

# **Horticultural value chain analysis**

Brendan Nolan  
Growcom

Project Number: HG03071

## **HG03071**

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# **Horticultural Value Chain Analysis and Policy Development**

prepared by

**CDI PINNACLE MANAGEMENT**



## PROJECT DETAILS

HG03071 Horticultural Value Chain Analysis and Policy Development

Funded by Horticulture Australia Limited and Growcom (Queensland Fruit & Vegetable Growers).

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## PREFACE AND MEDIA SUMMARY

In June 2004, Queensland Fruit & Vegetable Growers Ltd (now trading as Growcom) and Horticulture Australia Ltd (HAL) retained the services of CDI Pinnacle Management to undertake a research and policy development project pertaining to the Queensland horticultural value chain.

In broad terms the project has sought to:

- Develop a snapshot of the major drivers pertaining to the food industry, especially horticulture that are occurring globally.
- Gain a detailed understanding of the structures and issues influencing value chain participants beyond the farm gate in Australian horticulture.
- Identify the knowledge of and issues influencing Queensland horticultural producers and their attitudes / actions / relationships with the remainder of the value chain.
- Identify and discuss models and methods of doing business that may occur across the whole chain.
- Discuss and provide recommendations for actions that organisations such as Growcom and HAL may or should provide to the horticultural production sector in order for it to be better prepared for future change.

A grower survey was conducted in order to evaluate what are the current business practices engaged in by producers with others in the chain, issues associated with these relationships and how in the opinion of producers others may be able to assist them become better or more effective chain 'performers'.

These findings were 'benchmarked' with research undertaken about how international value chains are performing and secondarily with how others in the value chain within Australia view the production sector.

From these "three angles" a series of recommendations have been developed about how the production sector of Queensland (and Australian) horticulture may be provided with a framework to develop the skills, experience, confidence and structures necessary to become:

Strong and valued contributors to Australian food (and horticultural) value chains.

Internationally competitive members of the global horticultural industry.

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Our clients are innovators, early adopters and industry leaders and agencies. They are corporations in the food and agribusiness industry, small to medium enterprises (SMEs), individual producer / marketers, producer groups, development and government agencies, and marketers and processors.

CDI Pinnacle Management takes a non-traditional, interactive approach to consultancy. Using a step-by-step process, we assist businesses and agencies in developing and implementing progressive and tailor-made solutions.

We assist firms, industries and regions to develop and implement a global vision and provide the tools and assistance to achieve success in domestic and international arenas.

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## CHAIN SECTOR DEFINITIONS

In consideration of the literature, particularly that which is referenced from overseas, there is a variety of definitions pertaining to each sector of the horticultural chain. For the purposes of this report, the following definitions or rules will apply:

**Horticulture:** For the purposes of this report horticulture will not include cut flowers, turf and nursery products, but rather concentrate on fruits (not wine grapes) and vegetables.

**Grower:** Will also be referred to as producer or farmer. A person or company who grows and harvests produce.

**Produce:** Collectively referred to as fresh fruit and vegetables.

**Input Provider:** Are those companies who provide a range of goods and services to growers for the production of their produce. Examples of these companies include seed, chemical and fertiliser companies, crop agronomists, consultants and government agencies (i.e. DPI).

**Wholesaler:** A person or company who receives fresh produce from growers and who then markets that produce. The transaction may be on either a merchant or agency basis. A wholesaler does not undertake any transformation of the produce. Definition does not include brokers.

**Agent:** An agent agrees to undertake to sell the produce of the grower for the best possible price in return receiving an agreed percentage of the gross sale price. Due to the introduction of the Good and Services Tax (GST), industry sources suggest that few if any wholesaler transactions are on an agency basis.

**Merchant:** Is a wholesaler who purchases produce from a grower and then sells it to a third party. The difference between the actual sale price and that paid to the grower being the margin to the merchant. Industry sources suggest that this is predominate transaction basis operating between wholesalers and growers.

**Broker:** A person or company who markets a product on behalf of a grower for an agreed fee in advance. Title of goods does not pass to the broker at any stage. This fee may be a per unit value or per unit percentage.

**Providore:** A person or company who purchases goods from wholesalers and who then sells the product to restaurants, small food service outlets, caterers etc. There is limited transformation of the produce, save for repackaging. Transactions to customers are generally on a cost plus basis.

**Pre-Packer:** A company who takes bulk produce and packs into retail-ready sized packages. Most common with apples, citrus, onions and potatoes.

**Processor:** A person or company who takes produce and undertakes a major transformation of the produce. Examples of transformations include drying, dicing, cutting, preserving, juicing and using it as an ingredient. It does not include repackaging. Examples of processors in Queensland include Golden Circle, Mrs Crockett's, Harvest Fresh Cuts.

**Food Service:** Are companies who sell value added food to consumers. This will include fast food outlets, e.g. McDonalds, Subway and restaurants.

**Exporter:** A person or company who takes Australian produce and who then sends and / or sells the product to a country other than Australia. Exporters can buy produce direct from growers, wholesalers or brokers. An exporter generally works on a margin or cost plus basis.

**Retailer:** A company who sells produce to consumers and includes fruit barns, specialist fruit shops and supermarkets other than chain store and independent chain store retailers.

**Chain Store Retailer:** Are groups of companies who sell produce under a common corporate banner, e.g. Woolworths, Coles and Aldi. It does not include retail chains who have individual ownership of stores, e.g. IGA. In other countries may be referred to as multiples.

**Independent Chain Store Retailer:** Are groups of companies who have a common corporate banner but individual store ownership, e.g. IGA.

## 1.0 EXECUTIVE SUMMARY

This project's consultancy brief, "Horticultural Value Chain Analysis and Policy Development" sought to:

- Develop a snapshot of the major drivers pertaining to the food industry, especially horticulture that are occurring globally.
- Gain a detailed understanding of the structures and issues influencing value chain participants beyond the farm gate in Australian horticulture.
- Identify the knowledge of and issues influencing Queensland horticultural producers and their attitudes / actions / relationships with the remainder of the value chain.
- Identify and discuss models and methods of doing business that may occur across the whole chain.
- Discuss and provide recommendations for actions that organisations such as Growcom and HAL may or should provide to the horticultural production sector in order for it to be better prepared for future change.

A grower survey was conducted in to evaluate the current business practices engaged in by producers with others in the chain, issues associated with these relationships and how in the opinion of producers others may be able to assist them become better or more effective chain 'performers'.

These findings were 'benchmarked' with research undertaken about how international value chains are performing and how others in the value chain within Australia view the production sector.

From these "three angles" a series of recommendations have been developed about how the production sector of Queensland (and Australian) horticulture may be provided with a framework to develop the skills, experience, confidence and structures necessary to become:

Strong and valued contributors to Australian food (and horticultural) value chains.

Internationally competitive members of the global horticultural industry.

### 1.1 Globalisation Issues

#### CONSUMERS

Globalisation in the food industry is being driven by the needs / wishes / wants of consumers. These include:

- Income growth of consumers;
- Convenience;
- Greater assortment / variety of offer;
- Mass customisation;
- Desire to achieve greater chain awareness i.e. Where produce comes from;
- Increased health focus; and,
- Food safety and security.

Retailers, whether supermarkets, quick service restaurants (QSR), food service or others, are all directly impacted by the 'whim' of the consumers, and so will in an effort to secure the consumer dollar be as responsive to them as possible. This chain reversal has resulted in food retailers having enormous power 'down' the chain and so their decisions / strategies are what is driving the structure and nature of the food, including horticultural, industries.

## **RETAILERS**

Some of the developments that have occurred in the global food industry include:

1. Fewer but larger global retail food retailers.
2. A marked reduction in the number of suppliers used by global retailers.
3. A shift away from local to global sourcing policies by global retailers and in some instances processors and value-adders.
4. Increased use of house brands and private labels, altered store orientation, promotion of health and nutrition benefits by retailers as a means of differentiation from others.
5. An increasing focus on the achievement of cost efficiencies across the chain rather than increased sales margin generation.
6. Increasing movement towards supply and category management responsibilities being passed to others in the chain by retailers and some food processors.
7. Across chain development of and demand to others of food safety compliance and chain integrity.
8. Increasing development of alliances with others in the chain who are pro-active in terms of seeking innovative solutions across the broad range of consumer 'delivery requirements'.
9. A blurring of the line between fresh produce traditionally focussed on by retailers and meal solutions as provided by restaurants and quick service restaurants (QSR) with both sectors achieving cross overs between the 'categories'.
10. Greater focus on the use of information technologies (IT) across the chain to provide improved information and communication dissemination.
11. A trend towards the development of closed food supply systems whereby relatively few participants are involved in the transactional processes and / or the system is 'protected' by access to plant varieties protected by patent or IP.

## **PRODUCTION**

In response to the changing structures and needs of the global food and processing sectors the structure of the production has changed as well. Some of these changes include:

1. The development of global horticultural production and supply companies eg. Dole, Delmonte, Capespan and Chiquita. Concurrently a number of these global producers have developed internationally recognised brands.
2. Greater integration with global retailers and food processors particularly towards supply management and increasingly category management.

By comparison, Australia is regarded as a small player in terms of international trade in horticultural produce with considerably less than 1 per cent of total market share. Indeed it is outperformed 2-3 times by our neighbour New Zealand in terms of export performance. In fact over the last 2 years the total value of Australia's horticultural exports have declined.

Internationally, Australia is regarded as a poor performer in terms of reputation and the ability to meet the needs of the growth end of the market, global retailers.

Further Australia is regarded as an opportunistic exporter of produce, having a greater focus on the domestic market. This market is generally oversupplied, has many producers, is strongly competitive and in terms of communication and price transparency relatively dysfunctional.

These issues combined with a rapidly changing and evolving retail sector is now placing enormous change pressures on the Australian production sector.

## **1.2 The Australian Horticultural Production Sector**

The Australian horticultural production sector is comprised of 3 principal grower 'types':

- Individual growers;
- Network growers; and,
- Consolidators or Grower Packer Marketers.

Characteristics of each grower type and the roles that they play within the sector are described in Section 4.3.

Over time, with the decisions of large retailers and processors to deal with fewer and fewer supplies, many growers will have to become part of networks either as network growers or grower consolidators. Further some of these growers may become part of other consolidation networks, such as to "In-house consolidations networks" or to "Non-grower Consolidations networks"

## **1.3 Key Consultation Findings**

The key findings or conclusions identified from this survey are:

1. The vast majority of growers grow independently of others.
2. There is a moderate level of diversification amongst survey respondents into other agricultural and non-agricultural business activities. However, the survey was not able to determine if horticulture was the principle business activity or not.
3. There is a low level of grower consolidation amongst the survey respondents and from observations of the consultants amongst the wider industry.
4. Over 74 per cent of the survey respondents market their production to the wholesale sector.
5. The vast majority of production is marketed / consigned to Queensland or New South Wales customers. Just over 11 per cent of produce is sold to Victoria.
6. Growers generally agreed with other industry sources that the average rate of deductions by wholesalers from the gross sale price is between 11 and 15 per cent.
7. Producers generally have unacceptable systems with wholesalers for the provision of pricing information.
8. Producers generally have unacceptably long waiting periods pertaining to the provision of confirmed price advices by wholesalers.
9. The majority of growers are dissatisfied with the level of service / conduct of the relationship from their customers / service providers immediately adjacent to them in the chain.

## TERMS OF TRADE

The terms of trade or 'how businesses do business together' is highly variable across the producer–wholesaler sectors. This has in part contributed to the dissatisfaction amongst producers and wholesalers in regards to their relationships with one another.

Key findings associated with the 'terms of trade' between producers and wholesalers were:

- There is limited evidence of the use formal contracts or 'standard rules of business arrangement and engagement' specifying the nature of the business relationship between producers and wholesalers.
- Producers believe that the standard average business charge for wholesalers ranged from 11 – 15 per cent of the gross sale return, although on a consignment by consignment basis, the belief is that the figure does vary considerably. This return is an average level of deduction across all producers **over a period of a year**.
- The average level of business charges charged by wholesalers will vary depending on a number of factors including:
  - Variety of produce. High volume lines tend to have a lower business charge in comparison to low volume lines, due to transaction and handling costs.
  - Value of produce.
  - Breadth of sales prices. Products that have a wide range of prices lend themselves to having a wider range of business charges applied.
  - Producer Knowledge. Producers who have a greater degree of understanding of how the market is performing and what 'drives' the market on a given day will position them to make more informed decisions on the placement of produce and better negotiation position.
  - Quality of Product Supplied: Wholesalers value growers who supply high quality produce. Increasingly, as consumers become less and less tolerant of inferior produce, wholesalers will tend to 'look after' good suppliers and become less tolerant of poorer quality suppliers and penalise them by way of returns.
  - Reliability of Produce Supplies: Due to the nature of ordering of buyers in the wholesale market, wholesalers value growers who can supply regular quantities of produce. They are less tolerant of growers who 'play' the markets and wholesalers, as the wholesaler is less able to develop a lasting relationship with a particular customer.
  - Suitability of Product to Other Markets: Some products and sizes / qualities of products are better suited to different markets. There is considerable interstate trading of produce amongst wholesalers and brokers. If a product can give a better price in another market, a wholesaler may send it to that market, either with or without the knowledge of the grower.

Wholesalers may work on a basis that they average a growers return and apply 'average cost' roughly equivalent to industry commission standards and therefore not necessarily follow the practice of standard commission rates.

The level of deduction or 'commission' may vary depending on:

- The performance of the market and how the wholesaler performed in that market;
- Prices returned for equivalent standards of produce by other wholesalers;
- Perceived or actual level of knowledge that the grower has about market performance, sales on other market floors in other states;



- Prices paid by chain store buyers; and,
- The level of competition for additional supplies from a particular retailer.

Discussions indicate there is a wide spread practice of averaging of individual grower returns across a period, often a week.

The Federal government has recently committed to introducing an enforceable Code of Conduct that will have as part of the code a basic rules that define the terms of trade that may exist between commercial parties in the absence of any other form of written agreement. This will have particular impacts on producer / wholesaler relationships who operate under agency or merchant basis.

### **PAYMENT ADVICES AND TERMS**

This industry survey and other anecdotal evidence confirm there is considerable variability associated with how growers are advised about prices, when they are advised and when they receive payment for their product. The research highlighted the following:

- Growers are generally advised of prices by telephone, either with or without subsequent confirmation by facsimile. In a considerable numbers of instances the only price confirmation they receive is when they receive payment (26 per cent of all responses).
- Advice on prices returned or sold for, vary considerably from same day (17 responses) to more than 11 days (8 responses) to other (16 responses). This can be explained in part due to the nature of the product that is being sold, in that highly perishable lines will be turned over or sold more quickly than less perishable lines, e.g. hard produce lines. However, other contributors to the explanation of variable price advice include:
  - Producers don't have written agreements detailing acceptable terms;
  - Producers aren't insistent on receiving prices in a timely fashion;
  - Some wholesalers desire to average prices over a period or undertake some other price 'adjustment' activities; and,
  - Advice terms may be acceptable to the grower.

Average payment periods for produce from wholesalers are also highly variable. Of concern is that more than half of growers receive payment more than 22 days after delivery, whereas the accepted industry standard is two weeks after the week of delivery. 'Slow' payment may impact severely on farmers who have limited cash flow reserves or high overheads i.e. labour intensive farms. Further slow payment will add considerably to financial costs due either to lost interest on credit accounts or higher overdraft / interest charges on debit accounts. Reasons for the slow payment of grower accounts include:

- Poor credit 'management' guidelines employed by wholesalers;
- Growers aren't insistent on payment within terms due to concerns that they may lose a relationship with a wholesaler;
- History determining current practice;
- Cashflow considerations by wholesalers. Some wholesalers if produce is sold to an exporter may not receive payment for six weeks or more. Also some wholesalers may not have adequate financial reserves; and,
- Business viability of wholesalers.

Although not tested, anecdotal evidence suggests that there are a considerable number of growers who receive payment by cheque rather than direct deposit or electronic transfer. In addition to being a delaying payment technique (in some cases), i.e. 'the cheque is in the mail', the delays in payment caused by cheque payments rather than direct deposit have an impact on producers' cash flows.

As discussed in the above section, the Federal government has indicated that it will implement a horticultural industry Code of Conduct which will have in the absence of any other written agreed agreements standard terms and conditions associated with payment advices and terms.

### **MARKET SIGNALS AWARENESS**

There is considerable variation in terms of how aware producers are of price signals primarily with wholesalers. On a daily or 'within season basis', the variation extends from:

- Where growers do not actively seek any information apart from that supplied by their wholesaler and so trust the wholesaler to provide correct price signals

#### **TO**

- Where growers seek out information from independent sources, e.g. Ausmarket, other wholesalers, speak or exchange information with other growers and / or speak with other segments of the value chain, e.g. exporters, on a regular basis

Larger growers are generally more aware of price movements than other smaller growers, presumably as they have 'more' to lose if they are not 'on top' of pricing information. Further, larger growers tends to supply multiple markets and possibly market wholesalers and so are more able to get a broader cross section associated with the supply of prices.

Prices paid by chain store retailers are still set off the market where prices are reviewed weekly. In most instances the prices paid are based on the wholesale market price inclusive of freight delivered to a specific location i.e. Sydney, Melbourne, Brisbane. Growers are therefore responsible for payment of freight directly.

### **RISK MANAGEMENT**

Based on anecdotal evidence and the results of this survey, the horticultural industry is not proficient at the use of risk management tools.

The survey results highlighted that:

1. Nearly half of all respondents do not engage in any other form of business activity than growing fruit and vegetables.
2. Only seven (7) producers indicated that they engaged in non-agricultural business activities although there were a further nine (9) who were engaged in a non-specified activity. The other respondents who did engage in non-horticultural activities were still involved in agriculture either in beef, grains and oilseeds or sugar production.

With regards to 'inside the farm gate' risk management strategies, horticultural farmers generally revolve this around:

- Extending the production season associated with a particular crop;
- producing a variety of crops; and,
- marketing produce to a variety of wholesale markets, to either one or more wholesalers.

Other more sophisticated growers have undertaken a variety of other risk management strategies including:

- Growing product across a variety of regions which are geographically separated from one another in order to minimise the impacts of other adverse weather events.
- Engaging other growers to produce products either within the same or different production regions in order to minimise both the weather and cost of production risk.
- Developing marketing strategies to customer segments where at least some of the price risk is shared, e.g. maximum / minimum pricing.
- Developing forward supply contracts in order to again reduce the supply risk.
- Developing multiple customer strategies.
- Market segmentation - identify customer segments that can take the full range of product sizes and qualities that a grower produces. This effectively results in 100 per cent crop utilisation.
- Engaging in value adding activities either as a stand alone business, in conjunction with other farmers or as a joint venture partner.
- Invest further 'up' the chain in either wholesale, retail or associated service businesses.

Other non-direct farm activities that farmers do not seem to have embraced as extensively as other agricultural business sectors to manage risk include:

- Use of tax legal financial management strategies, e.g. Farm Management Deposits (FMDs), which allow producers to set aside pre-tax primary production income in profitable years to help balance income between good and bad times;
- Superannuation; and,
- Taking of sound financial advice from people beyond tax accountants.

