prepared away from home and represents about 35% of consumer expenditures on food and beverage products (**see Figure 3**), including spending in restaurants, cafeterias, pubs, and ordering from caterers. There are significantly more foodservice establishments than food retail establishments; therefore, there are more selling opportunities for processors, in particular for small- and medium-sized firms that can customize their product to the needs of their foodservice clients.

The Goods and Services Tax (GST), according to the foodservice firms, has had an untoward effect on this sector. The distinction between taxable food prepared away from home and non-taxable food prepared at home is becoming less clear because of the new ready-to-heat products available in grocery stores. In the face of this competition from the retail sub-sector, foodservice is emphasizing the value added that it provides, such as preparation of meals, convenience and ambiance.

SIGNIFICANCE

In 1997, foodservice's sales amounted to around $32 billion for food, meals, snacks and beverages (including alcoholic beverages) prepared and, in general, served in the estimated 120,000 foodservice establishments in Canada (**see Table 11**). While this sub-sector may not be the principal source for consumer food and beverage purchases, it is one of Canada's major employers and the largest employer within the agri-food supply chain, providing about 875,000 jobs (of which a high proportion are youths and women) and generating over $12 billion in value added, an amount of economic activity comparable to either the agriculture or the food and beverage processing sectors in Canada.

Foodservice also plays a role as a processor since its operators often process food ingredients in preparing consumer products. Foodservice is a major purchaser of Canadian processed food ingredients and entrée products, as well as agricultural products. For example, in 1995 foodservice purchased about $10 billion of products from the agri-food system – $9.3 billion from food and beverage processors and about $0.7 billion of agricultural products. The Canadian Restaurant and Foodservice Association (CRFA) reports that this sub-sector currently purchases about 75% of the mozzarella cheese and about 40% of the chicken produced in Canada.

STRUCTURE

Foodservice in Canada is typically classified into two major divisions, commercial and non-commercial, depending on whether the food purchase is the primary function of the business establishment, or secondary or incidental to the primary purpose of the establishment. Within each division, a diverse array of business concepts exist, as illustrated in Table 11.

Commercial Foodservice

The commercial segment is the largest component, accounting for 75% of foodservice sales and 45% of the business outlets in 1997.[25] This segment is the part of the sub-sector most often seen by consumers. The following five business segments or concepts, as defined by Statistics Canada, make up commercial foodservice:

25. CRFA's Infostats and Statistics Canada.

- *Licensed Restaurants*: These establishments hold a liquor licence and predominantly serve food. Licensed restaurants are primarily made up of two concepts: fine dining and family/informal (e.g. Swiss Chalet). Licensed restaurants are by far the largest component of the commercial segment and account for almost 50% of commercial sales and 36% of total foodservice sales.

- *Unlicensed Restaurants*: This segment is the second largest representing about 18% of foodservice sales. It is referred to by the sub-sector as quick service restaurants that do not serve alcohol, but have seats for their guests (e.g. McDonald's, Harvey's, Second Cup). In response to growing consumer demand for convenience, drive-through activity occasions have steadily increased at the expense of take-out in these outlets.

- *Take-Out and Delivery*: These establishments do not serve alcohol and provide very limited seating for their guests (e.g. Pizza Pizza, KFC).

- *Social and Contract Caterers*: Commercial companies which cater cafeterias in schools, hospitals, home for the aged, etc., or special events and do off-premise catering (e.g. Versa Services, Beaver Foods, Canada Catering).

- *Pubs and Taverns*: While these operators serve food, most of their sales come from alcoholic beverages.

Licensed and unlicensed restaurants and take-out outlets represent the bulk (65%) of foodservice sales. They are very broad and highly diverse in their menu categories and offerings. Full menu units represent only about 20% of the units. The remainder represent a wide range of specialized menu categories, such as pizza, oriental and steak.

Commercial outlets are generally supplied by distributors[26], but some products may be obtained directly from processors and producers ("suppliers"). In addition, commercial foodservice is the traditional home of highly competitive, branded foodservice concepts (e.g. Harvey's, Swiss Chalet, Pizza Hut) and branded food products (e.g. Coke, Pepsi, Heinz).

Above average growth is occurring in emerging segments and channels such as non-traditional locations for restaurant chain outlets (e.g. McDonald's in Wal-Mart and Harvey's in Home Depot), HMR alliances (e.g. Mövenpik in Loblaws) and warehouse clubs.

Non-commercial Food Service

Non-commercial foodservice operations account for 55% of foodservice outlets. Traditionally described as institutional, these establishments serve food as a necessity, or service, without direct compensation for delivering the product. In many cases, consumers in the non-commercial division were considered to be "quasi-captive" clientele, as their foodservice account was usually rolled into a general account in which a multitude of service charges were lumped together. However, the non-commercial category has since been broadened to include all operations that serve food and beverage products as subsidiaries or complementary operations to other businesses or service activities. Access to these foodservice facilities is largely confined to people who either work in or are users of the primary service or business activity. The following are examples of non-commercial foodservice operations:

- *Hotels and Motels*: Includes all food sold through hotels, motels and resorts (including fine dining, catering and quick-service).

26. The term "distributor" is used in foodservice to describe the same activities as those of the food broker.

- *Institutional*: Includes prisons, hospitals, schools, etc., that operate their own foodservice. It does not include institutions that use a contract caterer to provide the same services.
- *Leisure Industry*: Movie theatre snack bars, ball parks, arenas, etc.
- *Vending Machines*: All food products sold through automatic vending equipment.
- *Department Stores*: All foodservice sales through department stores except for areas leased or contracted out (e.g. McDonald's located within Wal-Marts would be part of "Unlicensed Restaurants," whereas an Eaton's Cafeteria would be included in the "Department Store" totals).

The non-commercial sector, like its commercial counterpart, uses distributors as its main source of supply. The institutional segment may have specific product requirements and specifications (low-salt foods, puréed foods, single-cup juices, etc.). This segment often contracts directly with processors for products including dairy, beverages, bakery and some dry goods, usually on a one-year contract basis. These products are delivered through distributors. Due to limited storage space, hospitals and homes for the aged, for example, require more frequency in their delivery of supply; it is this factor, along with price and quality, that primarily influences the selection of the distributor.

Composition

The commercial share of foodservice sales increased from 73% in 1990 to 75% in 1997 (see **Table 12**). During that period, the commercial segment has been driven by demand for family informal restaurants and quick service outlets. Licensed restaurants and take-out outlets' market shares of foodservice sales increased from 33% to 36% and from 9% to 11%, respectively. Social and contract caterers' sales increased significantly (23%) between 1990 and 1997, primarily due to their entry into the institutional foodservice segment. However, the share of unlicensed restaurants and accommodation foodservice fell because consumers are spending more money at Family Informal Dining restaurants (e.g. Swiss Chalet, Pizza Hut). In the pursuit of sales growth, the unlicensed segment, in particular branded concepts, has recently ventured into non-traditional locations such as hospitals, schools and department stores.

Compared to the retail food sub-sector, foodservice consists of considerably more outlets, about 120,000 foodservice outlets compared to about 27,000 retail grocery outlets. The average sales per unit of a foodservice outlet is only about one-tenth that of a retail food outlet. Similar to the retail food sub-sector, about 75% of foodservice requirements are provided through distributors, and about 23% is shipped directly from processors. The remainder is purchased from grocery wholesalers' cash and carry outlets.

Foodservice is both a source and a destination for value added products. Most foodservice outlets produce finished menu items using raw or semi-processed ingredients. However, there is an increasing trend in both the commercial and non-commercial segments for a supply of ready-to-heat (cold-plated), complete meals that need only be reheated, thereby reducing labour costs.

