The cost of food and drink

by **David Read**, chief executive, Prestige Purchasing

The most recent headlines on inflation make encouraging reading for those buying food and drink in the UK. "Food inflation hits 14-month low" was the key theme that the media picked up on. But delve just a tiny bit deeper and there is a different story.

After all, here we are in times when following the biggest financial meltdown since the 1930s, during the worst recession in 30 years, and when the greatest fear of the Bank of England is a prolonged period of deflation, yet food is still showing over 5% inflation. And the current outlook is that as the global economy recovers from the shockwaves of 2008, so too will the kind of price jumps that we saw at the end of 2007 and into the following year.

So sitting back and expecting to pass on any increases in food cost to the customer might prove to be a costly strategy. Yet for many restaurant businesses the potential for better rather than worse margins lies unnoticed and untapped for years, and the decision about whether to exploit it or not rests entirely within the management's own control.

The key to success lies within the complex world of distribution. In simple terms food and drink comes from farm, through processor, importer or primary wholesaler, to some form of secondary distributor who actually delivers it to the caterer's back door. Depending upon the particular product concerned these "supply chains" can be quite short, rather long, or somewhere in between. Quite often the same clients who buy strawberries direct from a local farm, are the same ones that buy processed foods with ingredients from all over the world. Foodservice outlets obtain produce through three main channels: wholesale, contract/central distribution (CD), and cash and carry. In some cases local suppliers such as butchers, bakers and fish retailers are used. In areas like coffee, cheese and snacks specialist suppliers may be used.

To understand the potential available from changes to the way you buy your food and drink, it is necessary to examine the behaviour of the large-scale operators. Progressively over the past 15 years they have moved away from using the wholesale model to one of CD. They have done this for a number of reasons:

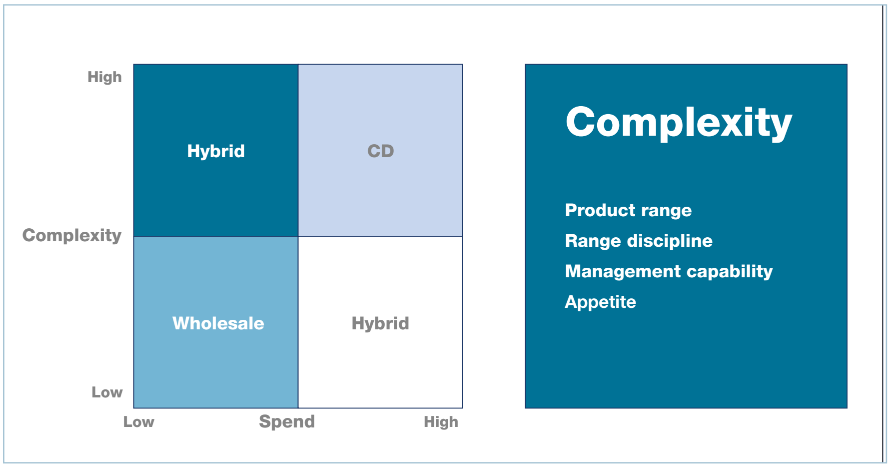
Stocking costs – by their nature, wholesalers have to carry a very wide number of product lines to service their large variety of customers. This ties up cash and adds complexity (and therefore cost) to the operators. This all adds up to a higher price of goods. Large-scale operators on the other hand buy high volumes of fewer products.

Reduced distribution cost – centralising the distribution of food and drink to store means less trucks, less drivers, less miles and way less complexity. Again, the cumulative effect of reducing all this is much reduced cost.

Direct access to supply – whilst wholesalers do buy in bulk and therefore have strong leverage with their suppliers, large-scale operators have found that direct access often creates lower price, improved quality and more access to critical things like innovation.

Control – Like it or not, even the best of wholesalers have an agenda. Why? Because they have shareholders and they have other customers. The large-scale operators like the control and flexibility granted to them by CD.

Wholesale or CD?



So why isn't everyone on CD? Don't get me wrong, the wholesalers do an outstanding job. By buying from a wholesaler you are effectively outsourcing your supply chain to a third party, and you generally get a good choice of product, reliability of supply, and low management effort – you just call and they just deliver.

And there are some serious practical constraints to operating CD. The very nature of CD dictates that the distributor is paid merely to carry the goods, and may or may not take actual title to them. The foodservice operator must therefore control its own sourcing and play a more active role in the management of its supplier relationships. This can place an unwanted burden on the organisation. For this reason many operators outsource their buying, but on a fee basis and with complete transparency, so that they can access the benefits of CD without the organisational burdens.

The other reason historically has been scale. CD works by the orders being placed for bulk delivery into the distributor, who then picks, packs and delivers. Only the largest and the most controlled of operators have been able to do this because the system cannot cope with lots of small quantities of individual product lines.

For a long time the operators' response to this has been to create a kind of hybrid CD where they negotiate a number of "nominated lines" with their wholesaler on a case rate or percentage on-cost. This gives the ability to access manufacturers and processors direct, but leaves the tail of product lines on a wholesale agreement.

Whilst a good compromise, this hybrid CD does not give anything like the level of control available from CD, and dilutes many of the other benefits as well. So people buying food and drink have been on the lookout for new solutions for some time. The great thing about capitalism is that where there is a gap in the market it is never long before someone comes along to fill it.

In recent times a new breed of distributor has emerged that makes the benefits of CD available on a restaurant's high volume lines and then takes just one delivery from a wholesaler for the remaining lines. This delivery is split into one for each of the branches, and is merged with the high volume lines already in stock.

Strategies for minimising distribution costs

- **Reduce your delivery frequency**
- **Increase your average drop value**
- **Enhance the order capture process**
- **Improve ranging/rationalisation**
- **Consolidate categories onto fewer vehicles**
- **Move to some form of contract distribution**
- **Lengthen your order cycle**

This solution not only delivers the kind of efficiency and cost reduction generally only available to those in CD, but gives control back to the caterer on all the high value items in the business. And it is deliverable on an extremely small scale – here at Prestige we have a client with just five outlets operating in this way.

One thing is certain. The restaurateur can no longer simply pick up the phone to the neighbourhood wholesaler and still remain competitive. With the cost of moving food often as much as 25% of the item cost, it is time every caterer understood the 'wheel cost' of food and drink!