### **RETURN MAXIMISATION**

Growers generally tend to use relatively unsophisticated strategies to maximise returns.

Production based strategies revolve around extension of production season for a crop, production of multiple crops and in some cases sharing of information and capital.

From a marketing perspective, the range of strategies used include:

- Development of forward orders
- Segmentation of the geographic distribution of product i.e. Brisbane, Sydney, Melbourne and export
- Customer segmentation i.e. Direct to retail, sales to processors, different returns.

Due to the unsophisticated nature of these strategies, it may be argued that they in fact result in return averaging.

It can be argued that many growers do not necessarily focus on cost minimisation either through innovation, efficiency evaluations or cost monitoring. This is a significant area of improvement that across the sector growers should focus on in order to maximise returns.

## ***1.4 Developing Successful Value Chains in Horticulture***

In order to develop value chains that are internationally successful, Australian chains must develop similar characteristics in terms of philosophy, structure, alignment and systems to

those chains. Research work undertaken by Fearne and Hughes (2000) and confirmed by our in-industry consultation identified a number of these issues / characteristics:

1. The development of pro-active relationships right across the chain.
2. Development information systems that allow for complete electronic integration.
3. Across chain information sharing for all elements of the business model.
4. A commitment of all members to seek innovative ways to improve market share, produce new products, reduce costs along the chain.
5. Development of chain relationships that seek to pro-actively change the view of customers as to how they view the particular category/ie the chain participates in.
6. Increasingly the development of products that have supply chain exclusivity (closed loop business systems).
7. Partnering with others that have strong financial stability.
8. Focus on whole of value (or supply) chain management.
9. Focus on cost management across the chain.
10. Increasing focus on chain management of the product range, not just retailer management.
11. Co-operative and pro-active input of promotion and merchandising.
12. Strong focus on provision of food safety and supply chain integrity.

### ***1.5 Future Structure and Issues for the Horticultural Production Sector***

In order to develop internationally competitive value chains, in combination with the impact of a number of 'external' issues eg. impacts by others on farmers ability to farm, government legislation, labour, the nature and structure of the horticultural production sector will continue to evolve.

Following consultation by way of surveys, discussions with individual sectoral participants and literature searches, the structure and principal issues that will impact on production sector viability include:

- Fewer horticultural farmers.
- Average size of farms or turnovers will increase over time, with the predominant movement out of the industry being of smaller sized farmers.
- Smaller growers with identifiable market niches who have a strong focus on costs management and good management / business skills will continue to have a strong future.
- A continual movement in and out of the sector of new entrants, only some of which may remain in the industry over time.
- Greater levels of consolidation of produce either at the production level through grower consolidators or through consolidation further up the chain either by non-grower consolidators or retail 'in-house' consolidators.
- Growers will tend to increasingly specialise in the crops that they grow, particularly in the vegetable industry.

- Full or 100 per cent crop utilisation (growers being able to market all of their crop) will become a focus of producers.
- Some producers will seek to partner with those further up the chain either in processing and / or marketing enterprises. The success will depend on the level of business management skills of the producer.
- More successful growers will have closer relationships with wholesalers, processors or retailers and will seek to exchange greater levels of production, supply and marketing information to the benefit of all.
- Increasingly growers or grower consolidators will become part of closed chains, involving input providers right up to processors and retailers.
- Varieties subject to plant variety rights or trademarks will become integral to closed chains.
- The average level of business skilling of the producers will rise, particularly in terms of business management, financial recording, data collection, communication and market investigation / development strategies.
- Producers will be expected to be leaders in innovation, rather than followers particularly in terms of gaining access to new varieties, development of innovative marketing concepts and strategies.
- Producers will increasingly be required to undertake activities that were considered the preserve of others in the chain e.g. supply and logistics management.
- Successful growers will be those who can identify points of differentiation or innovation from their ability to collect, analyse and action information either provided by others or sourced directly.
- Producers will be faced with increasing levels of compliance either from within the chain or those external to the chain i.e. Governments.
- Water access, impacts by others on producers farming practices, government legislation and access and management of labour will be the critical on-farm issues that will impact on farmers beyond value chain issues.
- Producers will need to continually seek to identify cost efficiencies that can be gained inside the farm gate, so as to be able to be more cost effective over time. Further it will be expected that they work with others in the chain to identify and achieve cost efficiencies outside the farm gate.
- Producers will be forced over time to increase with a wide range of imported fruit and vegetable products.
- Unless major structural and cultural changes occur in the horticultural export value chain, Queensland will have a mixed future in terms of export finance.

### ***1.6 Key Issues for the Horticultural Production Sector***

The skills set possessed by different members of the growing sector are different. Further, the skills and abilities that will be required by different businesses involved in production in future will be different and more sophisticated.

This study has highlighted 8 key issue areas requiring the development of services, provision of information, development of systems and mentoring and policy areas that will improve the value chain capability of the production end of the value chain.

Issue Areas	Key Issues
Entrepreneurship & Industry Leadership	<ul style="list-style-type: none"> <li>▪ Industry has a lack of commercial leaders who have the requisite skills to be relevant to upstream chain members, as value chains develop over time.</li> <li>▪ Exposure of industry leaders to best practice examples in business entrepreneurship, both inside and outside the sector.</li> <li>▪ Development of an industry culture that supports leaders and entrepreneurship as the mechanism that will drive overall industry benefit.</li> </ul>
Information Provision	<ul style="list-style-type: none"> <li>▪ Develop collection mechanisms for information pertaining to production costs and returns.</li> <li>▪ Provide access to wholesale market volumes and prices for all commodities in an easy to access mechanism and at low cost.</li> <li>▪ Develop greater knowledge and then dissemination of information on whole of chain costs and returns – (develop the tools to dispel the myths).</li> <li>▪ Provision of information on value adding, innovation initiatives and trends (consumer and retail) further up the chain.</li> <li>▪ Development and circulation of case studies (domestic and international) of successful new business initiatives and development.</li> <li>▪ Advice provision on standard business issues and developments i.e. BAS, ATO, WPH&amp;S.</li> <li>▪ Promotion of chain awareness i.e. New developments in chains, how they may impact on the production sector.</li> <li>▪ Have knowledge of and access to information providers and contacts that industry may require over time.</li> <li>▪ Gain access to and provide information concerning consumer preferences and desires, how they 'think' and what they will require in the future.</li> </ul>
Marketing and Business skills	<ul style="list-style-type: none"> <li>▪ Access, develop and disseminate knowledge of new markets / opportunities.</li> <li>▪ Identify and facilitate skills delivery systems in developing both domestic and international business relations.</li> <li>▪ Communication of best practice standards in business management from horticulture and sectors outside of it.</li> <li>▪ Training in business negotiation and general communication.</li> <li>▪ Facilitate a general awareness of standard business operational procedures with others further up and down the chain.</li> </ul>
Development of linkages & synergies	<ul style="list-style-type: none"> <li>▪ Provide or facilitate services that develop the ability to identify good fit strategic partners (vertical alliances) and implement business development strategies.</li> <li>▪ Provide or facilitate services that develop the ability to identify good fit strategic partners (horizontal alliances) and implement business development strategies for same.</li> <li>▪ Provide linkages to service providers who identify new business opportunities for production sector and others in the chain.</li> <li>▪ Promotion of initiatives that foster the development of knowledge of the chain beyond the farm gate i.e. Meet the wholesaler, retailer, exporter, logistics.</li> <li>▪ Development of an improved and more co-operative culture between different sectors in the chain.</li> </ul>

Issue Areas	Key Issues
Financial skills	<ul style="list-style-type: none"> <li>▪ Development of benchmarking systems – production and whole of chain focused pertaining to costs and returns.</li> <li>▪ Development of a base financial reporting standards / mechanism.</li> <li>▪ Assist growers to develop skills to make informed financial investment decisions, on farm and off-farm.</li> <li>▪ Communicate information on investment strategies and options. Also have the ability to refer to sound investment partners.</li> <li>▪ Communicate information on changes to laws / regulations that will impact financial management of individual farms.</li> </ul>
Business mentoring, coaching and support	<ul style="list-style-type: none"> <li>▪ Provide professional assistance so as to allow businesses to have analytical and strategic analyses of their business – business diagnostics</li> <li>▪ Provide access to qualified succession planning services</li> <li>▪ Assist with the formation of linkages with existing service providers.</li> </ul>
Systems development	<ul style="list-style-type: none"> <li>▪ Develop standard terms and conditions contracts for producers dealing with other elements in the chain.</li> <li>▪ Develop a pro-forma set of communication documents across the chain (focus on increasing returns transparency).</li> <li>▪ Develop and communicate information on standard business communication systems.</li> </ul>
Agri-policy	<ul style="list-style-type: none"> <li>▪ Maintenance and gaining increasing power in the chain for the production industry.</li> <li>▪ Provide assistance to the production community pertaining to market access issues (both export and import).</li> <li>▪ Prevention / lobbying on unfair trading practices within the chain.</li> <li>▪ Promote standard terms of business / trade developed in consultation with the chain to the production sector and others.</li> <li>▪ Promote development of enforceable business systems across industry (if appropriate).</li> <li>▪ Promotion to other sectors of the value chain beyond the farm gate of production sector issues / concerns.</li> <li>▪ Assist with / involve itself in government policy and initiatives for producers who wish to exit industry.</li> <li>▪ Lobbying with government to lower the costs of transacting and compliance.</li> <li>▪ Strategy and policy formulation to develop internationally competitive value chains i.e. Reduction of costs of transacting international business, addressing industry concerns of imports only along quarantine or phytosanitary lines.</li> </ul>

### **1.7 Horticultural Enterprise Re-Engineering Operation**

Horticulture is a diverse industry with a wide range of large and small growers, with a wide variety of business skills. Further their connection to and knowledge of the value chain beyond the farm gate is varied across the sector and is not necessarily dependant on business size.

As a result of the research conducted in this report and as discussed in Section 1.6 the breadth of issues that the industry needs to address in order to become more 'value chain competent' is vast. The challenge facing industry organisations is how to take these issues

and develop services and programs that can be delivered to their members or industry in a manner desired by the producers in a cost effective manner. This report recommends the implementation of a three tier system of service provision by Growcom.

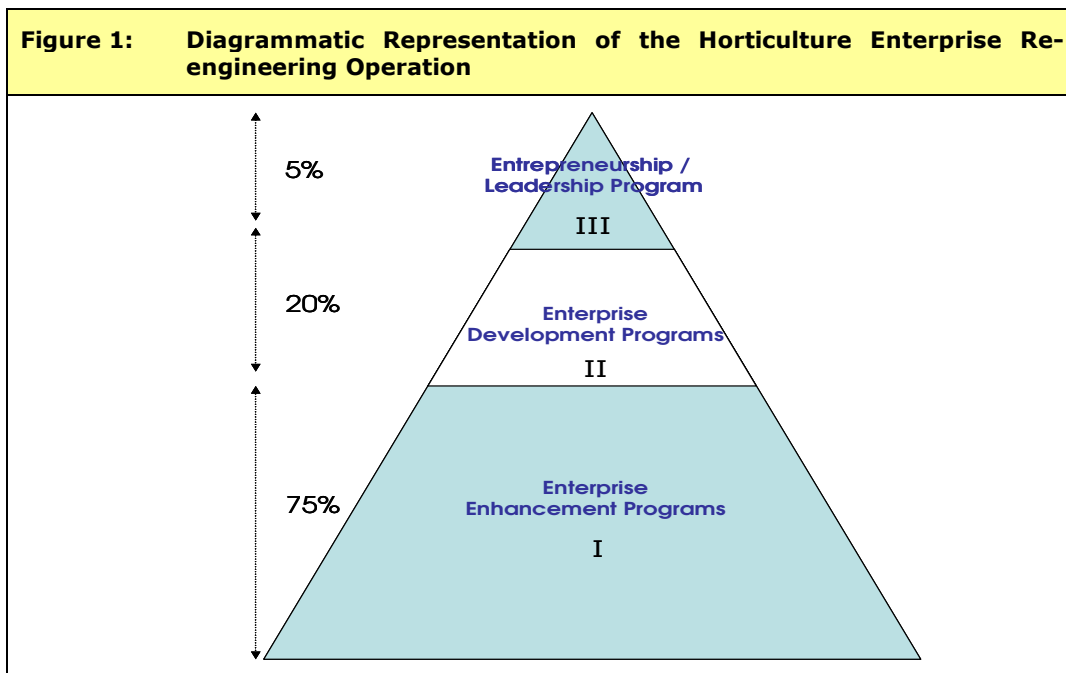
The HERO program will focus on delivering a range of services, strategies and programs that will assist those 'industry leaders' develop a higher and greater level of entrepreneurship and leadership skills in this sector. The broad range of business development and maintenance services that should be made available to the rest of industry, are in general already possessed by the top 5 per cent of industry.

In short, HERO will seek to provide commercially relevant services and programs to all 'levels' of the production sector.

These tiers will correspond to the level of skill sets that are possessed or required by different producers.

1. **Tier I** – are a combination of strategies and programs that focus on delivering to producers improved profitability / viability for their businesses. Customers of Tier 1 programs may be expected to be satisfied with their current role in industry but wish to develop knowledge or gain access to information that allows them to be more sustainable. The focus to Tier 1 programs will generally be on smaller business operations who may not previously have had access to these strategies and programs, for whatever reason.
2. **Tier II** – are a combination of strategies and programs that seek to build the capability to have larger and more profitable businesses. These businesses may wish to develop a different role or position within the sector that they operate in. In many instances they may be part of collectives or closed or semi-closed marketing systems.
3. **Tier III** – are strategies and programs that seek to foster the entrepreneurship or leadership of those firms and individuals who for reasons of their position in the value chain or position within industry are seen by others to be 'leaders' either in commerce and / or in industry leadership roles.

Diagrammatically the HERO program may be represented as follows:





## **TIER I SERVICE DELIVERY**

Tier I service delivery could be achieved by the development of a similarly focused delivery tool to that of Growcom's 'People Pak'. We have provisionally called this service delivery program 'Enterprise Pak'. Some suggested elements that may make up Enterprise Pak are:

- Standard terms and contracts for growers dealing with other elements of the chain.
- Suggestions / hints of how growers can improve communication with customers / other service providers.
- Development of a pro-forma set of communication documents suitable for the rest of the chain.
- Access to pricing and supply information, e.g. Market Information Services information.
- Regular updates / reminders regarding major government compliance events, e.g. BAS, Provisional tax, superannuation.
- General advice on standard business issues and developments.
- Facilitation of a general awareness of standard business operational procedures with other further up and down the chain.
- Information on access to business management / advice practitioners for taxation, accounting, business and succession planning.
- Provision of industry frameworks for recording of gross returns, costs and margins for subsequent financial analysis.
- Development and circulation of case studies (domestic and international) of successful new business initiatives and development.
- Circulation of other relevant information as identified by the delivery team and from communication with growers.
- Hotline or service line for growers to gain access to information, e.g. Terms of Trade, potentially industry accredited wholesalers, sources of information available to growers to seek remedy to marketing issues etc.

Significant elements / components of the Tier I services are already available through a variety of service providers, in-house information already held and government agencies. The missing element is the bundling of these services in a fashion to provide a 'first stop shop' for information provision. The HERO merely is the collective mechanism for the bundling of these services.

## **TIER II SERVICE DELIVERY**

Tier II service delivery focuses on providing a bundle of services that build the capability of individual enterprises to develop new and expanded business opportunities. Specific services that could or may be provided, but not limited to include:

- Development of whole of chain costs and returns models for industry for use in the development of benchmarking systems between individual enterprises and industry performance standards.
- Development of a methodology accessing information on value adding, innovation and new trend initiatives both within Australia and overseas and disseminating this to Tier II 'subscribers'. Development of case studies on innovative business activities both within and outside the farm gate would also form part of this service.

- Development of databases of quality service providers who can assist individuals and collectives of same, identify and develop sustainable relationships with 'good fit' strategic partners either in the production sector or across the chain.
- Promotion of initiatives that foster the development of knowledge of the chain beyond the farm gate.
- Development of a business facilitation / linkage service whereby organisations which identify and foster new business and trade opportunities may be directed to qualified growing enterprises. Conversely, growers would be able to gain access to networks / contacts / services who wish to develop new business opportunities.

Developing in-house expertise in these areas is not warranted at least initially as there is a need to 'test' the market place for the willingness of the production sector to pay for such services.

Similarly to Tier I delivery, the elements that may make up Tier II service delivery may or may not exist elsewhere in the market place. Organisations should not attempt to duplicate services and information that may be already available but rather facilitate their bundling in a way that is easily accessible to the production sector.

### **TIER III SERVICE DELIVERY**

It is individual enterprise development that drives industries forward. Supporting commercial and industry leaders assists a 'pull' mentality in terms of development rather than the traditional 'push' mentality where all in a sector must be seen to be pushed at the same rate.

There currently exists a range of programs that seek to foster and develop the leadership and entrepreneurship skills of industry leaders / formers. Examples of these include the Queensland Enterprise Workshop, National Enterprise Workshop, a variety of programs run by Archaeus, Blue Storm, the Australian Rural Leaders Program and the Monash University Produce Executive Program (supported by HAL).

Each of these programs seek to develop within participants a range of professional and personal leadership skills development, that will benefit their own individual business and the industry in which they operate. Importantly, these programs will develop a culture within the individual that is more forward thinking, seeking of innovation and new ways of doing business and development of a more global outlook. It is these leaders who will ultimately drive the commercial success of the industry (as they are the leaders in the growth elements of the industry). Over time, these entrepreneurs are also encouraged to develop industry leadership roles in peak or representative organisations.

It is recommended that horticulture industry organisations should seek to interact / negotiate with a selected group of these leadership / entrepreneurship program developers so as to develop a program directly relevant to horticulture. We have conditionally called this, "**The Australian Horticultural Leadership Program**".

### **AGRI-POLICY IMPLEMENTATION**

The issues discussed in Section 1.6 pertaining to 'Agri-Policy' indicate the broad range of services that are required, some of which provide whole of industry benefit and others that benefit only a small section of the producer community eg. commodity specific issues such as Import Risk Analyses.

In a number of instances the role of 'Agri-Policy' cuts across each of the services tiers that would be provided under HERO.

It must be stressed that industry regards many of the Agri-Policy services critical to successful business and industry development.

It is therefore recommended that whilst the HERO program may be regarded as an independently funded program (or suite of programs) careful financial and structural consideration should be provided to how growers and producers can best receive Agri-Policy services.

In Queensland, Growcom's Agri-Political Unit (APU) undertakes a number of the functions discussed in Section 1.6. These should continue and further be enhanced so that adequate resources are available to perform the additional functions that are required. In states other than Queensland, which generally do not have strong whole of industry representative organisations, careful consideration should occur in how a unit such as Growcom's APU is established. This consideration should extend to how the various industry organisations and their 'APU-type' services should be integrated.