In 1992, independents accounted for about 72% of restaurant units with the remainder owned by chains[27] and affiliated franchisees. By 1997, chains' share of units had increased from 28% to 34%. However, the chain's share of restaurant sales is in excess of 50% and within the quick

27. NPD Group defines a chain as three or more establishments under a common name. Franchisees are independent although affiliated with a chain and some chains have no corporate ownership. A significant number of the chain sales may be represented by franchisees which may or may not be independent operators.

service segment (unlicensed restaurants and take-out outlets) chains' share of sales is in excess of 80%. This structure approximates the situation in US foodservice.

Outlet density in terms of population per commercial outlet – which may be interpreted as a crude measure of competition – indicates that the intensity of competition within the commercial foodservice segment has increased. In 1988, an outlet existed for every 600 people and peaked at about 654 people per outlet by 1990. Since then, the number of outlets has increased significantly and the ratio was about 495 people per outlet by 1997.

Whereas the major retail food firms integrate retail and wholesale operations, vertical integration by ownership is not prevalent in commercial foodservice. Some firms, such as Cara (Swiss Chalet, Harvey's), McDonald's and Pizza Pizza, have increased vertical integration through the ownership of dedicated distributors, but this practice tends to be limited to certain regions such as Ontario.

Domestically owned firms account for about 80% of the sales within the licensed restaurant and catering segments. However, dominant multinational ownership is evident in quick service outlets with foreign-owned fast food chains accounting for seven of the ten largest companies in Canada. With sales of almost $1.8 billion in 1997, foreign-owned McDonald's of Canada is by far the largest foodservice company in the sub-sector. Its sales are almost three times larger than the second largest foodservice company, Cara, a major Canadian foodservice operator/distributor.

Concentration
Generally, foodservice is characterized as fragmented with the 10 largest foodservice firms accounting for only about 25% of foodservice sales in 1997; this is a significant increase from 17% in 1987. The top 50 firms accounted for about 40% of sales in 1997.[28] Overall, a similar structure exists in US foodservice, albeit with somewhat lower concentration levels.

Most operators in the commercial segment are licensed restaurants. The 10 largest licensed restaurant companies are chains. They accounted for only 18% of overall sales in 1997, a level that has remained relatively stable over the past 10 years. In contrast, the level of concentration within the unlicensed restaurant segment is much greater. In 1997, the top 10 companies represented about 85% of segment sales; in 1987, the top 10 firms accounted for only about 55% of sales. Similarly, within the non-commercial segments significant concentration is evident. For example, three companies (Versa, Marriott and Beaver) dominate the $250 million university catering business.[29] Five firms represent about 80% of the contract catering sales in Canada.

Foodservice Distribution
Distributors are the logistic link in the agri-food chain that warehouses and delivers food and beverage products to operators. Foodservice distributor sales amount to some $11 to $12 billion annually.[30] Distributors are usually classified as full service (broadliners) that carry a variety of products, niche distributors (shortliners) that specialize in a few product lines such as meat, produce, dairy, etc., and system specialists that primarily serve chain restaurants.

Due to the relatively small scale but higher intensity of service required by their clients, the main value added of distributors lies in their ability to break down and consolidate processors' shipments into customized client orders on a frequent delivery basis. Foodservice distributor deliveries often contain frozen, chilled and fresh products which are delivered in special

28. CRFA, *Foodservice Facts*, 1998, p. 13.

29. *Macleans,* "The Food Fight," Nov. 25, 1996, p. 57.

30. Based on what distributors buy, **not** what operators purchase.

compartmentalized trucks. In addition, some distributors operate separate cash and carry outlets[31] which are limited line warehouses where products are purchased and picked up. Unique to this sub-sector, most distributors operate a sales force of distributor sales representatives to sell products from their warehouses. However, most new product marketing is carried out by the processors' own sales force and brokers. In contrast to their retail counterparts, foodservice brokers tend to market products to operators and then go to distributors with orders, thereby pulling the product through the system instead of having it pushed by distributors.

Nationally foodservice distribution is quite fragmented. The top five distributors account for less than 20% of sales while the top 50 represent about 40% of sales. However, in the major markets, distributors are more concentrated with the top five probably accounting for about 50% of sales.

Until the early 1990s, mid- and large-sized foodservice distribution firms dominated the regional landscape. However, this picture has changed dramatically in the last few years as many mid-size firms have been absorbed by larger one-stop, full-service, broadline distributors. One company, Serca, has emerged as Canada's first national foodservice distribution firm; it is also the largest foodservice distribution firm with estimated annual sales of $1.3 billion or 13% of the market. In addition, two large US distributors, Sysco and Gordon Foodservice, have entered the Canadian market. Shortliners that specialize in meat, fish, fresh produce, frozen products and other specialized services have remained strong over the years. In addition, it should be noted that many distributors have come to rely on buying groups.

As is the case in the retail food sub-sector, buying groups play an important role by improving pricing through mass purchases with savings passed on to the members and promotional incentives available from processors. The two major buying groups for distributors are Federated Foods and Associated Food Distributors. The CRFA, with its 14,000 members, has recently bought into "Groupex" a foodservice buying group which provides rebates on about 20 product lines and services about 10% of its membership.

CONDUCT

Efficient Foodservice Response

In response to eroding profit margins, non-traditional competition, new technology enablers and adversarial relationships in the supply chain, Efficient Foodservice Response (EFR) was developed. EFR is akin to the retail food sub-sector initiative, ECR. It is designed to align processors, and foodservice brokers, distributors and operators to "facilitate a more competitive, demand-driven foodservice supply chain." The foodservice supply chain involves three intertwined flows: product, information and funds. Information and fund flows connect to product flow but add no inherent value to the consumer. Therefore, the movement of information and funds must be streamlined. By reducing supply system costs EFR is potentially a significant growth strategy for foodservice since it is estimated that, on average, a restaurant meal costs about three times as much as a home-prepared meal. The potential benefits of EFR in Canada could amount to more than $400 million.

A study done by FCPMC Foodservice Council, Technology Committee and KPMG, *EFR: Building a Case For Change* in 1996 concluded that the supply chain technology could be improved. For example, the study indicated that UPC codes exist for only about 60% of foodservice products and a significant portion of those in place are inadequate due to a lack of standardization. Scanning technology is not used in most distributor operations, and less than 2% of invoices and purchase orders are made electronically. The same study found the foodservice supply chain more efficient than the grocery system in respect to lower inventory levels and fewer invoice disparities.

31. Cash and carry outlets operate on a system of cash payments with no delivery available.

	FOODSERVICE	GROCERY
Supply Chain Inventory	52 days	81 days
Order Cycle Times	1-2 days	1-3 days
Invoice Discrepancies	12%	70%

Source: “EFR: Building a Case for Change, *KPMG, 1996.*

Lower inventory is an indication of good supply chain performance. On average, operators have only three days' inventory due to a crucial need for product freshness, relatively little storage space, and the lower percentage of products purchased on promotion. Because most operators use the same menu over a long period of time, it is critical that they receive their supplies from distributors on a regular basis; if not, they may have to temporarily remove an item from their menu which could result in consumer dissatisfaction.

A strong link already exists between distributors and operators, which requires quick responsiveness on the part of distributors to fill orders. Purchases from operators tend to be based on actual demand or “pull” rather than on forward buying and supply “push”. This reduces the cost of carrying inventories and results in fewer invoice discrepancies. As a result, the potential benefits of EFR are proportionally less than ECR, but still significant considering the very modest profit margins in foodservice.

As in the case of ECR, the success of EFR is based on sub-sector principals or enablers that enable a quick and continuous response by processors and distributors to operator needs, the elimination of excess costs and the provision of timely, accurate, electronic information flow.

The key EFR enablers are:

- Industry implementation of Universal Product Codes (UPC) and Shipping Container Codes (SCC) to ensure standardization of product identification.
- Electronic Data Interchange (EDI) to promote electronic commerce and eliminate paper flows and reduce administrative costs.
- Supply chain demand forecasting to streamline product flows and reduce inventory levels.
- Continuous Product Replacement (CPR).
- Activity Based Costing (ABC) to eliminate non-value added activities.