### **KEY ISSUES FOR SUCCESSFUL IMPLEMENTATION OF HERO**

The key issues that this report has identified which may impact on the successful implementation of HERO include:

1. Access to and provision of adequate financial resources over a period long enough to prove the relevance of such a program.
2. Development of an appropriate marketing strategy for the program that ensures the attainment of 'sales' goals for the program.
3. Grower apathy and overcoming perception of irrelevance by production sector of the program.
4. Gaining support from other value chain members.
5. Gaining support from other service providers.
6. The ability to integrate the program into industry organisations' internal operations.

### **1.8 Next Steps**

In order to 'test' the principal recommendation of this report, that is the formation of the Horticultural Enterprise Re-Engineering Operation, and the various elements that constitute it, including Agri-Policy service provision the report needs to be supported by HAL and Growcom.

If this occurs, it is proposed the next steps should be:

1. Development of an Implementation Strategy for the program, including identification of the major elements of the program, potential support and information services, potential service deliverers, funding sources and role of the various government and industry support agencies.
2. Development of an interim operational model for the delivery of HERO and Agri-Policy service provision.
3. Consultation with industry to discuss the various elements of HERO and preferred service delivery methods.
4. Adjustments based on industry consultation feedback to the Operational Model for HERO and Agri-Policy service provision.
5. Resourcing of HERO and Agri-Policy service provision
6. Implementation of HERO and Agri-Policy service provision.

It is strongly recommended that as the principal state horticultural industry representative organisation, Growcom should be the lead 'agent' responsible for the implementation of the recommendations of this report. Further, Growcom is best positioned and has the greatest level of knowledge about Queensland's industry participants. In addition it already has in existence a resource structure, through its regional offices to be the most effective mechanism to assist with the implementation of HERO.

However, there are numerous organisations which can add considerable value to the implementation of HERO, either through resource or service provision or funding. These organisations include Queensland Department of Primary Industries & Fisheries, Queensland Department of State Development and Innovation, FarmBis and the Department of Agriculture, Forestry and Fisheries. These organisations at a minimum should be consulted as part of Step 3, discussed above.

The suggested timeframe for implementation of HERO would be 9 to 12 months, with an initial focus on service delivery to be Queensland centric.

## 2.0 KEY DRIVERS IN THE INTERNATIONAL FOOD INDUSTRY

### 2.1 Consumer Trends - Drivers of Change in Asia

A number of key global consumer trends—particularly those related to the Asian agrifood industry—have been identified as drivers of change in food distribution systems and new product development. These include:

**Economic growth and per capita income growth:** As identified by DFAT (2002), economic growth and rising incomes in Asia have fuelled demand for food, particularly in low income groups. Arising from this, per capita food demand growth is consumer interest in better quality and food safety.

**Urbanisation:** The shift of populations in the Asian region in recent decades to urban centres offering higher wages and increased employment opportunities has been pronounced. Although the levels of urbanisation vary considerably between countries, the net effect has been a growth in disposable incomes which has translated into increased demand for food, and of better quality and greater variety. In turn, this demand has given rise to the development of modern food retailing and food service formats in larger cities.

**Population Growth:** By 2010, Asia's population will have increased to 3.8 billion, representing 56 per cent of the total world population of 6.8 billion (Laffan, 2004)

**Convenience:** Time-starved consumers worldwide continue to demand food in convenient formats as the norm rather than as added benefits, thus allowing them to spend less time preparing meals. This trend has driven growth in prepared meals and food service outlets in larger urban centres. The convenience factor also equates to a demand for increased functionality of foods and an ability for products to meet the nutritional needs of consumers.

**Health & Nutrition:** A significant proportion of consumers are becoming increasingly committed towards improved health through improved nutrition. This has not necessarily been reflected in the consumption of cooked at home meals, but rather through an increasing variety of prepared meals and whole meal preparations. For example, McDonalds in addition to their traditional menu are offering a wider range of healthy meal alternatives. Major retailers are moving increasingly into prepared meals. Further, the emergence of juice and salad bars are providing healthy meals that are also convenient.

Further, exercise in combination with health is currently viewed as 'trendy'. Gym and health clubs currently have record memberships.

In particular, improved health through exercise and nutrition is being driven by a significant segment of the 15-30's market and the female gender in their +40's.

**Westernisation of Asian food markets:** Consumer exposure to western cultural and commercial influences have permeated the Asian food industry. Western retail and foodservice formats and food products continue to be replicated throughout the region.

**Ethnic Foods:** In the 21<sup>st</sup> Century consumers will leave no stone unturned in their quest to discover new and exciting tastes from around the world. With global travel within the reach of more and more consumers, increased mobility in the workforce, and the advent of communication technologies such as the Internet, growth in the consumption of ethnic foods both in Australia and abroad is on the rise.

**Mass Customisation:** Consumers are increasingly demanding variety, different packaging and eating formats. They are not concerned that the food they want is different to the majority of the population. Mass customisation refers to how companies are having to be agile enough to respond to the growing variety of consumer preferences whilst at the same time maintaining business profitability.

**Improved Chain Awareness:** Consumers increasingly are wishing to gain a greater understanding of 'where' their food comes from. This in part due to their health and food safety concerns. It is also due to a desire to become more empathetic or 'in touch' with farmers because it provides a 'feel good feeling to them'. In Australia, this desire has been reflected in the enormous growth of 'farmers markets' in major metropolitan and urban centres.

## 2.2 Globalisation in Retailing

### FOOD RETAILING

In recent years there has been a drive by a select group of European and United States retailers to establish global retailing operations. Driven by consolidation of food retailing in Europe and the United States, their goal is to retail an ever-larger share of the world's consumer food purchases.

Global supermarkets offer the promise of better prices, based on their economies of scale. As a result, global supermarkets are an increasing part of today's globalisation of our food supply. The top 10 global retailers now operate in at least seven and as many as 28 countries. Whilst still at an early stage — only one-third of the leading retailers have any presence outside of Europe and the United States — this trend to developing off-shore footprints is set to continue with the European majors including Royal Ahold (Netherlands), Carrefour (France), Metro (Germany), and Makro (Netherlands) all moving to Asian markets.

A range of key store formats has accompanied the process of consolidation, with mass low-cost retailers seeing the biggest growth in the region. These include hypermarkets and discount warehouses such as Makro and Costco. Specialty food retailers including premium supermarkets and specialty department store food sections have also grown steadily, however traditional supermarkets are suffering significant loss of market share. The growth in hypermarkets and discount warehouses is resulting in increasingly more efficient supply chains focussing on driving costs out of the chain. This has and will continue to impact on the ways that suppliers, including those in Australia, do business with these global retailers.

In order to demonstrate the scale, spread and size of these international global retailers IGD compiled a global retailing index in 2002. The results are detailed below in Table 1.

Table 1: IGD Global Retailing Index 2002					
Rank	Country of Origin	Name of Company	Store Formats	2002 Group Sales (US\$ mil)	Countries of Operation
1	France	Carrefour	Cash & Carry, Convenience, Discount, Hypermarket, Specialty, Supermarket	65,011	Argentina, Belgium, Brazil, Chile, China, Columbia, Czech Rep., Dominican Rep., Egypt, France, Greece, Indonesia, Italy, Japan, Malaysia, Mexico, Oman, Poland, Portugal, Qatar, Romania, Singapore, Slovakia, Spain, S.Korea, Switzerland, Taiwan, Thailand, Tunisia, Turkey, UAE.
2	Netherlands	Ahold	Cash & Carry, Convenience, Discount, Drug, Hypermarket, Specialty, Supermarket	33,837	Argentina, Brazil, Chile, Cost Rica, Czech Rep., Denmark, Ecuador, El Salvador, Estonia, Guatemala, Honduras, Indonesia, Latvia, Lithuania, Malaysia, Netherlands, Nicaragua, Norway, Paraguay, Peru, Poland, Slovakia, Spain, Sweden, Thailand, United States
3	United States	Wal-Mart	Discount, Hypermarket, Supermarket,	229,617	Argentina, Brazil, Canada, China, Germany, Japan, South Korea, Mexico,

Table 1: IGD Global Retailing Index 2002					
			Superstore, Warehouse		Puerto Rico, UK, United States
4	Germany	Metro	Cash & Carry, Department, DIY, Hypermarket, Specialty, Superstore	48,349	Austria, Belgium, Bulgaria, China, Croatia, Czech Rep., Denmark, France, Germany, Greece, Hungary, Italy, Japan, Luxembourg, Morocco, Netherlands, Poland, Portugal, Romania, Russia, Slovakia, Spain, Switzerland, Turkey, UK, Vietnam.
5	UK	Tesco	Convenience, Department, Hypermarket, Supermarket, Superstore	40,071	Czech Rep., Hungary, Rep. of Ireland, Malaysia, Poland, S.Korea, Slovakia, Taiwan, Thailand, UK
6	Japan	Ito Yokado (incl. 7-Eleven)	Convenience, Department, Food Service, Specialty, Supermarket, Superstore	26,179	Australia, China, Denmark, Guam, Japan, Malaysia, Mexico, Norway, Philippines, Puerto Rico, Singapore, S.Korea, Spain, Sweden, Taiwan, Thailand, Turkey, US
7	France	Casino	Cash & Carry, Convenience, Department, Discount, Food Service, Hypermarket, Specialty, Supermarket, Warehouse	21,620	Argentina, Bahrain, Belgium, Brazil, Colombia, Comoros, France, Lebanon, Madagascar, Mauritius, Mexico, Netherlands, Poland, Reunion, Taiwan, Thailand, Tunisia, Uruguay, US, Venezuela, Vietnam
8	France	Auchan	Department, Hypermarket, Specialty, Supermarket	26,071	Angola, Argentina, China, France, Hungary, Italy, Luxembourg, Mexico, Morocco, Poland, Portugal, Russia, Spain, Taiwan, US
9	Germany	Aldi Einkauf	Discount, Supermarket	33,837	Australia, Austria, Belgium, Denmark, France, Germany, Luxembourg, Netherlands, Rep. of Ireland, Spain, UK, US
10	United States	Costco	Warehouse	37,993	Canada, Japan, S.Korea, Mexico, Puerto Rico, Taiwan, UK, US

Source: Agribusiness Association of Australia (2003); Stores (2004)

The success in Asia of global food retailers has been mixed. This has occurred because of global retailers' apparent lack of understanding of Asian customers. Where there has been success, it is generally in partnership with local partners who have a better understanding of the 'culture' of the community.

In Australia, the first of the global food retailers Aldi, has undertaken an aggressive expansion and pricing policy with its arrival in the last three years. Initially focussing on New South Wales, the company has now expanded operations to Victoria and Queensland. The normally secretive company has made it known that it intends to become a major player in Australia, through aggressive price competition and consumer 'friendly' formats.

### GLOBAL SUPPLY CHAINS

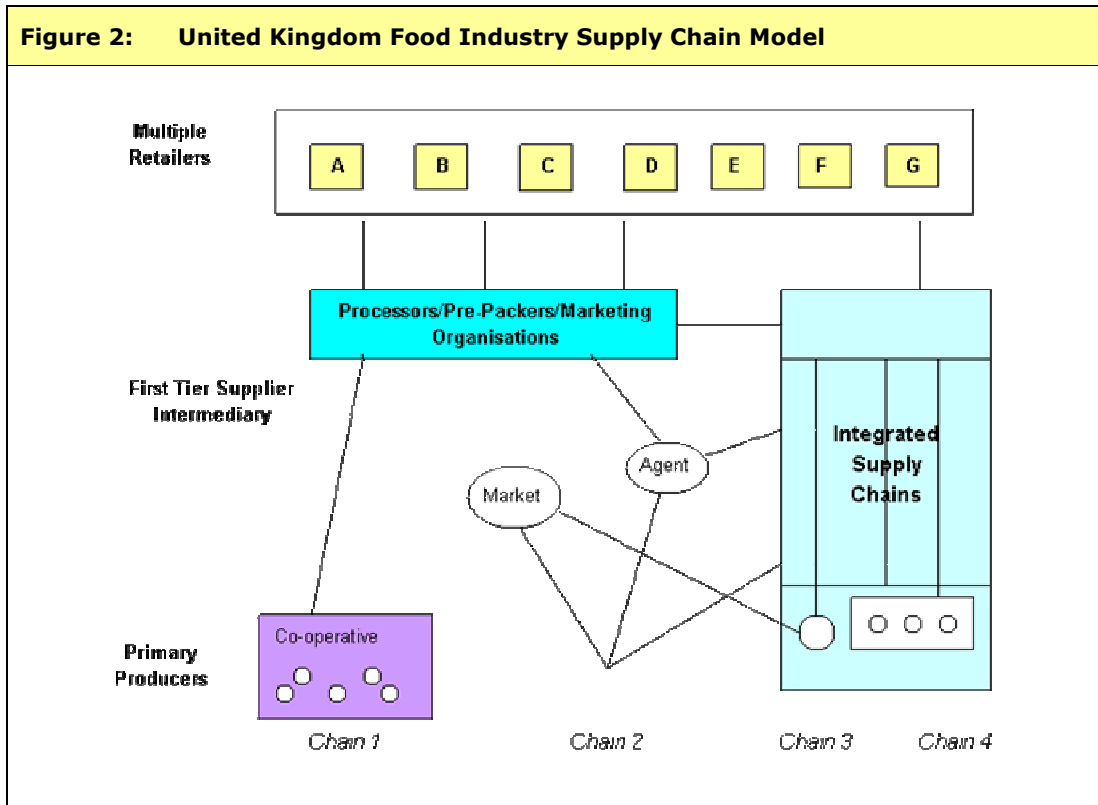
The Department of Foreign Affairs and Trade (2002) noted that globalisation of food retailing is bringing about historic change in the agrifood supply chain. Among the significant effects are:

- a massive increase in purchasing power of the global retailers;
- a marked reduction in the number of suppliers used by fewer, larger global chains;
- increasing aggregation of many of the first and second tier global retailers;

- a movement by retailers from less local sourcing towards more regional and global sourcing;
- increasing utilisation of house brands / private labels by the retailers; and,
- a significant shift in the weight of agrifood industry power away from the agrifood processors towards the food and beverage retailers.

In the United Kingdom, fresh food major supermarkets have driven supplier rationalisation amongst the food sector. Suppliers are typically large pre-packers or processors that are geared to the needs of the supermarkets. These pre-packers and processors are the key link between farmers and supermarkets and are increasingly taking responsibility for supplying, liaising with farmers and building global networks for year round supply. By assuming this category management role, these suppliers are being rewarded by volume growth (Imperial College London, 2004).

The supply chain, from the perspective of the United Kingdom food industry, is diagrammatically represented below in Figure 2.



Source: Imperial College 2004

The four chains represented from left to right show a transition from non-integrated to a fully integrated supply chain, with the last being where a processor / pre-packer may in fact only be 'permitted' to deal with one retailer.

Paradoxically, as the number of pre-packers and processors who deal with the major chains reduce, their ability to negotiate longer, more profitable supply contracts is increased. This occurs because with the sharing of information, particularly scan data and other proprietary information, retailers are increasingly being locked into these suppliers due to the fact that they know so much of the retailers business. Therefore each party, retailer and pre-packer or processor are equally 'dependant' on one another to do business. This dependency of interrelationships is now referred to as the Paradox of Power.



## GLOBAL SOURCING OF PRODUCE

Within Asia we see a transformation of the traditional pattern of agricultural and food production and distribution from one of predominately subsistence agriculture into a rapidly modernising system of agribusiness and agrifood processing and distribution. Asia has and will continue to be a major competitor in international markets at least initially in commodity food production, but increasingly over time in high value food products. Asia, generally regarded as a lower cost producer than Australia (and in many instances Europe and United States) in food products, will increasingly seek to gain market share from existing suppliers, including those in Australia.

A number of global retail chains have invested heavily in production systems, predominately in China, India and Thailand where through lower labour and production costs, they are able to provide a cost advantage over retailers whose production bases remain in Europe or the United States. Companies such as Syngenta have also invested in these countries as they seek through their genetic improvement programs to become global suppliers to global retailers.

Where global retailers have not invested in production systems, they have in the main handed over the responsibility to others in the supply chain. The concept of category management, as it applies to fresh produce, involves non-retailer parties to, at a minimum, be responsible for the consolidation and logistical movement of produce to designated receival points. Companies such as Enza, Capespan, Chiquita, Fyffes and Noboa have been given the responsibility to develop tailored supply programs no matter where the product is in the world. Discussions with Noel Shields (2004: pers. comm.) (former head of produce of Dairy Farm International)—himself now a global procurement manager — states that Australia's participation in these global supply systems is limited at best. The principal reasons for this are our lack of global focus, marketing skills development, scale of operations and in some instances the quality of our product.

Hussey (2000) at an AFFA conference, commented that in the European market for fresh fruit and vegetables Australia is being outperformed by southern hemisphere competitors. He stated that if Australian suppliers failed to establish competitive chain relationships in Europe then they will be competitively disadvantaged in the growth markets of Asia as European global retailers establish their footprints in this market.

The short-term implications of this trend for Australian exporters of fresh produce are that they need to be aware of the trend to outsourcing and either link up with contract operators, (who are no longer the supermarkets), or be prepared to form or join alliances that can guarantee supermarket requirements on a year-round basis.

## GLOBALISATION OF PROCESSED FOOD

Federal government research has shown that the international trade in processed food has increased rapidly, while trade in bulk commodities has declined. In 1985, trade in further processed food production accounted for 50 per cent of global agricultural trade. Today it accounts for 75 per cent of that trade and is growing at a rate twice that of primary products (AWIA, 2001).

Consolidation is not just occurring at the retail end of food and beverage industries, but also amongst agrifood processors. Large scale mergers and acquisitions are driving a trend towards having increasingly larger multinational corporations (MNC's). Recent examples include Kraft's purchase of Nabisco, General Mills purchase of Pillsbury, and Unilevers' acquisition of Bestfoods.

Industry sources suggest that as further consolidation occurs in individual agrifood categories, two or three leading global players are likely to emerge dominant within each category. This is already starting to occur, where United States' Lamb Weston division of ConAgra and JR Simplot Co, plus Canada's McCain Food are the leading global players in frozen French fries. The dairy industry, as can be seen even in Australia, is seeing the emergence of Fonterra and Parmalat as global players.

These global agrifood MNC's as a key strategy, are seeking to rationalise the location of their production facilities, their distribution systems and the sourcing of raw materials and finished products. These strategies are resulting in location of production facilities close to the major growth markets for their company's products, and so are presenting opportunities to those growth regions to develop new strategic linkages with MNC's.

Additionally, in 2001, there were an average 24,000 packaged food items on Australian shelves, 75 per cent of which had been introduced in the previous five years, thus reflecting the increasing sophistication of consumers.

### **GLOBALISATION OF THE FOOD SERVICE INDUSTRY**

Time-starved consumers have increasingly turned away from grocery aisles to eat-out, particularly at fast food outlets and family restaurants. Food-away-from-home now accounts for around 50 per cent of total food expenditure in the United States. That trend has been mirrored in Asia, Europe and Australia. The growth of multi-national chains, McDonald's, KFC and Pizza Hut, among others, throughout Asian markets has seen the development of new food supply opportunities for agribusinesses through centralised buying operations of these companies (Pinnacle Management, 2002).

The growing pattern of organised food service is characterised by chains of outlets using a uniform brand identity, centralised procurement of supplies, strong focus on quality, a major emphasis on cost competitive and efficient supply chains, standardisation and safety from suppliers, uniformity in product menus across outlets, uniform taste, existence of strong controls, and the use of technology. Saturation of European and North American food service markets has driven United States fast food chains in particular to focus particularly on Asia in their global expansion strategies. This has been accompanied by growth in new food service formats, particularly café chains including Starbuck's (United States) and Lavazza (Italy).

Interestingly, in response to the growth in food-away-from-home consumption and spending, food retailers have begun to blur the lines between grocery and food service by increasingly incorporating ready-to-eat and fast food programs into their store formats. In turn, this is creating new categories and emerging opportunities within traditional retailer store formats.

### **KEYPOINTS**

#### **KEYPOINTS**

- Asian consumers are becoming increasingly Westernised in their choice of food products, demand for increased convenience, choice, quality and food safety.
- The emergence of global retailers has re-engineered the way that business is done back along the value chain in the provision of food products.
- Global retailers are increasingly seeking to develop global value chains, where those participants who are able to align their business principles and capabilities are rewarded with access to the global retailer.
- Australia is generally regarded as being a 'bit' player in regards participation in global food chains.
- Globalisation of processed food and food service whilst presenting enormous market potential as each segment grows at a faster rate than the minimally processing sector is increasingly presenting barriers to entry for Australian producers as their skills, focus and scale do not 'match up' with the requirements of these players.

### 3.0 REVIEW OF THE AUSTRALIAN HORTICULTURAL SECTOR

#### 3.1 Overview of the Australian Horticultural Industry

Horticulture is the fastest growing industry in agriculture in Australia with 17,273 enterprises. A \$6.4 billion industry, horticulture is extremely diverse and comprises fruit, vegetables, nuts, nursery, extractive crops, cut flowers and turf. In F2002 the contribution by grouping to national gross domestic produce were (HAL, 2004):

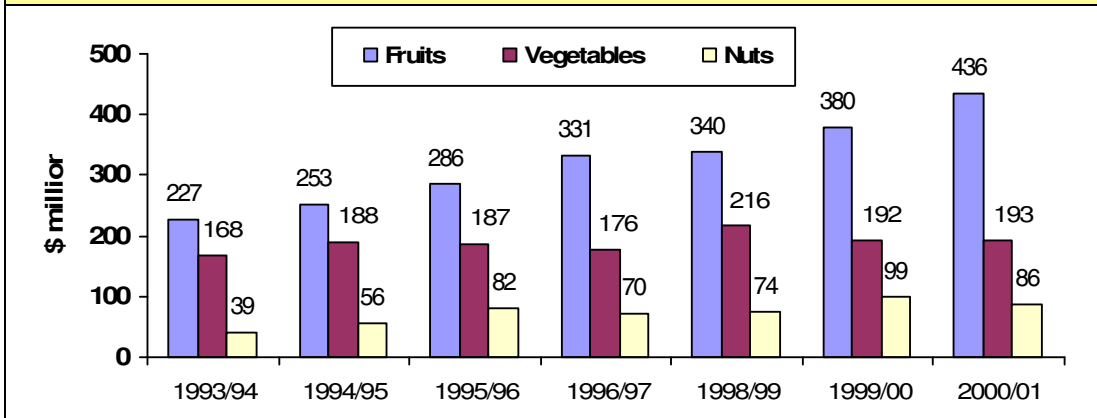
Fruit and Nuts (excluding wine grapes)	\$2.4 billion
Vegetables	\$2.3 billion
Cut Flowers	\$0.9 billion
Nursery Products	\$0.8 billion

Horticultural industries contribute significantly to the economies of regional centres across Australia. Some 55,000 persons are employed in growing fruit, vegetables and nuts to supply the domestic and export markets. A further 9,800 are employed in fruit and vegetable processing (not including wine manufacturing). Employment of 64,000 people translates to 20 per cent of total employment in agriculture being within horticulture.

Horticulture is a diverse industry producing a very wide range of crops. Estimates suggest that in Australia there is upwards of 180 horticultural crops currently in production and growing seemingly daily. The diversity of the sector, the wide variety of different customer segments and the lack of accurate information collection mechanisms, make estimating the contribution of horticulture to the economy of Australia very difficult.

The figure below demonstrates the majority of production value growth in horticulture has come from fruit industries, which has shown a steady upward trend since F1994 with the net value increasing by 92.1 per cent in that period. In contrast, vegetable value of production has been up and down with overall growth in the same period being 14.9 per cent. Nut production, particularly macadamias and almonds, have shown rapid overall growth. Since F1994 the value of nut production has increased by 120.5 per cent.

**Figure 3: Value of Australian Horticultural Production of Fruit, Vegetables and Nuts -1993 to 2001**



#### 3.2 Consumption of Horticultural Produce

Recorded per capita consumption of fruit and fruit products has increased by 56.1 per cent since the late 1960's when compared with F1999. In F1999 fruit consumption was estimated at 135.0 kilograms per capita.

Vegetable consumption has showed a slower but steadily upward trend since the late 1950's. In F1999 the apparent per capita consumption of vegetables was 162.0 kilograms, up 45.0 kilograms since the previous period (ABS, 2004).

Anecdotal evidence suggests that the growth in fruit and vegetable consumption has largely been in non-fresh products, with a much smaller growth in fresh fruit and vegetables.

### 3.3 Australian Exports

Total horticultural exports in F2003 were valued at \$849 million (inclusive of fruit, vegetables, nuts and flowers) or 13.3 per cent of the total, with considerable variation between crops. Australian export performance as a percentage of the total value of production has been relatively static up until F2002. Movements in demand are largely reflective of exchange rate movements and externalities, such as those caused by SARS and political disturbances. Since that period the value of horticultural exports has in fact declined with a former head of the Australian Horticultural Exporters Association suggesting the figure for F2005 may be as low as \$350 million.

In F2003, the Australian Bureau of Statistics estimated that the value of value-added horticultural exports in excess of commodity of exports was \$560 million.

On a state-by-state basis, export performance is variable with Western Australia and Tasmania the principal exporting regions as a percentage of production. By dollar value however Queensland, Victoria and South Australia are the principle exporting states. (Pinnacle Management, 2003).

As demonstrated in Table 2, oranges, grapes and mandarins are the principal fruit products exported, carrots and asparagus the principal vegetables and both macadamias and cut flowers / nursery (as a group) also significant contributors to export income.

<b>Table 2: Value of Australian Horticultural Exports by Commodity, F2000-2003 (\$A millions)</b>				
<b>Commodity</b>	<b>F2000</b>	<b>F2001</b>	<b>F2002</b>	<b>F2003</b>
Oranges	123	150	153	146
Grapes	74	72	136	96
Macadamias (shelled and in shell)	78	78	110	88
Carrots	36	40	49	48
Cut flowers / nursery	34	36	44	40
Mandarins	26	37	40	49
Asparagus	46	43	40	34
Apples	36	46	34	41
Cauliflowers	23	30	28	23
Onions	15	19	28	25
Nectarines	16	16	27	23
Plums	16	25	22	26
Pears	20	24	20	23
Melons	16	18	20	17
Broccoli	15	14	15	13
Other	129	135	158	157
<b>TOTAL</b>	<b>703</b>	<b>781</b>	<b>923</b>	<b>849</b>

Source: Australian Horticultural Statistics Handbook 2003

### 3.4 World Trade of Horticultural Produce

Australia and New Zealand are estimated to have only 1 per cent of the world trade in horticultural commodities. The largest exporter (not including inter-country trade of the EU) is the United States, with approximately 11 per cent of world trade. Such is the diversification of fruit trade that strong exporters such as Chile and Brazil still hold less than 2.3 per cent of world trade.

In regards to vegetables, five countries (Netherlands, Spain, Mexico, the United States and China) hold 59 per cent of the value of world trade.

Bananas, oranges / tangerine, apples and grapes, make up 71.4 per cent of the total trade in horticultural products (see Table 3). The major importing countries are all northern hemisphere based with the southern hemisphere suppliers being South Africa and Chile. Australia is not a major exporter of any commodity grouping.

<b>Table 3: World Horticultural Trade Summary by Commodity, 2001</b>				
<b>Fresh Fruit</b>	<b>A\$ (millions)</b>	<b>Participation</b>	<b>Major Importing Countries</b>	<b>Major Exporting Countries</b>
Banana	8,857	30.32%	U.S., Europe, Japan	Ecuador, Colombia, Philippines
Orange/Tangerine	5,286	18.09%	Germany, Netherlands, France, UK	U.S., Spain, Greece, Morocco, S. Africa
Apples	3,714	12.72%	EU, Austria	U.S., France, Italy, Holland, Chile
Grapes	3,000	10.27%	Germany, U.S., France, UK.	Italy, Chile, U.S., Spain, South Africa
Pears	1,322	4.53%	EU, Austria	Italy, Chiles, U.S., Argentina, South Africa
Peaches	1,294	4.43%	Germany, UK, U.S., Canada, Netherlands	EU, U.S. Chile
Lemon	1,066	3.65%	U.S., Germany, Japan, Netherlands	Spain, Turkey, Argentina, Mexico
Grapefruit	1,056	3.61%	Japan, Netherlands, France, Russia	U.S., South Africa, Israel, Cuba
Raisins	1,024	3.51%	European Union, Russia, Canada	U.S., Turkey, Chile, Greece, Australia
Melon	1,004	3.44%	U.S., EU, Japan	Mexico, Honduras, Costa Rica, Spain
Pineapples	643	2.20%	U.S., EU, Japan	Philippines, Belgium, Costa Rica, Cote d'Ivory, Honduras
Mango	447	1.53%	U.S., Netherlands, Hong Kong	Netherlands, India, Philippines, Mexico
Dates	384	1.32%	India, Russia, France, Malaysia	Tunisia, Algeria, Iran, Pakistan, U.S.
Papaya	113	0.39%	U.S., Japan, Canada, Netherlands	Mexico, Brazil, U.S., Jamaica, Belgium
<b>TOTAL</b>	<b>29,211</b>	<b>100.00%</b>		

Source: Unreferenced

#### NEW ZEALAND

Exports in F2003 of fruit, vegetables and nuts from New Zealand were valued at A\$1.34 billion, 57 per cent higher than Australia's exports in the same period. Anecdotal evidence suggests that New Zealand exports are roughly equivalent to that of domestic demand, whereas by comparison in Australia only 13.3 per cent of production is exported.

So why the disparity between Australian and New Zealand exports? Industry suggests a number of reasons:

1. Culture. New Zealand has a small population and in order to achieve export income has had to develop a strong customer focus. Without exports many industries would fail and so their commitment to overseas customers and markets is high.
2. Single Desk: A number of commodities, notably kiwifruit and apples, at least in the early days had a single desk for the marketing of its products. This allowed for significant market-end investment in promotional and logistical activities. For example the New Zealand Kiwifruit Marketing Board in the 90's had in excess of 75 people working in Europe. Australia has never had this level of investment in personnel at the customer end, due primarily to the fractured nature of the export chain.
3. Attitude: New Zealand is acknowledged as having a 'can-do' attitude towards any issues, exporting in particular. Australians are generally regarded as being domestic focussed and not necessarily willing to go the 'extra mile'.
4. Logistics: New Zealand is generally regarded as having a superior logistics and distribution network to Australia. This situation has improved in recent years, particularly with reforms to the waterfront in Australia.

## **SOUTH AFRICA**

South Africa with a population of 45 million is a major competitor in a number of Australia's major export markets. In F2002, the gross value of horticultural production was A\$2.78 billion, approximately half that of Australia. However South Africa maintains a very strong focus on exporting of high quality fruits and to a lesser extent vegetables. For example, over 60 per cent of all that is produced in South Africa is exported. Exports accounted for 73 per cent of all deciduous fruit income, although it only represents 35 per cent of the total volume of product that was produced. By contrast, only 8 per cent of the onions and 6 per cent of the potatoes produced in the country were exported.

## **CHILE**

Chile is fast becoming a powerhouse in international horticulture, particularly in fruit production. With a population of 15.5 million (75 per cent of Australia approximately) the country exported in 1998, \$1.86 billion worth of fruit. Since that period there has been significant growth both in terms of net value of production and exports.

Chile's major export customer is the United States with over \$0.86 billion worth of fruit and vegetable exports in 2000.

There are over 200 fruit exporters in Chile (1998 figures), but the top ten account for seventy per cent of exports. They are Dole (15.6 million boxes), David del Curto (13.2 million), Unifrutti (9.3 million), UTC (8.4 million), Chiquita (4.9 million), Copefruit (4 million), Rio Blanco (3.9 million), Frusan (3.5 million), Zeus (3.5 million) and Aconex (2.3 million). The major of export companies employ teams of qualified agronomists to contract supply and provide field advice for their own and contract crops.

Over 200 exporters exist in Chile ranging from large multinational companies selling all fruit in all markets, to small grower companies exporting only their own production of one species. The exporters are important drivers of innovation in Chile, with new packaging formats, tree/vine ripening and other programmes aimed at improving eating quality, particularly stone fruit. Generally Chile has concentrated on volume and rapid sales with North America and Europe as key export markets. However this strategy is evolving to situations where the focus is more on quality focussed on servicing particular market segments, over a broader geographic range and increasingly in Asia. Chilean exporters are often part of global networks either supplying parent companies or being part of a network of suppliers supplying global retailers (NZFF, 2004; CFBF; 2004).

## KEYPOINTS

### KEYPOINTS

- Australian horticulture is a major agricultural industry with a gross value of production of \$6.4 billion, 17,273 enterprises and over 55,000 people directly employed within the industry.
- Australia's consumption of fruit and vegetables has increased over time, although the mix between fresh and non-fresh consumption has altered towards more processed products.
- Australia does not 'rank' as being a significant contributor in world terms to the production of any major horticultural commodity (with the exception of macadamia nuts).
- Australian exports of horticultural products is significantly below that of its major southern hemisphere competitors.

## 4.0 THE AUSTRALIAN HORTICULTURAL VALUE CHAIN

### 4.1 A Historical Review

The Australian horticultural sector, particularly from a production view point is generally characterised as being fiercely individualistic. Growers have a reputation for not working well together and tending to be non-trusting of the people to whom they market their produce. This tendency has been driven by:

- The large distances between producers and customers making understanding of others businesses and the development of relationships difficult. This issue holds true both with the domestic market and also international markets.
- Until relatively recently poor communication mechanisms between each linkage in the supply chain.
- Generational farming. The presence of corporate horticultural investment in Australia is relatively low. Farms are generally family owned, often with members of many generations working them. In many instances there are examples of strong patriarchal control, which may inhibit the adoption of new technologies and methods of doing business.
- Ethnicity. Many farmers can trace their roots back to non-Anglo Saxon origins. This has and may contribute to poor communication due to language and ethnicity barriers and as well as poor uptake of communication technologies. In some cases regional and country rivalries from the 'old' country have extended to the 'new' country.
- An apparent unwillingness of the production and wholesaling sector to adopt communication technologies which would assist with the improvement of transparency along the value chain.
- The lack or removal of regulatory control in the development of "acceptable terms of trade" business systems between the production and other sectors.
- The diversity of the range of products produced, unlike relatively homogenous products such as milk, making issues such as production technologies, and research and development efforts more complicated to address.
- Farmers in particular not willing to invest in looking at industries beyond the farm to develop new understandings of how business relationships should be conducted.
- A perception by many that those beyond the farm gate are taking excessive margins.
- For many farmers a tendency to receive low margins from a high sales turnover and also businesses returning relatively low returns on capital invested.

As with all industries there are considerable extremes in terms of the size, focus / outlook, preparedness to adopt new technologies etc of individual businesses. This report will seek to document those levels of diversity by discussing the various different roles of each sector in the chain, how each sector perceives the other. It will then discuss some of the drivers/issues that are/will impact on the nature of the sector in which they operate and the horticultural industry as a whole.

### 4.2 Australian Horticultural Value Chain

The Australian horticultural value chain by other agricultural standards is relatively short as the product goes through few if any transformation steps prior to consumption. Even today the majority of fruit and vegetables are sold in their harvested form. When produce is processed, it generally involves one transformation process, e.g. fresh cuts, restaurant



meals, frozen chips. Products that may involve multiple transformation processes are some of those goods that are processed into highly processed / refined consumer goods, e.g. baby foods.

By contrast, in the wool industry the product must go through numerous transformation steps, with a variety of processors, ending up in a myriad of finished end goods.

However, the horticultural chain whilst relatively short is very complex with the large diversity of companies who are the ultimate suppliers to consumers, e.g. chain store retailers, independent retailers, food service.

Figure 4 below provides a description of the current Australian horticultural value chain structure. The diagram does not include any description of non-transactional steps such as freight movements or packing services. The diagram shows the flow of transactions, with those flows being relatively minor in the context of the overall transactional value of the chain shown by a dotted line. Major product flows as they pertain to the current industry are indicated by thicker lines.

The following sections will discuss the major transactions / movements in Australia's current value chain for horticultural produce.