The foodservice supply chain has agreed to support these enablers in principle. A significant start has been made through the establishment of the EFR Steering Committee composed of foodservice operators, distributors, and brokers and processors. The committee has focussed on the following common enablers: product identification and bar codes, electronic commerce and supply chain demand forecasting. Currently, activities are under way to assess the situation in the sub-sector, carry out pilot projects and publish “best practice” recommendations. Targets have been established with regard to product and case bar coding. The best practice recommendations will take 12 to 18 months to develop.

As ECR has been in process for a longer time and many of the processors and some integrated distributors have been part of the process, their experiences should provide a roadmap for EFR. In ECR, proprietary matters such as trade spending will complicate the supply chain demand forecasting initiative. Trade spending leads to inventory loading in the foodservice supply chain and with it the associated inefficiencies. Issues of trust and information sharing are also core to both EFR and ECR.

Many major operators have already devised their own version of EFR. McDonald's and Tricon (Pizza Hut, Taco Bell, KFC) have achieved the efficiencies of EFR by working with their distributors, processors and sometimes the growers. Also, companies such as McDonald's have had a significant influence on the vertical production and processing system that supplies them with french fried potatoes, ground beef and other products. McDonald's procures about 12% of the annual US russet potato market and presumably a significant share of Canadian production. This is an example of how producers may need to be more in tune with the specifications, availability and other needs of foodservice.

Private Labels

Most major distributors operate a private label line of products which are sourced globally. Since private label products achieve higher margins, it is this line that is promoted heavily by distributors to operators. It is believed that the penetration of private label products in foodservice is higher than in the food retail sub-sector.

PERFORMANCE

Much attention in foodservice focusses on the competition between foodservice and retail food and beverage outlets for a share of consumer food expenditures. In 1989, sales of foodservice firms represented about 36% of consumer expenditures on food and beverage products in Canada. By 1991, foodservice's share declined to about 33%, which the sub-sector attributes to the introduction of the GST and the recession. However, since this setback foodservice has, for the most part, slowly regained lost ground each year and, by 1997, its share of stomach had increased to about 35%.

Compared to the US, in terms of share of food and beverage expenditures, foodservice in Canada is somewhat underdeveloped. In 1996, US operators accounted for 39.1% of food and beverage expenditures, compared to 35.4% in Canada – a difference of 3.7 market share points. However, this difference has declined from a peak of 5.2 points in 1991. On the basis of per capita expenditures, foodservice also appears underdeveloped, with spending levels in Canada representing about 90% of US values in 1996, down from about par in 1988 and 1989.

In 1996, the commercial foodservice segment in the US accounted for about 30% of sales compared to about 25% in Canada. This relationship seems to arise from the combined effects of the slight underdevelopment of the non-commercial segment in Canada (which may be due in part to the under-reporting of activities in Canada) and the over development of the commercial segment in Canada. In 1991, the segment shares in Canada and the US were similar.

Foodservice firms in Canada believe that the underdevelopment that appeared in the early 1990s is the result of the following factors: GST, lower levels of relative disposable income (Canadian levels are about 80% of US values) and higher input costs, in particular, ingredient costs in Canada. Compounding the situation are the change in society's attitude toward the consumption of alcoholic beverages and driving, and the reduction in the business tax deduction for meals.

Consistent with the trend in the share of stomach, foodservice sales, in 1992 dollars, increased by 1% between 1988 and 1990 but then declined by about 15% in 1991. Real sales have increased steadily since that time. In 1997, the level of real sales returned to 1988 levels but still remain below the peak real sales levels achieved in 1990. Real per capita foodservice sales declined for the most part between 1988 and 1993. Since 1993, real per capita sales have improved but the 1997 value remains about 11% below the 1988 value (**see Table 13**).

However, the commercial foodservice segment experienced real growth of about 14% between 1988 and 1997. Although this segment also demonstrated a real sales trough in 1991, with real sales declining by 17% from the peak 1990 level, real sales have recovered by 24%. Real per capita commercial foodservice sales in 1997 are about 1% higher than they were in 1988.

Employment in foodservice has followed a similar pattern of expansion, contraction and subsequent growth. Employment levels were about 13% higher in 1997 than in 1988.

The cyclical trend in sales growth in foodservice also manifests itself in the performance of labour productivity. Real sales per labour hour increased from about $19.50 in 1988 to about $20.90 by 1990, an increase of 7%, but declined to $19.00 in 1991. However, since then labour productivity has, for the most part, steadily improved. By 1997, real sales per labour hour increased to about $21.50 – representing a 10% improvement since 1988. Improvements in labour productivity reflect the sub-sector’s efforts to contain costs in the face of declining demand due to the factors cited previously.

Commercial segment investment also suffered as the result of the sub-sector’s downturn in the early 1990s. Between 1988 and 1992, investment as a percentage of sales averaged an impressive 4.7% of sales, but between 1992 and 1996 the intensity of investment declined to 3.7%. In 1996 and 1997, investment seems to have returned to levels of about 4%.

Due to the nature of the foodservice business with its critical emphasis on freshness, inventory turnover levels are the highest in the agri-food chain, at least three times greater than in the food retail sub-sector and the food and beverage processing sector. Average levels of inventory turnover over the 1988 to 1996 period have remained unchanged at about 41.5.

Overall, between 1988 and 1996 net profit margins for commercial foodservice firms averaged 1.4% of sales. Average margins between 1988 and 1991 were strongest at 2.2% and declined significantly during the 1991 to 1996 period to about 0.8%. The recent trend between 1995 and 1997 reflects improving net profit margins from about 0.9% to 1.5%. Return on assets followed a similar pattern. Within the post-farmgate sector during the 1988 to 1996 period, foodservice posted the lowest average return on assets, about 70% to 90% of the respective returns of the food and beverage processing sector and the retail food sub-sector (**see Table 6**).

GLOBAL PERSPECTIVE

Many US-based multinational chains (e.g. McDonald's and Burger King) operate in Canada in a manner and format similar to their global operations. Although many of the consumer trends driving foodservice in the US are similar in Canada, foodservice in Canada is very much a strong reflection of national demographics and tastes. For example, some ingredients and menu themes found in the US are not as prevalent in Canada (e.g. Tex Mex, Spanish, Cajun).

As mentioned previously, foodservice in Canada is not as developed vis-à-vis market share as is its US counterpart. Both markets, however, are keenly focussed on the evolution of positive consumer trends as they affect their market. For example, a major US study predicted that most of the future growth in consumer food expenditures would be captured by foodservice. The consumer of the future will be increasingly service focussed.

The US and Japan lead the world in spending on food prepared away from home (commercial foodservice segment) with $252 billion and $211 billion US, respectively. On a per capita basis, Canada ranks sixth in the world behind Japan, Spain, US, Italy and UK. Canada's ranking is partly explained by the fact that food is generally less expensive in North America than in Europe and Japan.[32]

IMPLICATIONS FOR THE AGRI-FOOD SYSTEM

Significant consolidation has taken place within foodservice during the past 10 years and this trend is expected to continue. For suppliers (processors and producers) this trend to fewer distributors/buyers for their products will continue to pressure suppliers' margins and emphasize competitiveness. To stay competitive, processors will need to implement more efficient marketing strategies such as encouraging operators to advertise branded products on their menus. Increasing concentration in foodservice will change long-established relationships between suppliers and distributors and operators.

Complicating the concentration issue is the entry of large US distributors, warehouse clubs, cash and carry organizations and segment specialists – all trying to gain an advantageous position. Similar to the trend in the retail food sub-sector, increased buyer expectations in terms of pressure for rebates and allowances and more intensive sales support could lead to supplier margin declines in foodservice. It is also expected that in foodservice, broadline distributors' house brands will continue to challenge suppliers of Canadian processed branded products. Chain operators will be demanding that distributors carry more customized proprietary products which may lead to marketing opportunities for small- and medium-sized suppliers. Large multinational distributors/chain operators will also continue to emphasize sourcing products globally or, at least, on a north/south basis, particularly for private label products. Consequently, the increased emphasis on the competitiveness of Canadian suppliers will continue.