### 4.3 Growers

#### STRUCTURE OF THE SECTOR

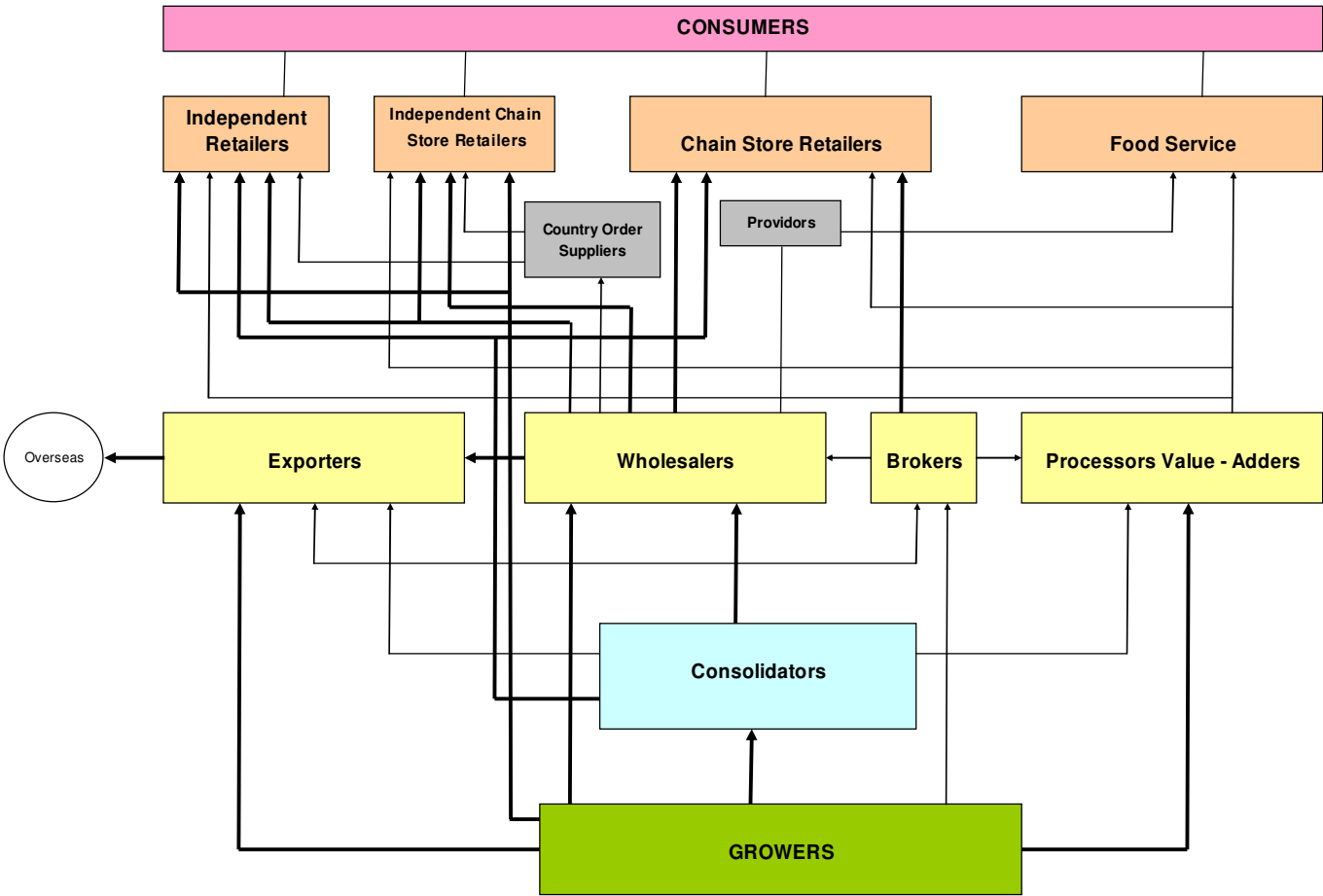
In Queensland there is a wide diversity of the scale of enterprise involved in horticulture. The range is from hobbyists who regard horticulture as a secondary source of income or producers whose turnover is less \$100K per annum up to family owned holdings who have sales in excess of \$40 million per annum. Within Queensland there is limited corporate farming with the notable exception of a number of tree and vine enterprises; Table Grapes Australia, Golden Mile and Nature's Fruit are examples of these.

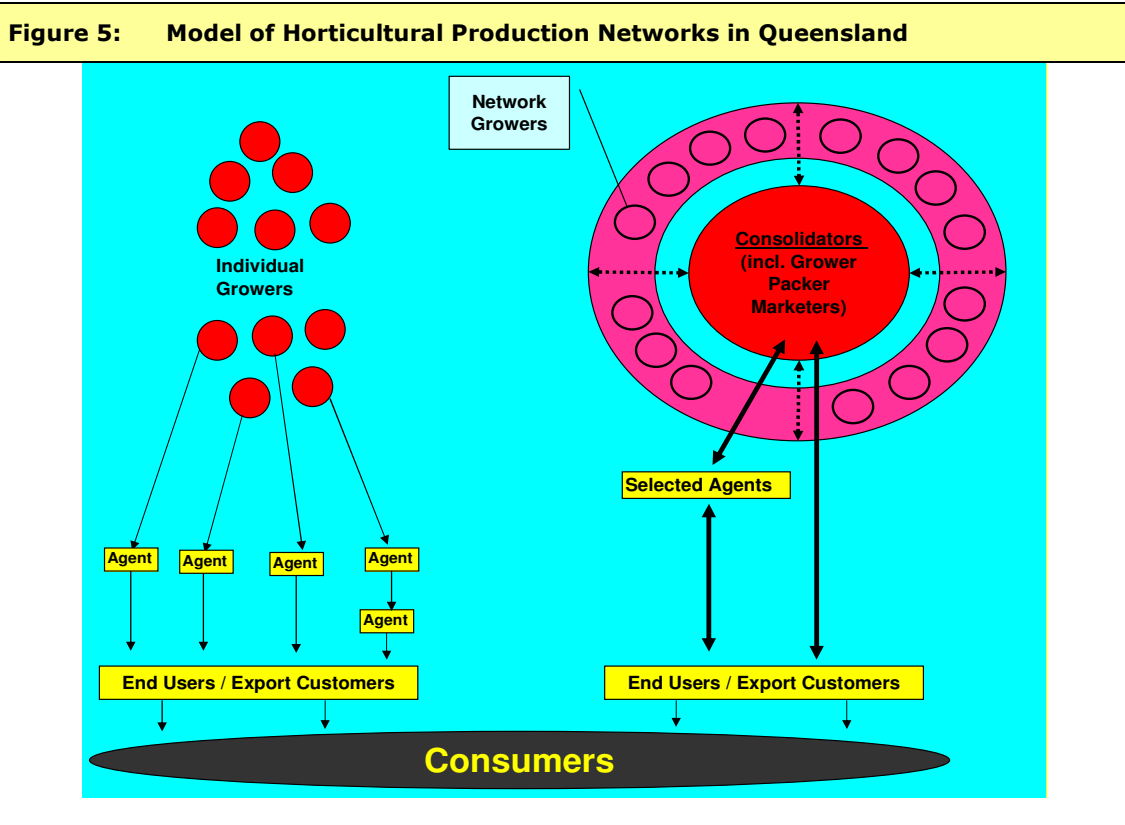
Further the nature of the relationships that each of these producers has with their customers is quite variable. In analysing the production sector of horticulture, we have found three distinct classifications of growers. These are:

1. Individual Growers
2. Network Growers
3. Producer Consolidators or Grower Packer Marketers.

Diagrammatically, the nature or position that they assume within the supply chain is shown in Figure 5. Thick black lines are indicative of major transaction paths and thinner black lines are relatively less important transaction pathways.

Figure 4: Current Australian Horticultural Value Chain Structure





Source: CDI Pinnacle Management

In considering how each of these parties interact both between themselves and others in the value chain, a number of general characteristics can be attributed to each of the three producer groupings. These are described in Table 4 below.

<b>Table 4: Characteristics of Different Types of Queensland Horticultural Producers</b>
<b>CONSOLIDATORS or GROWER PACKER MARKETERS</b>
<ul style="list-style-type: none"> <li>▪ Grow, pack and market to each customer's specific requirements</li> <li>▪ Have orders or contracts to fill <u>prior to planting</u> or advising Network Growers what to plant</li> <li>▪ Product is produced, packed, and warranted to comply with specifications</li> <li>▪ Market own product and that of network growers, if a grower consolidator. Non-grower consolidators market product on behalf of the network growers</li> <li>▪ There exists a variety of arrangements whereby produce is supply to the consolidator including product being sold to consolidator, maximum / minimum pricing scheme, fee for service packaging and marketing, fee for service for marketing, area contracts and volume contracts</li> <li>▪ Receive advice, guidance, instructions, support, estimates and other information direct from end users and trading partners</li> <li>▪ Good knowledge of where product is ultimately sold</li> <li>▪ Get information about supply chain and how to improve it (direct from end user &amp; trading partners)</li> <li>▪ Are part of a <b>system</b> that supplies products to fit requirements of specific customers and are directly involved in decisions about who they do business with and what must be delivered to satisfy consumer demands.</li> </ul>
<b>NETWORK GROWERS</b>
<ul style="list-style-type: none"> <li>▪ Operate as grower members of a network</li> <li>▪ Are guided and directed by a consolidator</li> <li>▪ Have orders or contracts to fill <u>prior to planting</u> (this may not cover all their production)</li> </ul>

<ul style="list-style-type: none"> <li>▪ Produce part of a substantial volume that is marketed via the consolidator</li> <li>▪ Market via a consolidator for most of their production</li> <li>▪ Get advice, guidance, instructions, support, estimates and other information from consolidator</li> <li>▪ Have reasonable knowledge of where their product is ultimately sold</li> <li>▪ Receive information about their supply chain operates and how to improve it via consolidation</li> <li>▪ Feel they are part of a system that produces products to fit the requirements of specific customers.</li> </ul>
<b>INDIVIDUAL GROWERS</b>
<ul style="list-style-type: none"> <li>▪ Mostly produce without firm orders or contracts to fill</li> <li>▪ Generally have small volumes to offer compared to any significant customer's requirement</li> <li>▪ Generally sell via one or multiple wholesalers, sometimes product goes through multiple wholesalers before the product reaches its penultimate delivery point e.g. retailer</li> <li>▪ Generally receive little feedback from wholesalers or end users as they are a small part of wholesalers total business</li> <li>▪ Have little knowledge of where their product is ultimately sold</li> <li>▪ Have low levels of knowledge about the supply chain in which they operate</li> <li>▪ Feel relatively powerless to do anything about changing the way they produce or market their products</li> </ul>

Source: *CDI Pinnacle Management, 2002*

### EMERGENCE OF CONSOLIDATOR NETWORKS

History has shown that horticultural producers do not have a natural tendency to work closely with one another, unless in a co-operative or similar commercial relationship, many of which did not focus on marketing of fresh produce as the primary activity. So what has been the driver to the development of consolidation networks? Largely, consolidation networks have been pro-actively or subtly developed as the result of initiatives driven by chain retailer activities.

Increasingly, retailers are seeking to develop networks or consolidation models that can assist / work with them to or deliver:

- Long lines of consistent supply and quality of product;
- Supply volumes of product commensurate with the needs of the retailer;
- A reduction in the purchase cost of produce by removing some chain linkages;
- Lower transaction costs (by reducing the number of suppliers who have to be dealt with);
- Pro-active relationships with suppliers who will deliver to their specification rather than rely on others to transfer that information;
- Development of retailer own-label branding; and,
- Pro-active relationships that will allow for pursuit of innovation in the chain whether in relation to transactions, relationships or varieties.

Consolidators, fall into three categories presently. These are:

1. **Grower Consolidators:** Are consolidators who grow produce in their own right, but who also co-ordinate / direct other growers to supply them. Grower consolidators are the company who has the relationship with the wholesaler / retailer / exporter. It is rare for network growers to be aware of the relationships between the customer and the grower consolidator. A more detailed description is presented in Table 4 above. Queensland examples of grower consolidators include Gaypak, Mulgowie Farming Company and NQ Banana Co-operative.

2. **'In-house' consolidators:** Have a contractual relationship with a retailer to possibly acquire produce on behalf of the retailer, but are also responsible for logistics and warehousing. C&S Global and Costa's are examples of this type of consolidator. In many instances, whilst these companies will have supply arrangements with growers or grower consolidators, the relationship is not as close as for the other two consolidator groupings.
3. **Non-Grower Consolidators:** Are consolidators who do not grow produce but who work closely with a limited number of suppliers to develop programs for the retailers or processors. Growers may or may not participate actively in the relationship between the non-grower consolidator and retailer or processor. In many instances the financial relationship between the grower and consolidator is different from a grower / wholesaler relationship. In many instances, this type of consolidator is either a current or former market wholesaler. Non-grower consolidators are responsible for all activities associated with the relationship except the growth, packaging and in some instances the movement of the product. Some non-grower consolidators may have financial investments in packaging operations, further strengthening / tying the relationship with the produce. Examples of this consolidator type, include Perfection Fresh Produce, Favco, Moraitis Fresh and Chiquita.

### RATIONALISATION OF THE PRODUCTION SECTOR

The Australian Bureau of Agricultural & Resource Economics stated that the number of farmers in Australia has declined while production in most sectors has increased. These trends indicate that individual farm businesses are becoming larger. Australian Bureau of Agricultural and Resource Economics data suggests that approximately 70 per cent of raw agricultural food and fibre products is produced, or controlled, by 30 per cent of farms. These statistics are supported by production figures from the Lockyer Valley—a major horticultural area in Queensland—where production is dominated by five major consolidation / production networks (Dunne & O'Keefe, 2004).

Why has this level of rationalisation occurred? Rationalisation has occurred largely as the result of cost pressures on smaller scale farms, as revenue growth fails to keep pace with costs growth. The impact of the cost price squeeze on smaller farmers has been that:

- Smaller farms have had to move into more intensive or high value cropping and / or specialised production e.g. shade house production;
- Smaller farms have been bought out by neighbours or others in order to make bigger productive units;
- Smaller farms have sold out of the industry with the farm area being used in some other form of land use, e.g. Property development;
- Smaller farms have had to get bigger by acquisition and / or increased borrowings; or
- Smaller farms have had to become suppliers to other aggregators or consolidators.

Due to the relative low costs of entry for many horticultural crops, particularly some vegetable crops, there has been over time a significant movement in and out of the industry by opportunistic farmers. These farmers are either involved in other agricultural enterprises or have jobs in areas other than agriculture.

As horticulture has become more and more specialised and technically advanced the margins available to these 'opportunistic' farmers have become less and so their presence is no longer as evident.

As an example, one of the greatest areas of aggregation / grower movement out of the industry has occurred in the Bowen tomato industry. Industry sources suggest that 15 years ago, there were 50-70 tomato farmers in region, this number has now decreased to 10, with five significant operations. Some farms in that region are producing well over one million boxes of tomatoes per annum, whereas 15 years ago a producer of 250,000 boxes was considered very significant.

So what has driven this cost-price squeeze at the grower level in horticulture? In its simplest form it is the general overproduction in comparison to demand from consumers driving down real prices, in conjunction with the general tracking of input prices with the consumer price index (CPI). The major causes of this over production are:

- Extension of production time zones in many traditional areas, whereby producers move out of their traditional zones in order to hopefully gain a market advantage if other regions 'fail';
- Opening up of new production regions, particularly in respect of fruit production whereby supply windows are lengthened;
- Development of new varieties allowing for increased per unit area of production and / or more regular or consistent production;
- Technical advances allowing for greater recovery of yield, more efficient harvesting and improvements in transportation and cooling technology;
- Limited per capita growth in vegetable consumption; and (possibly most importantly); and
- The poor communication of price signals down to the production end of the chain.
- Purchasing strategies of chain store retailers and others.

### **FUTURE STRUCTURE OF THE PRODUCTION SECTOR**

The Queensland horticultural sector over a number of decades has undergone considerable rationalisation, a process which is expected to continue. This is because as the growth in fruit and vegetable demand fails to keep pace with industry's ability to produce it within Australia, and internationally as we become less competitive in relation to our competitors, the industry will face a virtually constant state of oversupply (except for the influence of weather). Further, those higher up the value chain are increasingly developing strategies that focus on forming relationships with those who have the ability to produce high quality produce in sufficient volumes over an extended time period.

In order to meet the needs of the larger retailers and processors, either producers will become larger and/or consolidators (grower, non-grower, in-house) will emerge. Grower consolidators and large growers will have to possess skills ranging from on-farm management, preparedness to adopt and invest in innovation both within and beyond farm gate, category management skills, an ability to interpret and manage information across the chain and a willingness to invest in relationships across the chain. The need to develop such skills will preclude a large proportion of the producer population from achieving these positions in the value chain. In most instances, producer consolidators and large growers will develop these skills independent of traditional industry organisations and, rather, will recruit suitably skilled personnel or use external consultants.

Retail in-house consolidators, non-grower and grower consolidation models will require producers who are part of these networks to have an entirely different set of skills. These producers will need to be able to work within a consolidation framework where they are able to deliver to the specified needs of the consolidators, to a pre-agreed packaging format, volume and grade. In many instances their ability to deliver to these pre-agreed standards will by negotiation determine the level of rewards. These types of models are more common in southern states where there has been in the past a greater predominance of processors who have provided supply contracts. Queensland producers have more of a 'trading mentality' due to their greater predominance of relationships with the wholesaler market sector.

Successful producers in the future will need to seek to achieve 100 per cent crop utilisation (utilising all of the crop that they grow) in order to maximise potential return.

Individual growers will continue to survive and prosper only if they are able to either:

- Produce crops in a cost efficient manner whereby the size of the market precludes entry by larger players;
- Produce crops to the exacting specification of buyer, whether they be a retailer, wholesaler or processor as the arbiter of consumer choice / demands;
- Be increasingly quality focused. The low quality end of the market is becoming smaller and wholesalers in particular will wish to deal with only quality suppliers as their customers only have demand for such product;
- Have a marketable point of difference in terms of the product that they produce; and/or
- Adopt business practices and knowledge that enables growers to understand and act upon market signals, information provided by others or discovered by self, combined with strong on-farm skills.

Individual growers who do not address these needs will face challenges to their commercial survival as they will become increasingly irrelevant to the rest of the chain.

### **OTHER KEY INFLUENCERS ON THE PRODUCTION SECTOR**

Other major influencers to the costs and operational structure of the production sector but not subject to detailed discussion in this report include:

#### 1. Cost , skills and availability of labour

Seasonal labour is seen by the production sector to being less and less available, particularly in its preparedness to undertake certain activities. Also the bodies that represent labour are being increasingly successful in raising minimum award levels. These two factors will continue to impact adversely on the competitiveness of individual farmers.

Further, the skills required by workers in the sector, particularly those that are impinged on by workplace health and safety and other compliance directives are increasing. As businesses grow, HR and business skills are also becoming important areas in which skills are required. Increasingly however the ability to source these workers is becoming more difficult and indications are that this situation will continue.

#### 2. Access and cost of water

Access and cost of water combined with labour and prices received for produce as the major factors impacting farm viability. Increasing government regulation of water resources, lack of capital development works , a trend toward 'user pays' and water 'trading' all suggest that farmers will be faced with increasing management pressures for the water they do use and the costs associated with being given access to it will also cause significant impacts.

3. Impact of urban communities on the ability of farmers to carry out 'normal' farming practices on their land.
4. Increasing costs of business of compliance, both governmental and 'through' chain.
5. The development of, availability of and cost of new technology.

### **KEYPOINTS**

- There are 3 'types' or classifications of growers, individual growers, network growers and producer consolidators or grower-packer marketers.

- The producer sector is undergoing enormous rationalisation pressure due to structural changes further up the value chain (chain reversal).
- Over time due to chain reversal and gradually increasing dominance of the retail marketing sector for fresh produce, individual producers will have to develop strategies that differentiate them from the grower-packer marketers (grower consolidators).
- There are 3 types of consolidation models currently in existence, growers consolidators, 'in-house' consolidators and non-growers consolidators.
- There is a wide range of other 'external influencers', labour (cost and availability), water (cost and availability), government policy, community expectations, compliance issues and access to new technology that will also be 'shapers' to the production end of the value chain.

#### **4.4 Retailers – Structure and Influences**

##### **STRUCTURE OF THE SECTOR**

Australia has the highest level of retailer dominance by as few players in the rest of the world. Industry sources suggest that the major retail chains of Woolworths and Coles have 55-60 per cent market share of the fresh produce category (and closer to 80 per cent in dry goods). The majority of the balance of the market is shared between independent retail chains, e.g. Metcash (IGA), specialist independent fruiterers and fruit and vegetable barns.