The competitive marketplace, the implementation of the GST and the recession of the early 1990s have created an expectation of value by both consumers and operators. Although, foodservice is still regaining its 1989 peak share of the consumer stomach, indications are that it is poised for continued growth. This growth means the provision of food products that consumers would not prepare at home, in larger portions and at reasonable prices. Although it appears that the bulk of the new product ideas originate with operators, processors will be expected to be a major source of product development.

Operators will expect processors to focus more on customer value and the development and provision of more value added products. Such product innovation must focus on reductions in "back-of-the-house" labour inputs (e.g. better selection of prepared foods), improvements in operator margins, differentiation of product and improved product flexibility. For example, the introduction of value added products such as frozen pizza crusts, consistent in quality to prepared crusts, permits operators to reduce labour costs and expand menu offerings but not at the expense of product quality.

Consistent with foodservice's commitment to enhance customer value and restore and improve its market share is adoption of EFR. Since the retail food sub-sector appears committed to reduce system costs through ECR, so too must foodservice to remain or improve its competitiveness. Accordingly, the new corporate players must be experienced and committed to the use of technology to reduce distribution costs and increase supply chain efficiency. The large distributors are expected to push food suppliers toward implementing EFR by demanding Universal Product Codes (UPC), continuous replenishment and category management.

32. *The Globe and Mail*, October 5, 1998, p. B2.

Opportunities for proactive products and services provided by processors are also developing in the expanded services of existing segments, such as catering due to the increasing outsourcing of institutional and accommodation foodservice. The shifting of such services may mean increased demand for value added products that save institutional resources and transfer value added from institutions to suppliers.

Given the regional and relatively fragmented nature of the foodservice, vendor access and support will remain a challenge for suppliers. Such operator/supplier relationships may be strengthened through improvements in information technology and communication. However, recognition of the local market focus must be maintained or emphasized.

Foodservice also has significant impact on agricultural production. Operators have specific demands for their primary ingredients (e.g. variety of potatoes, chicken sizes, vegetable specifications). Because their menus are set for long periods of time, operators depend on receiving primary ingredients on a consistent basis. It is also important that these products be available for as long as possible. For example, in Toronto, a number of hotel chefs have contracted with local growers to supply them with greenhouse produce on year-round basis.

The intensity of product and channel blurring is growing. Due to the significant interest and attention paid to HMR by retailers, interchannel blurring will likely increase. In an attempt to capture market share from operators, retailers are offering competing products ranging from almost ready-to-eat fresh and frozen products to ready-to-eat food products to the inclusion of specific foodservice offerings in retail outlets (e.g. Mövenpik in Loblaws). While the evolution of this trend is unclear, retailers may increasingly look to established foodservice chains to run their HMR operations. Such alliances will require that processors develop products and distribution systems accordingly.

However, competition from HMR will again emphasize the critical need for foodservice attention to ingredient pricing consistency and availability of supply. For example, the pricing structure for dairy ingredients includes special pricing for the use of cheese in the preparation of frozen pizza offered by HMR retailers, but not for the use in fresh products offered by operators. Such pressures may lead to operators seeking alternative sources of supply or ingredients, or trying to achieve more flexibility within the current supply system.

FOOD BROKERS

Food brokers ("brokers") are the marketing link between food processors and their retail and foodservice customer base. As agents of processors, brokers provide a range of product sales and marketing services, including retail and head office selling, consumer promotion, category management and invoicing. Brokers touch on any channel where a food product may be sold (e.g. retailers, wholesalers, mass merchandisers, drug and confectionery wholesale, convenience stores.) In particular, the brokers' value added is their local market knowledge, combined with the use of today's innovative technologies and their intimate and in-depth category knowledge as it applies to a particular area or region. In some instances, brokers play a role in screening the viability of new food products, and educating and advising neophyte processors about market realities and the skills – particularly financial resources – that are necessary to effectively deal with the market reality.

SIGNIFICANCE

Brokers represent products in 279 of the 500 categories in a grocery store, about 16,000 grocery items. They currently represent about 31% of the products, mainly dry (including juices) and frozen grocery products as well as foodservice products, that move through grocery distributors' warehouses. Brokers generally do not represent products delivered direct to stores (milk, soft drinks, bread) or commodities such as fresh produce, fresh meat or eggs. It is believed that broker representation in the foodservice is on par with the retail food sub-sector. Brokers may also represent more small- and medium-sized businesses in foodservice than their retail counterparts. Food brokerage firms employ more than 7000 Canadians and generate about $460 million in commission revenue. Foreign processors exporting products to Canada often use the services of Canadian brokers.

STRUCTURE

Consistent with the general trend in the agri-food chain, food brokerage has evolved from primarily province-wide brokers to regional brokers (Western Canada, Ontario, Quebec, and Atlantic) through a series of mergers. The centralization of retailer/operator purchasing points and the customer demand for single-source representation (i.e. one firm representing the processor to the buyer) have motivated these mergers. It is estimated that the number of brokerage houses has declined by 50% since 1991.

Brokers are not a homogenous group. Size of operations and level of sophistication varies widely. However, as in many other fields, the top 20% of Canada's brokerages likely represent 80% of the total tonnage sold.

CONDUCT

Although a national brokerage house does not presently exist in Canada, firms endeavour to provide principals with national coverage through brokerage house affiliations.

Most brokerage houses do not usually take title to the product, but a few houses have integrated to the point where they either manufacture products or take title to products from processors and warehouse and transport products. In this way, these houses form another link in the agri-food distribution chain.

The average brokerage commission in Canada is 4% to 5% of sales. This rate compares favourably with the estimated average cost of a processor's direct sales force of about 7% of sales.

PERFORMANCE

From 1991 to 1997, the grocery and foodservice volume represented by the broker community grew by 33%, from 22.5% of warehouse items to 30.9%. As outsourcing grows in its acceptance and North America becomes more homogenous in its “go to market” strategies, this trend is expected to continue. Brokers believe that they could represent 50% of warehouse categories by 2000.

GLOBAL PERSPECTIVE

Brokers have been used more extensively in the US than in Canada. It is estimated that US brokers handle up to 60% of the products that pass through warehouses. A number of factors contribute to the higher development level in the US:

- a much larger customer base with far more points of contact;
- a larger assortment of products carried in retail stores;
- more processors, many with a regional focus;
- generally, a much larger marketplace; and
- larger volumes and lower commission structure.

The trend to consolidation of brokerage houses seen in Canada is also present in the US market. Many Canadian processors rely on US-based brokers to penetrate the US or other international markets.

Most European brokers take title to the products they represent. These are full-service sales/ marketing/logistics firms which truly carry out the full business continuum.

In Australia, food brokerage is not as well developed as in Canada. It is estimated that less than 15% of products appear to be broker represented.

IMPLICATIONS FOR THE AGRI-FOOD SYSTEM

Consolidation

Food brokerage in Canada has been marked by mergers, resulting in fewer but larger firms with stronger resource bases with which to serve their clients. Observers believe that mid-sized brokers will continue to be pressured by competitive forces. Eventually, food brokerage will be mainly composed of large national firms and niche regional players that serve processors on a regional, specialized class of trade or specialized trade activity (e.g. category management) basis. They also expect more vertical integration will occur and that brokerage houses may increasingly embrace non-traditional functions.

As a result of the efficiencies gained through these mergers, brokers may be better placed to serve the processing sector in Canada. In particular, a greater range of services may be available to small- and medium-sized businesses. On the other hand, as consolidation results in fewer brokerage houses, processors’ choice of brokers is reduced and the leverage of brokers is increased.

Efficient Consumer Response /Efficient Foodservice Response

Through its participation on the ECR National Steering Committee, food brokerage is working with other members of the agri-food chain to bring efficiencies to the supply chain. Brokers have made investments in technology and resources to carry out electronic commerce and category management on behalf of small- and medium-sized businesses which may lack the resources to capitalize on the benefits offered by ECR. Among the benefits of this investment is brokers' potential capability to track trade (promotion) spending on their principals' behalf which will be further enhanced as processors' activity becomes available electronically. Because trade spending is of great concern to processors, brokers may lead in timely management information. Brokers are also active on the national EFR committee and in all areas of EFR.

North American Market

With the globalization of the food processing sector, it is possible that the same “go-to-market” strategies will be used across North America. In this case, Canada would need to move closer to US levels of brokerage use. Companies such as H.J. Heinz, Pillsbury, Campbell and Kraft use brokers in the US, but not in Canada. As a portent of this possibility, a US-based multinational processor has recently undertaken a search for brokers across Canada.

There is some speculation that US brokers will enter Canada through either acquisition or the extension of their own operations into Canada. For example, this would occur if a US-based retailer were to move the purchasing function of its Canadian operations to the US, or a major US retailer makes a Canadian acquisition. In these instances, brokers will likely follow their customers. As globalization and consolidation continues, US brokers have followed their customer base into new markets.

CONCLUSION

The food distribution sector is playing an increasingly important role in the Canadian agri-food system by generating significant economic activity and contributing to the provision of one of the world's most affordable food supplies. In addition, as it is the first link in the consumer demand chain, the agri-food sector helps to interpret and respond to current and future consumer trends and, in doing so, shapes the rest of the agri-food supply system.

The past decade has seen this complex sector read the changing needs of consumers and develop itself beyond a purveyor of food products and ingredients to a marketer and a meal solution planner. But in doing so, the distribution sector has astutely identified its customers' continuing emphasis on value. As a result, the sector continues to re-engineer itself through changing formats, products and services, corporate consolidation and the implementation of technological efficiencies. In the process, the traditional competitive channel line between the retail food sub-sector and foodservice has been blurred.

Significant changes in the distribution sector inevitably have an impact on processors and producers. Increasingly, most processors have had to deal with retailers as branded product competitors instead of only vendors that sell their products. At the same time, suppliers are being asked to work more closely with retailers to examine and remove unnecessary costs from the supply chain. Meanwhile, fewer and fewer retailers result in fewer and fewer buyers, thus creating a more demanding business environment.

Difficult macroeconomic conditions, coupled with emerging and beneficial consumer trends, have contributed to the ebb and flow in foodservice growth. In step with the retail food sub-sector, foodservice is reacting with a similar growth strategy – corporate consolidation, the embracing of information technology and a strong consumer focus.

In the past, brokers may have been seen as the somewhat underused resource of consumer, market and category information. Today, given their rising sophistication and influence, brokers are poised to provide more comprehensive service in Canada, particularly with small- and medium-sized processors.

Opportunities will exist for suppliers that help the distribution sector respond to consumer needs by emphasizing value or react to the blurring of the interchannel competition between food retail and foodservice.

The Canadian agri-food system begins and ends with the consumer; the only constant is change. The distribution sector remains an important portent of these changes. Accordingly, suppliers must continue to acknowledge, understand and respond to these changes if they are to remain competitive.

FIGURES

FIGURE 1

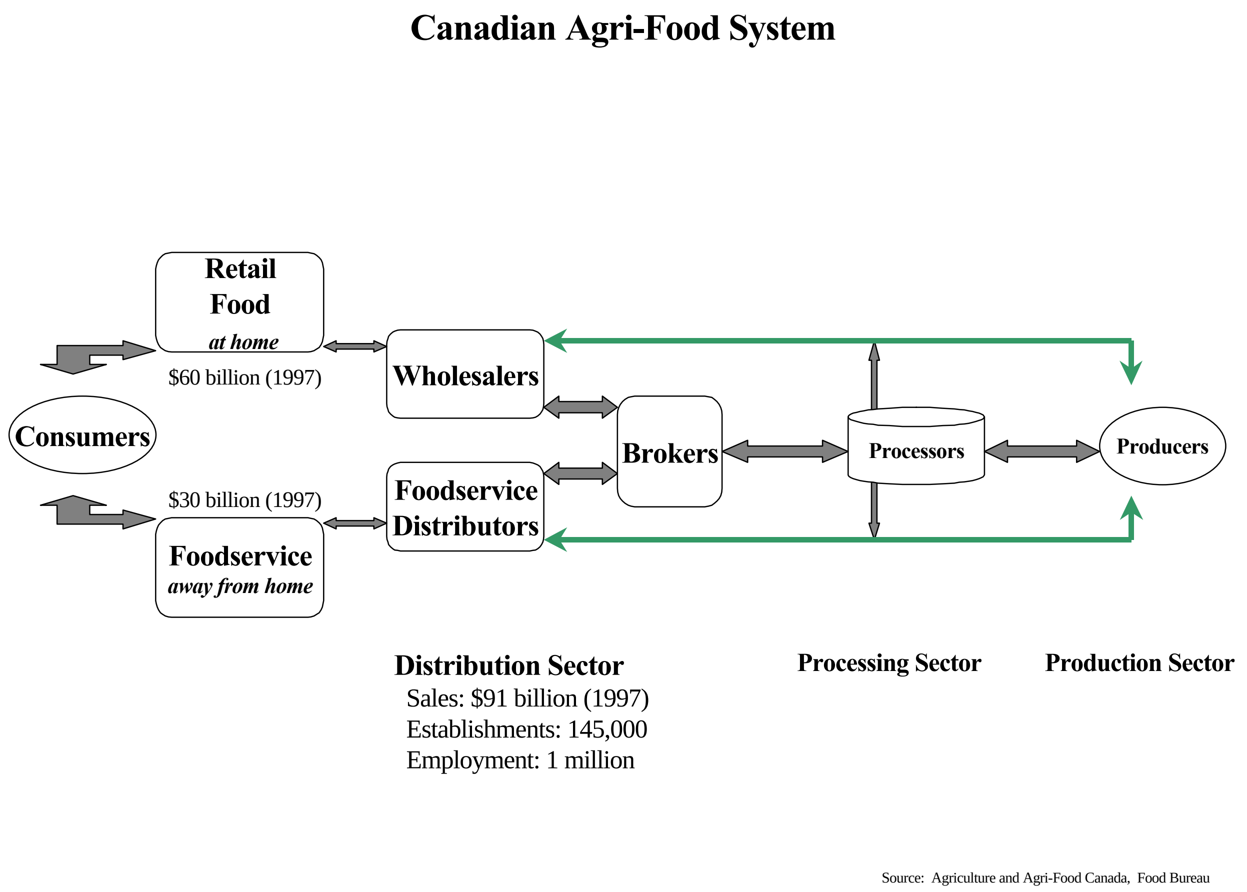
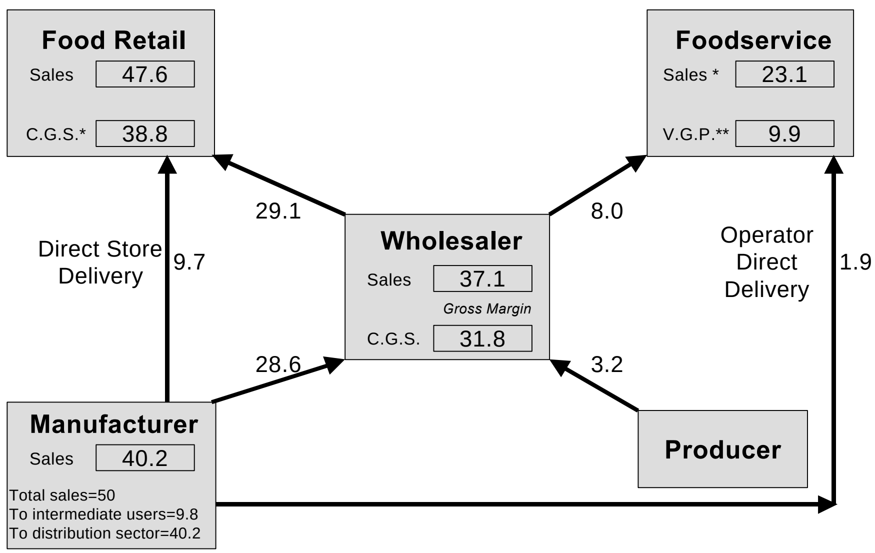