The disaggregated nature of the sector has not allowed the compilation of accurate statistics on the relative shares and performance of the sector.

Over the last decade there has been a dramatic shift in the dominant purchasing source of fresh produce retailing away from small-scale specialist fruit and vegetable shops and barns to supermarket chains. Accurate market share data in the fresh produce industry is difficult to obtain, but it is estimated that Woolworths hold a 30 per cent market share, Coles 18 per cent and, before its demise, Franklins held a five per cent market share. This later share has been partially broken up between independent chains and the other two major players.

In a submission to the Baird Review, Coles stated that their average profit margin was 3.4 per cent across all categories, as compared with the United States with rates of 4 per cent of 5 to 6 per cent in the United Kingdom (Commonwealth of Australia, 1999). Industry sources suggest that in dry goods the average profit margin is 1-2 per cent and significantly higher in fresh produce. Fresh produce is acknowledged as providing the highest return per square metre of major supermarkets.

##### **FACTORS INFLUENCING THE RETAIL SECTOR**

Whilst there may be relatively few players in retail, the level of competition is high, as each seeks to gain an improved level of market share. In particular, the fresh produce category is currently in a strong competitive environment as it is seen to be the major point of differentiation between retailers, whilst also delivering the highest level of margins. Beyond returns per unit area, some of the other drivers that retailers are driving down the chain include:

- Improved variety of offer. Reg Claires, former CEO of Woolworths commented that 15-20 years ago there were 40 lines of produce, and five years ago this figure had risen to 140, with experience showing this number has increased even further. An improved variety of offer is seen as a major differentiation point between retailers. This improved variety of offers includes different new products or varieties and / or greater variety of formats, e.g. pre-packed.



- Consumer demands for variety. Consumers are demanding an improvement variety of assortment of offers, including produce that delivers improved levels of convenience, e.g. fresh cuts, microwaveable packing.
- All Year Round Supply: Consumers are demanding that produce of any type be available all year round, whether it is from local production or from imports. For example, grapes which were available for 3-4 months up to 10 years ago, is now available for up to 10-11 months of the year.
- Food Safety and Integrity: Consumers are increasingly becoming health conscious particularly in regards to how the food they are presented with has been handled. Retailers are therefore driving the development of packaging formats that reduce the potential for infections from the handling of produce, e.g. hepatitis. As a result retailers are demanding the adoption of quality assurance systems, often in-house, such as Woolworths Vendor Quality Management Systems and Coles SQF program.
- Sustainability: Consumers are increasingly becoming aware of the resource / production sustainability issues. Issues such as the use plastic bags are modifying retailer behaviour and similarly others will become higher on the agenda of consumers over time.
- Stock Management: Consumers are not forgiving of retailers who do not have available what they require whenever they require. As a result retailers have increasingly focussed on inventory / stock management so that out-of-stocks do not occur. This has driven the development of JIT, supply programming and vendor stock management, whereby retailers are working increasingly closely with vendors.
- Cost: Competitiveness is driving retailers to seek ways that they can drive costs out of their chain. Concepts such as lean thinking, supermarket internalisation, category management, vendor management systems, waste / ullage control systems, ECR, self-scan, are all strategies being adopted by retailers to either lower the cost of goods / inventory or minimise the transaction cost internally. To be discussed in greater detail later is the developments occurring associated with shelf-ready packaging for the supply of produce.
- Supplier Rationalisation: Historically chain store retailers purchased the majority of their stock from wholesalers operating in the major capital cities. Over time retailers have increasingly sought to develop alternative supply arrangements both with some of those companies operating within the wholesale market and more directly with grower consolidators. Once again, recent developments and its implications will be discussed in a later section.
- Quality: The quality of produce is a major influencer in regards to consumer demand and choice of retailer. Retailers are therefore less tolerant of variable quality produce and as such are increasingly seeking to identify suppliers who can both deliver the consistency of quality and length of lines. This is in part a major contributor to the drive to supplier rationalisation.

Similar drivers exist with regards to the food processing sector as with the retail sector.

#### **4.5 Recent Developments in the Australian Retail Sector**

The Australian retail sector particularly as it applies to fresh and minimally value added produce is undergoing a series of dynamic changes and is in a virtually constant state of flux. Industry sources suggest recent and future developments may in fact result in a fundamental shift to the way that the whole value chain is structured and the responsibilities that parties in the chain assume, with potentially significant implications to profitability.

The drivers to this change include:

1. Industry perceptions that Coles are gaining market share from Woolworths on the back of improved category management of fresh produce and their fuel loyalty program which has more outlets, even though a later start-up.
2. Concerns by both of the 'Big Two' about the growth of Aldi in the eastern seaboard particularly as it relates to ongoing margins and potential loss of sales. There also abounds industry rumours that other chains may target Australia, such as Costco, a very large multi-faceted retailing organisation.
3. A renewed focus on driving costs out of the retailing section of the chain to improve competitive efficiency with retailers. Examples of such initiatives include supplier rationalisation, chain shortening and retail-ready packaging.
4. A drive to source and supply produce to consumers all year round, with a renewed focus on importing product to meet supply niches.

### **WOOLWORTHS STRATEGY**

Woolworths has been acknowledged by industry as the leader and pace setter in the development of the fresh produce category to date. According to industry source, the "Fresh Food People" brand has assisted Woolworths to obtain up to 38 per cent of the fresh produce category sales. The key drivers to this position as industry leader are seen to be:

- Adoption of proven international retail marketing strategies;
- Professional retail formats;
- Stronger focus on delivery of service and quality of produce in comparison to competitors;
- Skilled staff; and,
- Produce sourcing policy leading to a generally shorter chain length.

However this position as 'king of fresh produce retailers' has recently been placed under threat as both Coles and independent retailers successfully claw back market share. This rejuvenation has been driven by a number of factors including:

- Historically a pricing policy of Woolworths providing higher than industry standard gross margin returns which has allowed others to be more competitive in terms of price;
- A loss of key staff to competitors;
- A perceived lack of innovation / change of formats at Woolworths retail level;
- Adoption by Coles of a model very similar to that of the 'Woolworths' model.

Woolworths has however been quietly working away at developing a major new initiative in produce retailing which, if successful, will remove significant costs out of Woolworths, although some industry observers are concerned that it might add costs to the rest of the chain, particularly at the production end.

The recently announced to industry, Mercury Program, will focus on a number of new initiatives. These include:

- Logistics – Rationalisation of the logistics model. Firstly, preferred suppliers will be given access to the right to use Woolworths contracted logistics providers to transport produce. This is expected to deliver considerable savings across the chain. Additionally, there will be considerable rationalisation of the distribution centre network whereby fresh produce will be warehoused in a single location.
- One Touch Initiatives – Shelf-ready Trays – By January 2005, Woolworths have indicated to suppliers that they wish all goods, including produce, to be supplied in shelf-ready trays. Goods will have to be able to be put on and taken off display in the carton / tray

that it is supplied in. This initiative seeks to reduce the cost of labour associated with the current processes associated with stacking and unstacking of shelves.

- In order to best link product displays with packaging, Woolworths will in future, only accept product that is stacked either six or 12 cartons to the layer.
- Supplier Rationalisation – Woolworths remains committed to continuing to drive the reduction the number of direct delivery suppliers and number of wholesalers / brokers who supply produce. In future the number of suppliers will vary on a line-by-line basis, depending mainly on the supply and demand dynamics of the line.
- Further it is thought that Woolworths will seek to increasingly drive the development of a house branding strategy.

### **IMPLICATIONS OF WOOLWORTHS STRATEGY**

The Woolworths' 'one touch' initiative in particular will have profound effects on the horticultural value chain. Some of these implications may include:

1. Packers having to develop a whole new range of packaging which may or may not be aligned with packaging supplied to other customers. This will frustrate efforts towards industry packaging standards. Further it has the potential to add significantly to costs of compliance by producers and packers.
2. Produce that is rejected by Woolworths, being subject to heavy discounting by other purchasers as the product is either known to have been rejected by Woolworths or is in an unsuitable packaging format.
3. May result / assist in a further rationalisation of suppliers, as some may determine the new packaging requirements too onerous and / or expensive to comply with.
4. Will further promote the development of direct linkages between suppliers and Woolworths, as packers will need to have more complete information about supply in particular, as well as quality standards.
5. May support the development of a new category of packer, whereby a company may pack product delivered in bulk by suppliers solely or otherwise for Woolworths. These businesses may be located close to the source of purchase, i.e. a metropolitan centre. This type of model is similar to that which exists in the United Kingdom, with the services provided by Mack Multiples, and allows for a high degree of responsiveness by the packer and supplier.
6. May reduce the role of local Woolworths buying officers, as supply programs become more centrally controlled and direct.

Further the transportation / logistics initiatives have the potential to deliver considerable 'in-chain' savings to participants. It will however require the development of a more complex information system, in many cases by transport operators who may not be experienced or currently involved in farm to Distribution Centre (DC) distribution. Further, existing farm to DC transporters will not give up this market easily and so therefore may result in a greater level of competition at this level of the supply chain.

### **COLES STRATEGY**

With the retention of many of Woolworths' senior staff in recent times, Coles is and has developed a purchasing / supply strategy similar to that of Woolworths.

In the past Coles had a slightly longer horticultural value chain, whereby CS Global and Costa's have been given the role of major category suppliers to Coles. Previously, Coles provided orders to either CS Global or Costa's who were then responsible for ordering, logistics and distribution.

Industry sources, suggest that Coles will in future, particularly where there are relatively few suppliers in a category, purchase product direct from packers and will use CS Global and Costa's for logistics and distribution. However, it is expected that at least in the short term where there are many suppliers to a product category, that these intermediaries will maintain their current roles.

Coles recently announced that they intend to restructure their DC network. This will involve the construction of a number of new DC's either being independently or joint venture owned, management either by Coles or others (as currently exists for CS Global and Costa's). In essence it appears that Coles will seek to achieve increased cost reductions of operations and, where appropriate, divesting the management of supply and logistics to others.

Coles have indicated their intention to increasingly source product under supply management programs, with a decreasing focus on ad hoc / spot-buying from the wholesale markets. The level of this commitment will vary depending on the nature of the supplier base (few or many suppliers), the seasonality of the product line and the variability associated with consumer purchasing patterns.

The impact of such a strategy by Coles, is similar to that which has been provided by Woolworths, this being:

1. Increased level of direct supply coordination from the producer or specially aligned wholesalers / brokers.
2. Potential for the removal of some costs from the value chain through removal of duplication of roles.
3. A move towards the adoption of 'house' brands.

#### **IMPLICATIONS OF THE COLES STRATEGY**

The implication of the Coles strategy on horticultural producers can be summarised as follows:

- An increasing focus by Coles to have reduced numbers of suppliers and less of a focus on dealing with the wholesale sector for supply, either through or not an intermediary.
- Increased numbers of direct relationships with suppliers who can deliver to the requirements of Coles and share their 'vision' for the future.
- Reduced opportunities unless part of a consolidation network for producers to become Coles suppliers.
- Increased opportunities for 'fast moving' suppliers to develop a lasting relationship with the Coles network, through supply, logistics, product and marketing innovation and support.

#### **ALDI STRATEGY**

Aldi has aggressively moved into the eastern seaboard grocery industry, with indications of 40 stores being opened in Sydney, 19 stores in Melbourne and the recent opening of two stores in Brisbane, with a confirmed indication of a further 10 to be opened in Brisbane alone by the end of 2004.

The company has an aggressive locations strategy, whereby stores are closely located to either of the big two retailers. Their aggressive pricing strategy focussing on a limited range of SKU's (about 600), shelf / pallet-ready packaging and 'no frills' image is seen as a credible threat to the dominance of Coles and Woolworths.

Sources suggest that Aldi are prepared to operate on margins as low as 15 per cent on produce lines, well below the 35 per cent of other players. In Australia, Aldi currently only

sources 20-25 fruit and vegetable lines, and does not see produce as a central plank to its marketing strategy. This may however change over time.

It is unclear how Aldi will develop its fresh produce offering, which may be subject to change. Presently Aldi have appointed external supply co-ordination managers who have the dual role of facilitating logistics and transportation (similar to CS Global and Coles). Whether or not this is a long term strategy is uncertain, as normally purchasing policy of grocery items is for direct negotiations between packer / processor and Aldi. It is clear however that over time that Aldi will demand 'house label' packaging.

### **INDEPENDENT CHAIN STORE RETAILERS – IMPACTS OF PURCHASING DECISIONS ON THE VALUE CHAIN**

Independent chain store or independent retailers are seen by industry as not being as advanced in the development of 'direct' supply relationships with growers and / or consolidators. This in part is seen as a timing issue as, until recently, these retailers lacked access to centralised receipt and distribution centres for fresh produce. In addition, independents tend not to have the scale of purchasing necessary to be of interest to larger growers. Additionally, a number of these companies were comfortable with sourcing produce from the wholesale market on a normal trading basis.

Many independent chain store retailers do not have a focus on the fresh produce category. In major urban centres consumers tend to use them for convenience or 'top-up' shopping. In regional Australia on the other hand they are seen as more central by consumers as the Big Two retailers may not be located in their town. It is apparent in urban centres the fresh produce category has less importance than in regional centres. It must be noted however, that since these stores are independently owned the level of focus on fresh produce does vary.

Independent retailers purchase fresh produce from a variety of sources. These are:

- Direct from local suppliers.
- As an individual or buying group where an in-house buyer purchases produce generally from the wholesale market. In most instances they are then responsible for organising consolidation and distribution.
- Using the services of a 'country order' buyer whereby an independent company arranges the purchase, consolidation and movement of produce to the independent retailer.

There is limited evidence of the development of direct supply linkages between independent retailers and producers, with most relationships involving the presence of a wholesaler. Industry sources suggest that this is not likely to change greatly in future. Based on the likely level of throughput, the costs of establishment of distribution centres and associated infrastructure does not make it efficient.

### **INDEPENDENT RETAILERS**

Due to their relatively limited purchasing capability, independent retailers are virtually entirely dependant on the wholesale markets for the supply of produce.

Where independent retailers are located outside metropolitan regions, they organise buying groups whereby a representative of a number of independents from the same geographic region travel to the major metropolitan markets up to three times per week to buy on behalf of the group. Alternatively, 'country order buyers', who are located within the major markets, receive and consolidate orders and then arrange for transportation.

Many independent retailers have in recent years altered the process by which they purchase produce. Previously, most buyers would 'walk the market' negotiating with individual wholesalers for different products, with the focus being on minimising the price paid. As the cost of doing business for retailers have continued to grow, many retailers today pre-order produce either the day before or prior to the markets opening. Those orders are then consolidated by the wholesaler ready for pickup when the market opens.

The implication of this approach is that retailers are increasingly focussed on the brand that a wholesaler has available and will tend to come back to that brand if it satisfies their requirements. Price becomes less of a focus in return for quality of produce and convenience associated with its purchase. If however a produce line is not available on a regular basis, the wholesaler is less able to market the brand effectively. As a result, wholesalers are increasingly seeking high quality, longer lines of product in order to meet the needs of its customers. Of less interest to wholesalers are growers who supply small lines of produce, unless they are of a very high and consistent quality.

**THE FUTURE FOR INDEPENDENT RETAILERS**

Industry considers that the future role of independent retailers will largely hinge on three issues, these being:

1. The ability of the independents to compete as the larger chain retailers seek to maintain or increase market share either by pricing cutting or driving costs out of their chains.
2. The ability of independent retailers to maintain a level of differentiation from chain store retailers through quality, level of service and display formats, in particular as some chain retailers are looking at shelf-ready packaging.
3. The ability of the retailer to maintain traffic flows, if they are outside a major shopping centre or mall.

Certainly the future of fruit barns or lower cost retailing operations is uncertain. Consumers are increasingly focussed on quality produce and are not necessarily interested in lower quality produce, no matter the price. This statement must obviously be qualified in respects of some of the lower socio-economic regions.

Industry is generally uncertain about the medium-term future of independent retailers. Some consider that they are under great threat as the 'majors' exert greater pricing and cost reduction influence over them, thereby threatening their own margins. Others consider the future to be bright, as they believe that given the drive to cost reduction through changed formats a certain proportion of consumers will respond with their feet in going to retailers who provide a high degree of service, product differentiation and quality.

Location will obviously become even more critical in future, as smaller scale shopping centres in many particularly established regions are faced with lower traffic flows, as the larger centres are more able to provide the 'one stop shop' convenience.

**KEYPOINTS**

 **KEYPOINTS**

- There are 5 major groups of retailers who are currently influencing the nature of the value of the chain and the developing and driving of strategies at their level. These are Coles, Woolworths, Aldi, Independent chain stores and independent retailers.
- The retail sector, is presently undergoing significant change through the development of marketing strategies, development of lean thinking principles the impact will influence forever the structure of the horticultural value chain.
- The major influencers to the sector can be summarised as: increasing consumer demand for variety, all year round supply, food safety and integrity, sustainability, stock management, competitive costing, supplier rationalisation, quality and downstream category or supply management..

## 4.6 Central Markets

### STRUCTURE OF THE SECTOR

Traditionally, wholesale markets in the major capital cities were the centre piece of the selling and distribution system associated with horticultural produce. The normal practice was that producers delivered produce to their agent on consignment to sell on their behalf. The buyers for the supermarket chains 'trawled' the central markets and purchased their requirements on an opportunistic basis. There was little, if any, information exchange or supply co-ordination—practices that has become the focus of some grower discontent and mistrust.

Although central wholesale markets do continue to perform these roles, their relative importance as a 'clearing house' has declined as more direct linkages have been formed between growers and retailers. Anecdotal evidence suggests on average that the supermarket chains source approximately 40 per cent of their requirements from the central markets and this percentage continues to fall (Dunne & O'Keefe, 2004).

In today's world the central markets have four primary functions:

- Receival of produce by non-wholesalers for on-forwarding to customers by way of non-grower consolidation network. For example, in Brisbane, CS Global receives produce direct from growers / suppliers who then organise the distribution to either Coles stores or other customers. In this event the 'contracting' point for the sale of the produce is outside the wholesale marketing system. There are many other examples of this type of role by the central markets.
- Receival of produce for subsequent sale by wholesalers.
- As a transportation, storage and logistical hub for the movement of produce.
- In southern centres, such as Sydney and Melbourne, as a centre to allow fruit and vegetable growers (or their 'agents') to directly negotiate the sale of their produce.

Industry sources suggest there are three tiers of wholesalers based on size within the Brisbane Wholesale Markets, with the largest (no more than eight) having a turnover of in excess of \$80 million per annum, a middle tier with sales turnover of \$20-\$79 million and a third tier of with sales of less than \$20 million per annum. The last tier are generally family-owned businesses with low levels of staffing and investment in infrastructure. Industry sources suggest that in the future, third tier producers are going to have the greatest difficulty in surviving as costs (for example stand rental fees), investment required in storage facilities and technology also increase.