FIGURE 2

FIGURE 2

Estimated Revenue Flows
Food and Non-Alcoholic Beverages
(includes fish)
$ billions in 1996



Source: AAFC

*** C.G.S.: Cost of Goods Sold**
*** V.G.P.: Value of Goods Purchased**

FIGURE 3

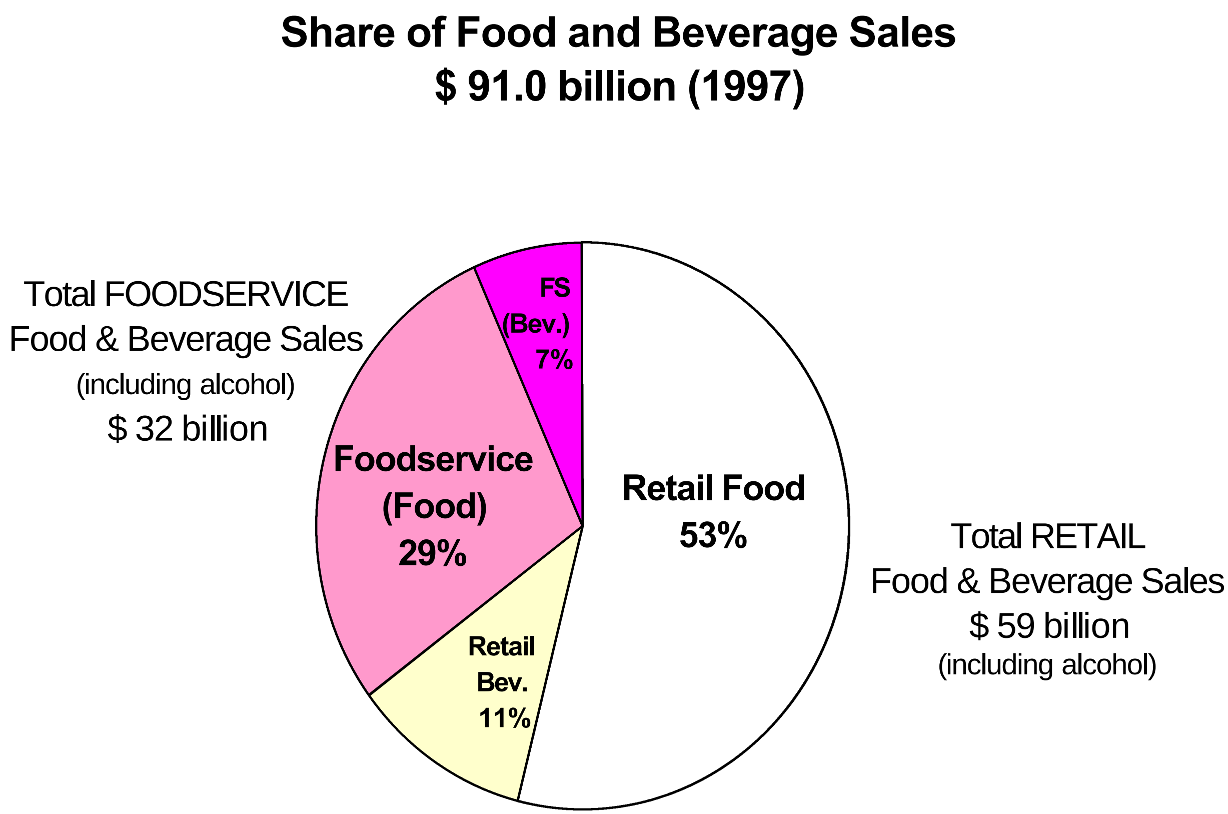
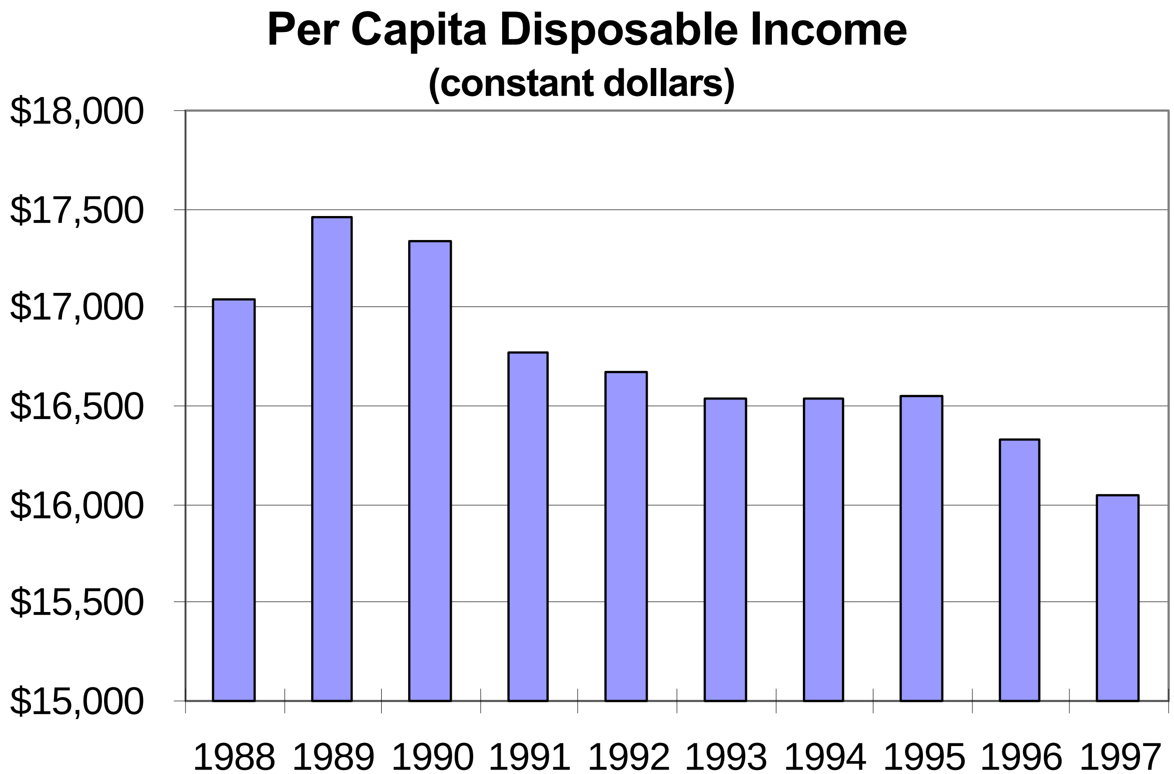

Share of Food and Beverage Sales
$ 91.0 billion (1997)
Total FOODSERVICE
Food & Beverage Sales
(including alcohol)
$ 32 billion
FS
(Bev.)
7%
Foodservice
(Food)
29%
Retail Food
53%
Retail
Bev.
11%
Total RETAIL
Food & Beverage Sales
$ 59 billion
(including alcohol)

FIGURE 4


Per Capita Disposable Income
(constant dollars)
$18,000
$17,500
$17,000
$16,500
$16,000
$15,500
$15,000
1988
1989
1990
1991
1992
1993
1994
1995
1996
1997

TABLES

TABLE 1
CANADIAN AGRI-FOOD SYSTEM
1994

	Sales* ($ mil.)	GDP ($ mil.)	Trading Profit ($ mil.)	Jobs
Retail	45,000	7,000	1,000	342,117
Foodservice	28,000	13,000	1,600	875,000
Wholesale	44,000	3,900	400	68,223
Broker	460	n/a	n/a	7,000
Processor	58,000	12,000	4,700	249,000
Producer	25,800	12,000	6,600	425,000

**Wholesale and retail sales do not include alcoholic beverages.*

TABLE 2
RETAIL FOOD SALES

	Current ($)	**Constant (1992)** ($)	**Increase over previous year** (%)	**Per capita constant** ($)
1988	37,170	40,140	x	1,492
1989	38,957	40,835	1.7	1,491
1990	41,108	41,440	1.5	1,491
1991	42,858	42,225	1.9	1,502
1992	42,560	42,560	0.8	1,492
1993	44,107	43,327	1.8	1,499
1994	44,832	43,996	1.5	1,503
1995	46,290	44,254	0.6	1,494
1996	47,580	44,929	1.5	1,500
1997	49,104	45,678	1.7	1,508

Source: Statistics Canada, CANSIM matrices 6434, 6535, 0001

TABLE 3
FOOD RETAIL CHANNEL SHARE
1996
(percentage)

Supermarket/Grocery Store	83
Speciality Food Stores	8
Drug Stores	2
Warehouse Clubs	4
Mass Merchandisers (incl. Dept. stores)	1
Gas Stations and Others	2
Food and Non-Alcoholic beverages	100

Source: Statistics Canada/AAFC

TABLE 4
TRADITIONAL FOOD STORE SALES (INCLUDES FOOD AND NON-FOOD)
1997

		No. of Stores	% of Total Stores	Sales `($millions)	% of Total Sales
Chains	Supermarkets	1,611	5	25,763	45
	Convenience Stores	6,290	18	3,500	6
Independents	Voluntary Groups	5,212	15	19,918	35
	Unaffiliated	13,217	37	3,270	6
Specialty Food Stores*		9,203	26	4,197	7
TOTAL		**35,533**	**100**	**56,648**	**100**

Source: Canadian Grocer "The Canadian Grocery Industry, 1997" p. 6.
**number of outlets is from Statistics Canada (1994)*

TABLE 5
POPULATION PER GROCERY STORE IN MAJOR US AND CANADIAN MARKETS

Rank*	City	# of Stores	Population	Density**	Country
1	**Hamilton**	**19**	**650**	**34,211**	**Canada**
2	Minneapolis	99	2,790	28,182	US
3	**Toronto**	**160**	**4,445**	**27,781**	**Canada**
5	Boston	214	5,817	27,182	US
6	**Vancouver**	**87**	**1,891**	**21,736**	**Canada**
7	New York	412	8,573	20,808	US
15	Chicago	467	7,789	16,679	US
16	L.A.	552	9,159	16,592	US
18	**Calgary**	**53**	**852**	**16,075**	**Canada**
19	Miami	133	2,061	15,496	US
21	Grand Rapids	70	1,015	14,500	US
31	San Francisco	127	1,664	13,102	US
33	**Montreal**	**260**	**3,359**	**12,919**	**Canada**
35	**Kitchener**	**32**	**403**	**12,594**	**Canada**
40	Washington	374	4,612	12,332	US
45	**Edmonton**	**77**	**892**	**11,584**	**Canada**
46	Portland	156	1,778	11,397	US
47	**Ottawa**	**71**	**777**	**10,944**	**Canada**
51	Syracuse	71	746	10,507	US
54	Atlanta	351	3,579	10,197	US
56	**Victoria**	**47**	**313**	**6,660**	**Canada**
57	**Quebec City**	**112**	**698**	**6,232**	**Canada**
60	Reading	57	352	6,175	US
61	Omaha	113	682	6,035	US

*abridged table; original includes 61 cities

**Density=Population/Store

Source: "Distribution Study of Grocery Store Sales", Supermarket News; and Statistics Canada

TABLE 6
FINANCIAL PERFORMANCE - AGRI-FOOD SYSTEM (POST FARMGATE)
(percentage)

	1988	1991	1994	1995	1996	Average 1988-96	1988-91	1991-96	1994-96
Food Wholesale/Retail									
Operating Profit Margin	1.74	1.65	0.91	1.90	1.85	1.58	1.79	1.45	1.55
Net Profit Margin	1.17	0.64	-0.49	0.80	0.76	0.78	1.29	0.41	0.36
Return on Assets	4.47	2.78	-2.04	3.39	2.94	3.12	5.19	1.68	1.43
Return on Equity	14.64	10.84	-8.76	14.64	12.58	11.56	18.52	6.79	6.15
Return on Capital	5.26	5.91	3.28	5.39	8.39	5.62	6.09	5.35	5.69
Food Service									
Operating Profit Margin	4.55	2.98	2.31	3.38	5.16	3.64	4.05	3.25	3.62
Net Profit Margin	3.10	0.85	0.50	0.89	1.24	1.41	2.22	0.77	0.88
Return on Assets	6.62	1.71	0.97	1.85	1.90	2.89	4.80	1.41	1.57
Return on Equity	23.46	6.71	3.92	7.56	7.97	10.49	16.76	5.68	6.48
Return on Capital	12.20	6.65	4.48	5.70	5.73	7.34	10.13	5.37	5.31
Food Manufacturing									
Net Profit Margin	2.24	1.96	2.19	1.66	1.87	2.02	2.10	1.97	1.91
Return on Assets	5.28	3.98	3.99	3.16	3.67	4.10	4.57	3.76	3.61
Return on Equity	13.07	9.99	8.90	7.28	8.68	9.90	11.54	8.82	8.29

Source: Statistics Canada, Quarterly Financial Statistics

TABLE 7
TOP 10 ENTERPRISES BASED ON ANNUAL OPERATING REVENUE
(percentage)

Food Retailing Industry:	1988	1991	1994	1995	1996	1997	Average Period	Average 1988-1992	Average 1993-1997	Average 1995-1997
Trading Profit Margin	2.72	3.50	3.36	4.12	4.04	3.89	3.41	3.19	3.62	4.02
Operating Profit Margin	1.90	2.37	2.02	2.79	2.74	2.65	2.26	2.19	2.33	2.72
Net Profit Margin	1.18	0.92		1.42	1.30	1.37	1.07	1.08	1.06	1.36
ROE	11.22	16.00		16.46	14.34	14.33	12.34	12.87	11.80	15.05
ROA	3.93	3.27		4.67	4.48	4.71	3.62	3.64	3.60	4.62
Op. Profit /Equity	18.04	41.27	24.26	32.34	30.32	27.66	27.94	29.34	26.53	30.11
Op. Profit /Assets	17.26	24.15	17.34	22.06	25.23	23.05	20.56	21.21	19.91	23.45
Inventory Turnover (X)	13.28	13.81	14.39	14.49	14.39	15.27	14.10	13.59	14.62	14.72

Food and Non-Alcoholic Beverages Processing Industry:	1988	1991	1994	1995	1996	1997	Average Period	Average 1988-1992	Average 1993-1997	Average 1995-1997
Trading Profit Margin	5.54	6.44	7.43	6.14	6.54	6.54	6.54	6.64	6.69	6.62
Operating Profit Margin	4.14	4.63	5.28	3.97	4.34	4.36	4.56	4.74	4.38	4.23
Net Profit Margin	2.69	2.79	2.75		2.10	2.16	2.37	2.62	2.05	2.13
ROE	19.61	14.77	10.62		10.83	11.38	12.10	14.28	9.39	11.10
ROA	7.47	7.19	5.36		4.53	4.57	5.23	6.07	4.19	4.55
Op. Profit /Equity	30.15	24.51	20.37	24.10	22.40	22.98	23.32	25.58	21.07	23.16
Op. Profit /Assets	22.94	27.62	27.28	22.37	25.40	24.72	25.25	26.30	24.20	24.16
Inventory Turnover (X)	11.83	14.37	10.76	11.54	10.58	11.28	11.60	12.20	11.00	11.13