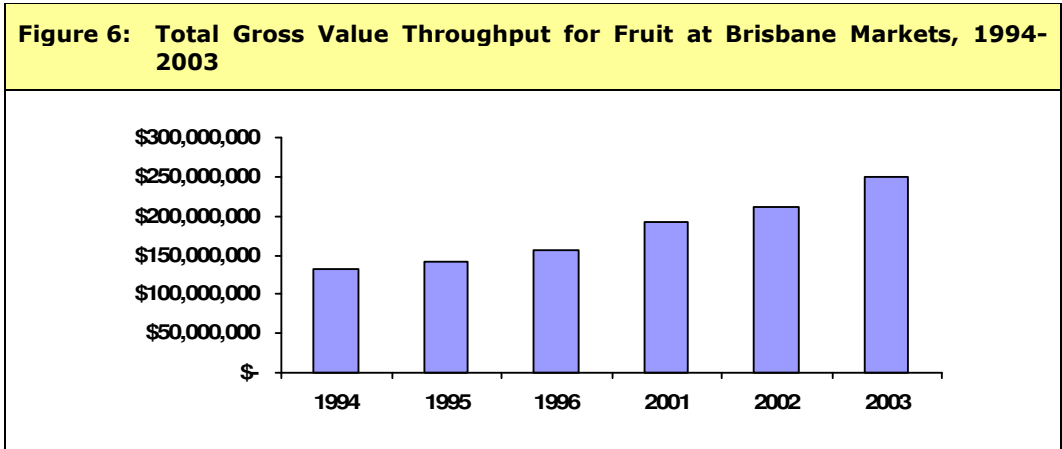
Currently, given the low level of turnover of wholesaling businesses the level of profitability of the wholesale sector is sufficient to maintain those already in the sector and / or to attract new entrants as others move out. Increasingly wholesalers are having to take a closer look at their margins and cost strategies. They will need to adopt practices to support progressive growers and to discourage poorer or smaller growers, and identify market niches in which they can grow their business.

A number of players, mostly from outside the wholesaling sector, have forecast the demise of the wholesaling sector as has occurred in the United Kingdom and increasingly in the United States. This will only occur if the independent retail sector in Australia is displaced and if wholesalers do not undertake business engineering to be relevant to those who survive.

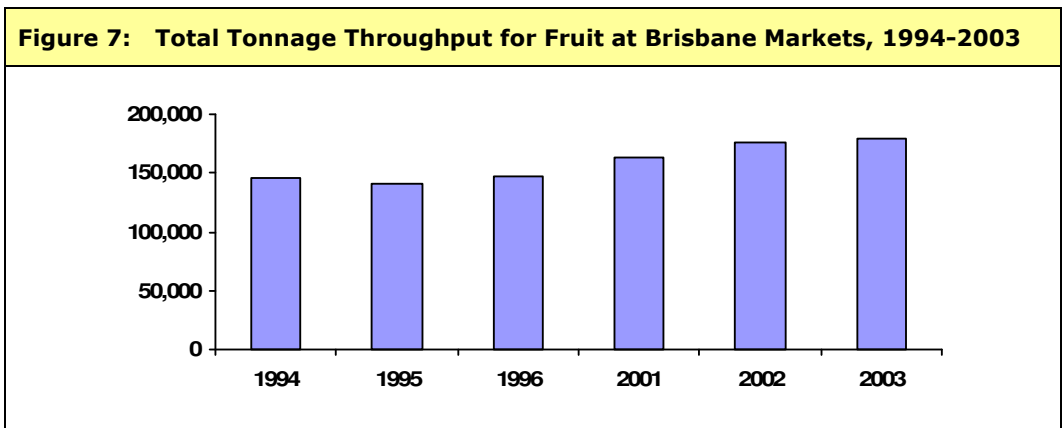
### GROWTH OR DECLINE IN CENTRAL MARKETS

There has been considerable debate over time as to whether or not the wholesaling sector is in a state of decline or not. Brisbane wholesalers point to the increasing value and throughput of the Brisbane markets over many years as the argument to say that the wholesaling sector is 'alive and well'.

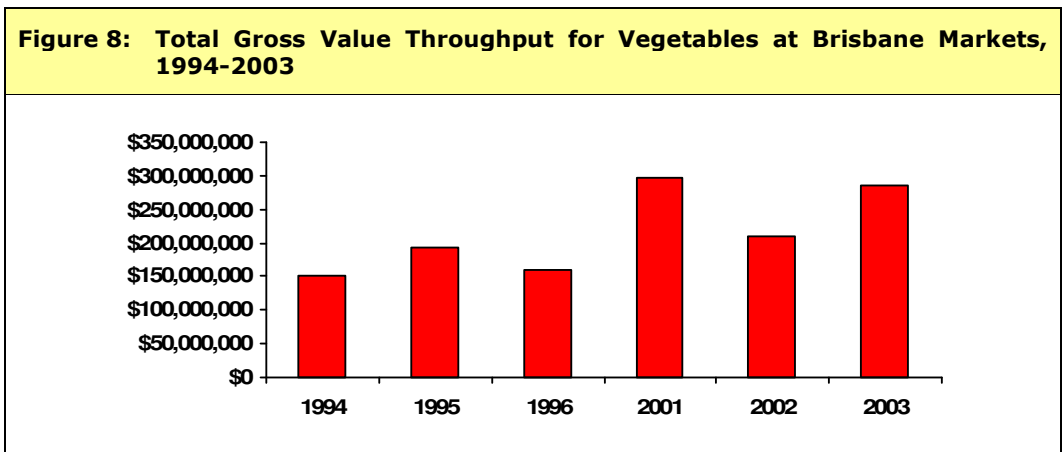
Indeed, in the period from 1994 to 2003, there has been a 23.8 per cent growth in fruit and 1.8 per cent growth in vegetable throughput through the wholesale markets. Even more spectacular in terms of growth is the value of the produce, being 89.5 per cent for fruit and 90.3 per cent for vegetables (Market Information Services, 1996 & 2004). These findings are demonstrated below in the figures below.



Source: Market Information Services, 1996 & 2004

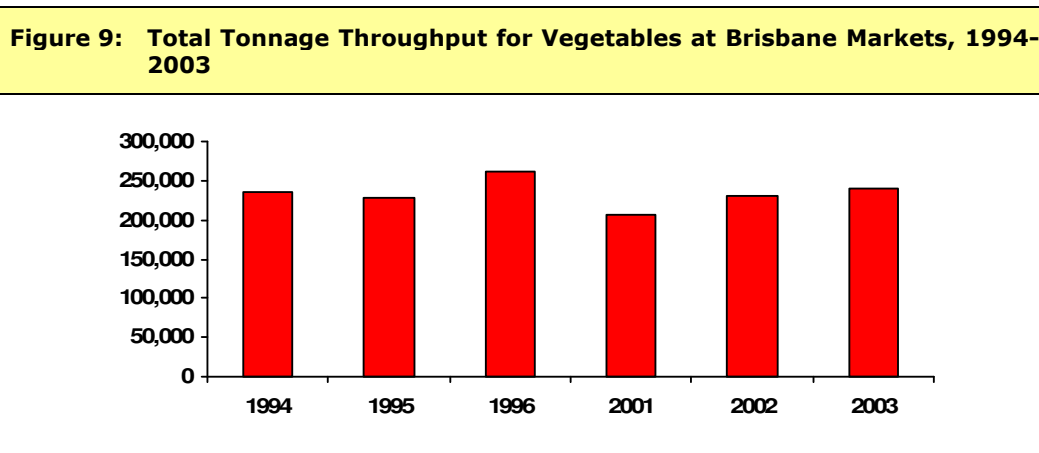


Source: Market Information Services, 1996 & 2004



Source: Market Information Services, 1996 & 2004





Source: Market Information Services, 1996 & 2004

Industry data suggests that the value growth has been driven by the following:

- Average unit value of major fruit lines such as apples, avocados, nectarines, oranges, peaches, pears, plums and watermelons have increased significantly.
- Average unit value of major vegetable lines such as carrots, cucumbers, lettuce, mushrooms, potatoes, shallots, tomatoes and zucchinis have increased significantly.
- Average volume of major fruit lines such as avocados, bananas, grapes, mandarins, nectarines, plums, strawberries and watermelons have increased significantly.
- Average volume of major vegetable lines such as capsicums, carrots, cucumbers, mushrooms, onions, shallots and zucchinis have increased significantly.

During the period 1995 to 2003, population growth across Queensland was 16.3 per cent.

Whilst the figures show there is throughput growth in the central market, others claim the sector is declining. There are a number of explanatory factors for this occurrence, including:

1. The gross unit value of produce has increased over time.
2. With the growth in the major metropolitan centres has come growth in demand for produce. Further, as evidenced in this report, the growth in annual per capita consumption of fruit in particular has increased the volume of product sold in the metropolitan markets.
3. The demise of markets in many of the regional areas, such as Rockhampton and Townsville in Queensland, has therefore forced country retailers to source product increasingly from capital cities such as Brisbane.
4. There has been a growth in the number of central receival businesses such as CS Global, IGA Distribution Centre, Simon George & Sons (providores), Moraitis Produce and a variety of exporters, all of whom receive product from the production sector, but who in many instances do not use the services of the market wholesalers to access produce.
5. For Queensland producers, Brisbane is often seen as a transit hub, i.e. produce comes in from regions west and north and then transhipped to markets further south by transportation companies whose operations are located within the markets. These figures are included in throughput statistics.
6. Retailers or retailers agents, e.g. CS Global distribution centres are increasingly being located within or close by the Brisbane market precinct. Produce to these businesses does come directly to them, by-passing the wholesaling sector. Once again these figures are included in throughput statistics.

7. Other businesses, e.g. food service, food processing and providores, have increasingly located their operations within the Brismark precinct. Where produce is supplied to them directly—which is anticipated to be a relatively small percentage of their total usage—this produce should not be included in 'wholesaler intake'.
8. The interstate trading of produce by Brisbane wholesalers is significant, particularly in regards to Queensland produce. Much of this trade is without the awareness of producers. Whilst technically 'wholesaler intake', it can be argued that the produce is not consumed in Queensland and therefore not 'truly' marketed by wholesalers to their endpoint customers.

The number of wholesalers acting in each of the major markets has shown limited if any decline in recent years. In Brisbane there are currently 54 wholesalers which is a similar number to five years ago. In Sydney the number is estimated at 120 which is about 15 fewer than five years ago.

If we use Brisbane as representative of the other wholesale markets, there has been some turnover of wholesale stands in recent years, but certainly not at any accelerated rate. The major players in terms of wholesalers remain and continue to be profitable.

### **FUTURE ROLE OF WHOLESALERS**

Historically, producer perception of wholesaler behaviour is of one where they portray asymmetric markets information and opportunistic behaviours. This has resulted in low levels of trust between producers and wholesalers, although paradoxically in many instances the development of strong relationships between the parties.

Growers see themselves as price-takers and hence possessing little market power. Historically, growers have managed their risks through diversification of their agent, retail base and types and timings of when crops were produced. They have limited access to independently verified pricing information beyond that provided by a few service providers eg. Market Information Services.

Wholesalers who do not have access to the major chains must look at developing and maintaining lasting relationships with independent retailers and independent chain store retailers. Other sectors, for example, food processing and providores will not provide a substantial and reliable enough base for most wholesaling businesses alone. Wholesalers must differentiate their businesses in such a way that they are seen as important by their customers. Examples of how wholesalers have or may seek to differentiate their businesses include: becoming a specialist in particular produce lines; integrating their services directly with a grower / grower network; handling on certain high-value produce lines; or being a marketer of small 'end-of-stock' lines from other retailers.

It is agreed by all that the wholesaler sector will have an ongoing role in the horticultural value chain, provided that the independent retail sector survives and chain store retailers continue to source at least some product from the markets. The nature of this role may however for some wholesalers depend on their perceptions and anticipation of the service needs of their customers in the future.

Some examples of these changing wholesaler roles may include the:

1. Development as **Non-Grower Consolidators**, e.g. Favco to large retail operations.
2. Development as a **Whole-of-Category Managers**, e.g. Perfection Fresh Produce to large retail operations.
3. Development of a **Packaging / Formatting Consolidator** system similar to Macks Multiples in the United Kingdom supply system, whereby a company takes product from producers and repackages it into formats desired by retail customers. In many instances they are also responsible for distribution and logistics facilitation

- to major customer groupings.
4. Development as a **Specialist Wholesaler** who does not service chain retailers but rather other customer segments, e.g. Quality Fruits.
  5. Development of a **Brokerage / Producer Chain Manager**, e.g. Harvest Fresh Company.
  6. Combinations of some of the above.

Individual wholesaling businesses will continue to be viable and valued members of the horticultural value chain if:

- They have a clear focus on the customer segment that they are servicing;
- They develop skills, systems and communication systems that enable them to be regarded as specialists in a particular market segment;
- They continue to add value to the business of their customers or develop a focus on the needs of their customer, both up and down the chain;
- They have 'quality' suppliers; and/or
- Invest in relationships / linkages down the value chain.

### **CASE STUDIES OF WHOLESALER BUSINESS RE-ENGINEERING**

A number of former wholesaling businesses have broken out of the mould of being regarded as a 'traditional' wholesaler who has many growers, with many different types of products with limited regularly ordering clientele. These businesses have sought to develop a different operational model most of which are different from one another.

Three case examples of different models that have been developed by wholesalers are presented below:

**Perfection Fresh**

Established in 1978, Perfection Fresh has grown from a Sydney Markets-based operator to a national wholesaler supplying supermarkets including Woolworths, Coles and Action, independent retailers, food processors such as Golden State Foods, and fast food chains like McDonald's.

Perfection has forged strong links with international breeders and seed companies, and has an ongoing international research effort which allows the company to identify and bring to its suppliers and customers world's best practice and produce ideas to Australia.

As Australians embrace more varied cuisines, the company has identified and developed a range of new produce varieties that each add a new facet to the dimension of home cooking, restaurant and food service menus. The company now offer over 20 branded products—many unique to Australia—and some 60 general fruit and vegetable lines.

Perfection has seven regional offices acting as local collection and dispatch depots and assist growers with product planning, quality issues, distribution and logistics management. Growers receive financial support, access to breeder and seed company research, agronomic advice, technical services, regular regional briefing meetings and field days. Perfection also offers growers the benefits of a well established customer base and secured marketing channels through direct and long term supply relationships with customers.

Perfection Fresh staff specialise in research and development, food safety and quality assurance, logistics, finance, administration, sales, customer service and marketing—allowing us to manage every aspect of the fresh fruit and vegetable supply chain.

Perfection due to the strength of its relationships with its customers, has recently become Australia's first fresh produce supplier to Woolworths to gain access to their scan data. This electronic integration will enable Perfection to develop marketing and merchandising campaigns in co-operation with their retail partner.

*Source: Perfection Fresh (2004) Simonetta (2004: pers. Comm.)*

### National Fruit Marketing Pty Ltd

National Fruit Marketing Pty Ltd (NFM), is a recently established alliance of four central market wholesalers, R.W. Pascoe Pty Ltd (Brisbane), A&H Fruit Supply (Sydney), Barkers Melbourne (Melbourne) and D&G Fresh Fruit Distributors (Adelaide). The company is seeking to provide "a national focus to building strategy supply chain partnerships, and providing critical mass and category management expertise to the retail sector". Whilst each company will maintain its own independent wholesaler operations, each partner will be able to coordinate supply to market customers and distribution points to all customers. The group argues its major benefit over brokers is that they are able to take the entire marketable crop and so provide "a one-stop-service" to retailers. Other benefits include branding through common packaging and lower transaction costs through single invoice payments.

*Source: Good & Fruit Vegetables (July, 2004)*

### Mack Multiples

Mack Multiples sources fresh fruits, salads and vegetables from over 40 countries and supplies the United Kingdom's major multiple retailers. There are currently eight business units within the division. These are Mack Bananas, Mack Soft Fruit, Mack Citrus, Mack Grape, Mack Stone Fruit, Mack Salads, Mack top fruit and Mack Vegetables.

From each of these business units their technical and commercial teams travel the world, seeking the best growers and exporters to meet their customers' demanding standards in respect of quality, consistency, food safety and value.

Produce is shipped to the United Kingdom and is either then delivered directly to their customers or, where appropriate, is ripened, selected, packaged and stored from a distribution centre in central United Kingdom. Most importantly, with the emergence of one touch retail packaging Mack assumes responsibility for co-ordinating the packaging and delivery of the produce to their customers.

Mack wholesale and service division supplies a full range of fresh and freshly-prepared fruits, vegetables and flowers to the retail and food service sectors from branches in Birmingham, Bristol, Cardiff and Southampton. Daily deliveries are effected through a comprehensive, integrated telesales and distribution network. Also within this division is Mack international, a primary importer servicing both wholesale and retail customers throughout the country.

*Source: (Alibaba.com, 2004).*

### KEYPOINTS

- The wholesale sector is presently relatively stable with few entrants into the industry.
- There are a number of structural pressures which are and will continue to impact on the future profitability of wholesalers businesses largely driven by changes in the structure of the retailing sector.
- The wholesale sector will continue to remain an integral link in the value chain although the traditional business methods, structures and arrangements will be forced to change. This will require the development of skills, systems and communication strategies not possessed by all who operate in the sector.
- There are a number of examples of how wholesaling businesses can re-engineer their business operations to better reflect the needs of their 'upstream and downstream customers.

## 4.7 Exporters

### STRUCTURE OF THE SECTOR

Australia in 2003 had approximately 2,100 companies who were registered to export produce from this country, with the majority of export activity being undertaken by less than 180 companies.

There are a number of distinct types of exporters who operate within this country. These being:

1. Exporters who have dedicated linkages to international customers. These exporters develop supply programs and may actively work with customers in developing merchandising programs. These exporters generally specialise in a limited range of products and have direct linkages with producers rather than purchasing off the market. In many instances, these suppliers deal directly with supermarkets either with or without an importer, who generally perform a distribution function.
2. Exporters who may be part of an existing wholesaler business, who may have long term overseas relationships and / or who work on the 'spot' market.
3. Exporters who operate in the spot market over an extended period. Generally they do not have linkages with retailers but rather with the overseas wholesale / importer sector. These exporters are generally smaller in nature and who generally purchase product either off the wholesale markets or directly from growers on an ad-hoc basis.
4. Opportunistic exporters are those who may be importers / exporters often from industries other than horticulture, but who see short terms opportunities to source product. These exporters generally source product from the wholesaler sector.
5. Some growers are also exporters in their own right, generally working with a importer in the country of destination. Unless a collective who can supply product over an extended period, it is unusual for a grower exporter to be a direct supply to an overseas supermarket chain. In many instances, these grower exporters have separate export divisions and may in certain instances in order to service their customers, undertake the exporting of other growers products.

### AUSTRALIA'S EXPORTING IMAGE

Australia generally has a poor image as a fruit and vegetable exporting nation.

A report completed in 2000 commissioned by Agri Chains Solutions Ltd to research how Asian buyers perceive the performance of Australian food and fibre industries concluded that:

- Buyers across all sectors, but particularly fruit and vegetables, complained about the fragmented and uncoordinated nature of our industries
- Australia's performance across key areas of importance to Asian buyers, including logistics, packaging, innovation, joint planning and market understanding was consistently below both our customers needs and our competitors performance.