Empty cells not available due to confidentiality
Source: Statistics Canada - Special Tabulation

TABLE 8
US SUPERMARKET INDUSTRY
PERFORMANCE

	1992	1993	1994	1995	1996	Average
Gross Margin	24.9	24.5	25.2	25.2	25.1	25.0
EBITDA (% sales)	3.7	4.1	4.7	4.8	4.7	4.4
Net Profit Margin	0.5	0.9	1.1	1.2	1.1	1.0
ROA	2.2	3.2	4.2	3.6	4.0	3.4
ROE	8.7	13.2	16.2	13.6	16.3	13.6
Investment/Sales	-	-	2.5	2.7	2.9	2.7
Asset Turnover	4.6	3.4	3.7	3.0	3.7	3.7
Inventory Turnover	15.8	15.5	16.0	17.8	17.2	16.5

Source: FMI

TABLE 9
PERFORMANCE OF THE LARGEST FOOD RETAILERS
CANADA AND US

	1991	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**		**Average**	
Loblaw								**Period**	**1993/1997**	**1995/1997**
Sales $M	8,533	9,262	9,356	10,000	9,854	9,848	11,008	9,694	10,013	10,237
Net Income $M	105	80	93	127	147	174	213	134	151	178
Capital Exp $M	154	198	315	339	302	389	517	316	372	403
Invest/Sales	1.80	2.14	3.37	3.39	3.06	3.95	4.70	3.2	3.7	3.9
EBITDA/Sales	3.80	3.40	3.50	4.10	4.60	4.90	5.20	4.2	4.5	4.9
NI/Sales	1.23	0.86	0.99	1.27	1.49	1.77	1.93	1.4	1.5	1.7
NI/Assets	4.4	3.2	3.4	4.3	4.6	4.9	5.3	4.3	4.5	4.9
Inventory Turn	13.8	14.4	14.3	14.3	16.2	14.9	15.6	14.8	15.1	15.6
P/E						**17.3**				
Sales/sq.ft							**534**			
Avg. Store Size							**43,600**			
									Average	
Kroger								**Period**	**1993/1997**	**1995/1997**
Sales ($M US)	21,351	22,145	22,384	22,959	23,938	25,171	26,567	23,502	24,204	25,225
Net Income ($M US)	101	101	171	269	319	353	444	251	311	372
Capital Exp ($M US)					726	734	612	691	691	691
Invest/Sales					3.03	2.92	2.30	2.8	2.8	2.8
EBITDA/Sales		4.40	4.06	4.29	4.80	4.86	5.20	4.6	4.6	5.0
NI/Sales	0.47	0.46	0.76	1.17	1.33	1.40	1.67	1.0	1.3	1.5
NI/Assets	2.5	2.3	3.8	5.7	6.3	6.0	7.0	4.8	5.8	6.4
Inventory Turn	13.8	14.2	14.2	14.2	14.7	14.7	14.7	14.4	14.5	14.7
P/E						**17.9**				
Sales/sq.ft ($CDN)							**537**			
Avg. Store Size							**49,418**			

Source: Annual Company Reports

TABLE 10
TRADING PROFIT, AGRI-FOOD SYSTEM
($ billion)

	Agriculture	Food & Beverage Manufacturing	Retail & Wholesale	Food Service	Food Marketing
1988	2.9	3.4	1.8	1.7	3.5
1989	3.1	3.6	2.1	1.9	4.0
1990	6.2	3.6	2.0	1.7	3.7
1991	6.0	3.8	1.9	1.5	3.5
1992	6.2	4.4	1.7	1.6	3.2
1993	6.5	4.3	2.1	1.5	3.6
1994	6.6	4.7	1.5	1.6	3.1
1995	7.5	4.5	2.4	2.0	4.3
Average	5.6	4.0	1.9	1.7	3.6
Total	**45.0**	**32.2**	**15.5**	**13.5**	**29.0**
Share	0.42	0.30	0.15	0.13	0.27

Trading Profit: Earnings before net interest, taxes, depreciation and amortization.

Source: AAFC and Statistics Canada.

TABLE 11
FOODSERVICE SALES
1997

	Sales ($millions)	% of Total Foodservice	% of Segment
Commercial	24,295	75	100
Licensed Restaurants	11,605	36	48
Unlicensed Restaurants	5,866	18	24
Take-out and Delivery	3,407	11	14
Social and Contract Caterers	1,958	6	8
Pubs, Taverns and Nightclubs	1,459	5	6
Non-commercial	7,915	25	100
Accomodation	3,400	11	43
Institutional	2,463	8	31
Leisure Industry	1,003	3	13
Vending Machines	267	1	3
Department Stores	240	1	3
Other	542	2	7
Total Foodservice	**32,210**	**100**	

Source: Canadian Restaurant and Foodservices Association, Foodservice Facts

TABLE 12
FOOD SERVICE SALES
($million)

	1990	1991	1992	1993	1994	1995	1996	1997
Commercial								
Rest -Licensed	8,741	7,978	8,291	8,848	9,132	10,669	11,218	11,605
Rest - Unlicensed	5,218	4,904	5,194	5,273	5,660	5,602	5,822	5,866
Take Out	2,470	2,249	2,296	2,445	2,738	3,008	3,193	3,407
Social Contracts	1,634	1,558	1,624	1,579	1,597	1,703	1,738	1,958
Pubs and Taverns	1,244	1,164	1,165	1,297	1,410	1,309	1,349	1,459
Sub-Total	**19,307**	**17,853**	**18,570**	**19,442**	**20,537**	**22,291**	**23,320**	**24,295**
Non-Commercial								
Accommodation	3,405	3,131	3,173	3,016	3,006	3,327	3,398	3,400
Institutional	2,231	2,465	2,490	2,352	2,258	2,663	2,665	2,463
Leisure	875	915	909	932	964	979	969	1,003
Vending	305	258	222	239	240	252	266	267
Other	234	224	226	232	242	540	543	542
Department Stores	247	233	231	212	221	231	225	240
Sub-Total	**7,297**	**7,226**	**7,251**	**6,983**	**6,931**	**7,992**	**8,066**	**7,915**
Total ($ million)	**26,604**	**25,079**	**25,821**	**26,425**	**27,468**	**30,283**	**31,386**	**32,210**

SHARE OF SALES
(percentage)

	1990	1991	1992	1993	1994	1995	1996	1997
Commercial								
Rest -Licensed	33	32	32	33	33	35	36	36
Rest - Unlicensed	20	20	20	20	21	18	19	18
Take Out	9	9	9	9	10	10	10	11
Social Contracts	6	6	6	6	6	6	6	6
Pubs and Taverns	5	5	5	5	5	4	4	5
Sub-Total	**73**	**71**	**72**	**74**	**75**	**74**	**74**	**75**
Non-Commercial								
Accommodation	13	12	12	11	11	11	11	11
Institutional	8	10	10	9	8	9	8	8
Leisure	3	4	4	4	4	3	3	3
Vending	1	1	1	1	1	1	1	1
Other	1	1	1	1	1	2	2	2
Department Stores	1	1	1	1	1	1	1	1
Sub-Total	**27**	**29**	**28**	**26**	**25**	**26**	**26**	**25**

Source: CRFA

TABLE 13
FOODSERVICE SALES
($ million)

	Current $	Constant $ (1992)	% Annual Change	Per Capita (constant $)
1988	23,806	29,692	x	1,104
1989	24,588	29,141	-1.9	1,064
1990	26,604	30,060	3.2	1,082
1991	25,079	25,565	-15.0	909
1992	25,821	25,821	1.0	905
1993	26,425	26,079	1.0	903
1994	27,468	26,772	2.7	915
1995	30,283	28,939	8.1	977
1996	31,386	29,515	2.0	985
1997	32,210	29,795	0.9	984

Source: CRFA and Statistics Canada

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