The "Getting Fresh with Europe" study commissioned by the Department of Agriculture, Fisheries and Forestry (AFFA, 2000) highlighted that:

- Other southern hemisphere suppliers have a greater focus on building longer term relationships with distributors and suppliers, with less of a focus on a 'trading' mentality.
- Australia's competitors have or are developing a level of scale that is relevant to target customers, whereas as Australia is not.
- Australia's competitors are investing in the marketing end through presence and cooperative activities with customers'

- Australia's competitors are seeking to benchmark and then through continuous improvement improving all efficiency aspects of the chain'
- Australia has a lack of focus (and knowledge) of the customer and generally a predilection not to seek the information.
- Australia only has a focus on the next link in the chain.
- Australian suppliers are losing market share in Europe as southern hemisphere competitors have a clearer focus on delivering the quality, consistency and volumes required by customers.

Further, European supermarkets are continuing to develop a presence into Asia. These European supermarkets are bringing with them their current sources of supply who are more likely to be Chilean or South African than Australian. In many instances they have long term supply agreements with suppliers in place and so the report concluded that Australia might well find itself locked out of traditional export markets, without a major change of focus and commitment.

John Webster (2002) Managing Director of Horticulture Australia Ltd in an address to the 2002 Australian Agribusiness Congress (November) commented that as a global player:

1. Whilst Asian markets are growing steadily, Australia's seasonal window of opportunity is narrowing as other competitors extend their own production window. This is particularly the case with China who is rapidly becoming a net exporter of many horticultural commodities;
2. Australia's competitors have lower production costs, lower freight costs, superior quality and better organised, well funded industry funded marketing programs. This is particularly the case with the New Zealand, South African and Chilean industries.; and
3. Comparatively, Australia is disadvantaged by its lack of critical mass in a global context (RGICCC, 2003). The lack of critical mass is largely the result of its comparatively small domestic sector and a focus to view export markets in many instances as a dumping ground when 'home' markets are faced with oversupply.

Such has been the performance of the exporting sector that as a percentage of overall sales turnover in produce, exports have declined in recent years. Industry sources suggest that two years ago, horticultural exports of fresh produce were around \$600 million, with estimates for this year being as low as \$350 million.

Industry sources commented that two of Australia's leading exporters, Antico International and Southern Cross Produce, are increasingly developing a domestic focus in order to maintain sales revenue.

### **AUSTRALIA'S FUTURE DIRECTION IN EXPORTING**

The value of Australian fruit and vegetable exports has rapidly declined over the last three years. Senior industry sources placed the value of exports two years ago at \$600 million per annum, with the figure last year dropping to \$450 million and estimates for this year at around \$350 million. There are a number of external influences that have contributed to this dramatic fall, in addition to some fundamental structural issues, some of which were discussed earlier. Some of the external factors included:

- SARS crisis in Asia reducing demand.
- Continued development of China, particularly in terms of vegetables, as a major exporting powerhouse, despite some issues associated with food safety through the presence of chemical residues. Growth in Chinese supply of horticultural produce will continue to gain momentum with the adoption of western technologies.

- The intermittent opening and closing of the 'grey' supply channels to China from Hong Kong since the middle of 2003.
- Appreciation of the Australian dollar.
- Global concerns about the economy based on the Iraq war.

Of greater concern to the longer term future of exporting are some of the structural developments in the industry both within Australia and internationally. Some of these include:

- **Structure of the Australian Exporting Industry:** Australia is regarded as an ad hoc exporter to the wholesale and 'wet' market segments of 'open market' economies of such as Hong Kong and Malaysia. In effect there are many exporters competing with relatively few buyers in the marketplace. This results in customers 'playing' off one exporter with the others, with the relationship focus being price-driven. In order to compete it is often the case that exporters need to buy product brands at lower levels of quality or alternative brands. The impact of this is that customers often do not consistent or uniform brands, regular variability in quality and general dissatisfaction with the standard of relationship.
- As this market segment continues to decline in favour of more direct and long standing relationships, driven by the presence of European and European / Asian supermarket retailers, Australia's market share of these markets can be expected to continue.
- **Global Sourcing:** Australia is not regarded currently as a source of fruit and vegetables by global procurers.
- Active Fresh Produce, controlled by Noel Shields, is a global procurer on behalf of an international retail chain. An Australian, Mr Shields contends that Australia's lack of focus on long term relationships, being innovative in how they manage relationships and produce, lack of commitment, lack of scale and price competitiveness are all factors currently impacting on Australia's ability to be regarded seriously as an international or global supplier (Shields, 2004:pers. comms.).
- During the course of compiling this report a number of developments aimed at addressing this poor image were underway. However in terms of success they are largely unproven.

#### **KEYPOINTS**

- Australia is historically regarded as a poor performer across a range of desirable traits by key export customers
- The current structure of our horticultural value chain and 'culture' needs to be realigned to that of our international competitors and customers.
- The production end of our value chain needs to work more closely with the exporting and customer end of the value chain in order to supply product and service of any international standard.
- The structure of our exporting sector, with many small scale and opportunistic exporters gives Australia a poor image as an exporting nation.
- Without major structural and cultural adjustments right along the whole chain Australia will be continue to be regarded as a poor performer in international markets.
- Cost structures along the value chain will continue to impact adversely on our international competitiveness.



## IMPORTATION OF FRUIT AND VEGETABLES

The Australian government has confirmed that it will continue to pursue the removal of trade barriers, particularly so in relation to produce. The exception to this is where Australia may have issues based on quarantine matters that are allowable under WTO rules. To this end Australia currently has in excess of 50 applications in front of Biosecurity Australia seeking to import a range of fruit and vegetables.

Australian's are increasingly being offered imported produce for consumption. Navel oranges, cherries, garlic, grapes, avocados, kiwifruit and mangoes are all examples of produce currently being imported.

So why is produce being imported on what is regarded as an oversupplied market?


Most of the lines that are imported are brought into Australia in times of short or nil supply from the domestic industry. Consumers are demanded that produce is available all year round, and so the 'seasonal windows' that exist or existed are now largely under threat.

It appears that this trend will continue. For example, in New Zealand in 1991 / 92 it adopted an effectively 'open door' policy to a diverse range of fruit and vegetable products. At that time the value of consumption of produce was NZ\$450-500 million. Ten years on and the value of consumption of produce has risen to NZ\$1.1 billion, with nearly 50 per cent of that figure being imported produce (personal communication, Australian / NZ exporter / importer).

Australian retailers as well as importers are expected to continue to foster this trend in at least the short term.

It should be noted however that due to the relative small size of the Australian market (approximately 20 million people) some produce lines may not be economical to import according to some importers.

### KEYPOINTS

 **KEYPOINTS**

- Non-quarantine barriers to trade will increasingly be removed in accordance with a general worldwide trend to remove impediments to trade.
- Australian consumers will be increasingly have made available to them produce all year round and so the seasonality of many lines, particularly fruit will be reduced or removed

## 4.8 Food Service

### STRUCTURE OF THE SECTOR

The food service sector comprises companies that supplies food products to institutions, e.g. Hospitals, retirement homes, prisons, schools, restaurants, quick service restaurants (QSR), vending, catering companies and hotels. Few if any of these companies source produce direct from growers and in many instances use an intermediaries to source from the wholesale markets, the principal supply source.

Companies such as Simon George and Sons in Queensland who act as fresh produce providores who have operations close to the central markets are a good example of the type of businesses who supply this sector.

Providores may undertake minimal processing of the product prior to delivery, i.e. cutting, portion control, to the companies who supply the prepared food to consumers.

Food processors / value-adders supply a more finished product to the customers in this sector.

### **DRIVERS OF THE SECTOR**

Industry sources suggest that approximately 30 to 40 per cent of the main meals consumed in the household each day are supplied by the food service sector. There are two major segments, restaurants (higher cost / higher 'quality' / longer consumption times) and quick service restaurants (QSR) such as McDonalds, KFC and Pizza Hut.

In Europe this sector has a more dominant role, with estimates that closer to 50 per cent of the main meals being consumed away from home, with a slightly higher figure for the United States. It is anticipated that growth in this sector whilst slowing will be the dominant 'food consumption' sector in Europe and United States in coming decades. In Asia, the percentage of food service varies considerably with lower percentages in lesser developed countries and higher in more developed economies.

So what is driving the growth of this sector? There are many all directly linked to consumer behaviour. Some of these drivers include:


1. Consumers demand for an increasing range of offer of meal solutions. Consumers are less satisfied with the traditional 'meat and three vegetables' diets of yesteryear.
2. Increasing diversity of culture and ethnic mix of our society resulting in a greater exposure to various traditional meals from other countries. Only a few decades ago, beyond 'Chinese food' there was little else for consumers to access.
3. A reduced focus on the consumption of food (in some cultures) as a social event with more of focus on it simply being a fuel.
4. Time spent preparing meals have declined from an average of close to one hour 20 years ago, to less than 20 minutes currently with predictions for it to fall further to eight minutes in the coming decade. This has been driven by the increased level of outside of work activities that people engage in and longer work hours.
5. Social structure. With the advent of singular families and double income relationships consumers are either less likely to prepare 'at home' meals or do not have the time to do so.
6. Convenience marketing. Many of the QSR companies have significant promotional budgets aimed specifically at particular customer segments promoting a variety of issues mostly focused around convenience and promotion of an enjoyable eating experience.
7. Home Design. Some new homes particularly inner city departments increasingly do not have a 'traditional' kitchen attached to them. Microwaves are tending to replace ovens in these types of developments, so 'driving' these residents to consume main meals outside of the home.
8. Increasing focus on health. The QSR sector is becoming increasingly responsive to the desire by Australian consumers for healthy alternatives even in franchises that previously may not have adopted such an approach, e.g. McDonalds. In part this has been driven by the desire to develop 'whole of family appeal'. For instance, with a wider range of offers ranging from healthy to less so, each member of the family unit (particularly parents) can buy food to meet their individual consumption needs.
9. Mass customisation. Consumers through their desire to have meal solutions 'tailor made' are driving the food service sector to provide a wider range of offer which can be 'mixed and matched'.

All of the developments discussed above, can be regarded, as more or less common across all more developed economies. However, by many are considered to have a more mature restaurant sector with Australians well accustomed to seeing them as their preferred

alternative to eating at home. This can be attributed to a number of factors including the relatively slow penetration of QSR into Australia, access to good quality, locally produced food products (meat, fish and produce) and excellent climate making 'going out' for meals more convivial.

Industry sources in Australia consider that the speed of growth of the food service sector is declining and may not reach the levels of that in the United States and Europe.

**KEYPOINTS**

 **KEYPOINTS**

- More meals will be consumed away from the home in addition to more meals that are consumed in the home requiring less and less time to prepare
- Consumers are increasingly focusing on variety in meal selection
- A new emerging category are 'healthy' fast food alternatives
- A move away from traditional at home consumption will severely impact on the fruit and vegetable specialist retailers. Those retailers who are able to offer a variety of meal solutions may acquire greater shares of the consumer dollar.

**4.9 On-line Fruit & Vegetable Purchasing**

On-line or internet purchasing of fruit and vegetables only has a limited share of the consumer market. Sydney, Melbourne and to a lesser extent Brisbane are the major centres from on-line purchasing occurs.

Companies that run on-line businesses contend that for them the business has considerable upside, as produce is paid for in advance and stock inventory turns over every day (sales perfectly match purchases). The benefits to consumers are seen to be that produce is fresh daily and due to the lack of need for high cost warehousing may be less expensive. Conversely, the transportation costs are seen to add to the costs of goods.

Industry sources suggested that on-line purchasing of fruit and vegetables only account for 1-2 per cent of the total market. Growth is currently static. It is thought that the lack of a culture to purchase on-line is due to the historical purchase preferences for consumers, in addition to the fact that consumers in Australia find it easy to transport goods home from retail stores and generally combine other activities with food shopping.

## 5.0 CURRENT PRACTICES IN THE MARKET PLACE

The horticultural value chain is changing rapidly, more so than in decades past. Due to their close relationship with consumers, retailers are increasingly the arbiters of change. Those businesses that are not prepared to accommodate changes by initiators / pioneers will no doubt face viability issues in the future.

In the past, the horticultural chain was supply-driven. Producers produced and were able to sell at a profit. Today, chains are increasingly being demand-driven with consumers being in the box seat. As discussed in Section 2.1, consumers are driving change down the chain and those producers who are not prepared to understand the needs of consumers and make changes within their businesses will be at a disadvantage to those who will.

Retailers and food service as the link providers between consumers and the rest of the chain need to be totally aware of and are dependant on the consumer to be successful. Without consumers they do not have a business. Therefore in order to protect and enhance their position retailers and food service operators will increasingly seek to drive change down the chain.

### 5.1 Chain Reversal and Chain Shortening

In Australia the transition from supply to demand-driven chains is evolving rapidly. This chain reversal combined with the presence of relatively few players in the retail sector and many players at the production end is seen by producers as placing them in a position of weakness in terms of negotiation ability and at risk in terms of long term survival.

This section, amongst other issues, examines the current business practices that are occurring across the value chain. It will seek to identify how these practices are impacting on producers and to develop a range of possible measures in combination with the other sectors that will enhance the viability of the production sector.

### 5.2 Transaction Types Between Producers

Queensland producers do not have a high level of commercial relationships between one another. The exceptions to this are where:

1. A producer purchases produce at the shed door for subsequent re-packing and marketing, generally not under their own brand. This is most common in the citrus and pome fruit industries in southern Australia, but less common in Queensland.

Produce is generally sold on 'spec', that is by private negotiation on the day between the grower and packhouse. Generally the product is sold in bulk 'all in', that is all for all product in the bin.

2. Another producer contract packs for a grower on a contract fee basis. The packer may also market the produce on behalf of the grower. Generally the product is packed in the brand of the contracting grower.

Contract growers may or may not receive a portion of the returns from the sale of non-packed fruit which is then generally sold to processors.

3. A grower consolidator has a network of growers who supply them under a variety of arrangements.

In terms of supply, the majority of grower consolidators contract growers to have planted a set area of land. Consolidators will also specify the time for the crop to be planted as well as the variety. The consolidator may or may not specify the production method that is to be used, provide agronomic support across the life of the crop, undertake major cultural operations (mainly planting and spraying) or harvest the crop.

4. Growers form alliances through co-operatives or marketing groups. The nature of the relationship is generally governed by the supply and marketing of produce, but may in some instances extend to inputs such as cartons and fertilisers.

Growers who are involved in consolidation models are paid on the following basis:

- A set return per volume, either harvested or packed.
- A set return per area.

Bonuses may or may not be paid on crops that perform above a certain set of pre-agreed standards.

Grower consolidators may deduct costs / charges based on the level of activity that they undertake.

The advantages of this form of production system to growers are that in certain instances they have lower level of capital investment, less time spent in packing operations, lower levels of compliance administration and business management and most importantly 'access' to a market which they may otherwise not have had (due to their size or negotiation skills). Whilst there is a lower level of overall risk to the enterprise, as the grower consolidator takes most of the price risk (in most situations), average returns on this basis are therefore generally lower to the consolidator member. Returns are however generally subject to less price volatility.

**KEYPOINTS**

**KEYPOINTS**

- There are 4 major types of relationships existing between producers:
  1. Contract packing and in some instances marketing
  2. Sale of produce for repacking by other producers for subsequent resale
  3. Supply of produce under a variety of transaction arrangements to producer consolidators.
  4. Horizontal or group alliances of producers

**5.3 Transaction Types Between Producers and Wholesalers, Processors and Brokers**

**BACKGROUND**

The basis of the transaction process and the establishment of price settling mechanisms has been a subject of discussion and debate between the production and the remainder of the value chain for decades.

In particular, how producers and wholesalers establish price, and rights and obligations of the parties in the establishment of terms of trade has been the subject of two independent reviews since 1998 (the Baird Review and Buck Review).

Both of these reviews recommended a revised mandatory and enforceable code of conduct for the horticultural industry. On both occasions the Federal government whilst accepting the majority of the recommendations would not legislate the implementation of an enforceable code of conduct.

Since late 2003 the Horticultural Australia Council (HAC) which comprises the majority of producer industry organisations, formulated a proposal called the Horticulture Business Code, which in its opinion sought to provide fair terms of trade between growers and others in the value chain based on 21 recommendations.

In August, 2004 the Federal Minister for Small Business Joe Hockey undertook to attempt to broker a solution between producers and in particular the Australian Chamber of Fruit & Vegetable Industries, for the development of a mutually agreed terms of trade.

Negotiations between the ACFVI (representing wholesalers) and the National Farmers Federation (NFF) and HAC in late September saw agreement on 19 or the 21 principles for trading but still failed to gain consensus on two important issues focussed around the basis of agent and merchant transactions.

Following this meeting and the inability to gain consensus on all of the issues raised, the Federal Government on the 4<sup>th</sup> October, announced that within the first 100 days following the election that it would introduce a mandatory Code of Conduct.

Therefore in discussing the various transaction processes that can exist between producers and others in the value chain, it must be noted that they may be subject to change depending on the final outcomes associated with the recommendations of the Horticultural Business Code.

Details of the Horticultural Business Code and areas where there still exists disagreement between producers and wholesalers is provided at Appendix A.

## **TRANSACTION TYPES**

Horticultural producers sell produce to others in the value chain under four different marketing 'arrangements'. These are:

1. Merchant transaction
2. Agency transaction
3. Broker transaction
4. Agreed price setting mechanism, e.g. fixed price, agreed price one week in advance, negotiated price within a maximum and minimum limit.

Each of these arrangements have certain rights obligations into how each party to the transaction must behave commercially. Further, the predominant transaction method varies depending on to whom the producer sells their produce.

For wholesalers, the principal transaction types with growers are merchant, agency or 'perceived' agency transactions. Brokerage transactions are not regularly used by wholesalers, rather they are left to 'specialist' brokers.

Broker transactions are generated by brokers who either sell to wholesalers, direct to retailers or to processors.

The fourth transaction type is predominately used by the processing sector and where there are direct supply linkages to large retailers or the organisation charged with facilitating supply and price negotiation on their behalf.

As discussed in the section above there are ongoing discussions about the nature of the transaction process as it applies to agency and merchant transactions. If the Horticultural Business Code is adopted, the impacts that it will have on the nature of the transactions are detailed in Table 5 and Table 6 below. The other two transaction bases, brokerage and 'fixed price setting mechanisms' are described in Table 7.

<b>Table 5: Agency Transactions – Current Practice and That Proposed by Horticultural Business Code</b>		
<b>Item</b>	<b>Agency (Current)</b>	<b>Agency Transaction (Horticultural Business Code)</b>
Title in Produce	Remain with producer until produce is sold to the buyer.	Remain with producer until produce is sold to the buyer.
Price Returned	Gross sales price less commission and prescribed charge, e.g. Unloading, ripening fees.	Gross sales price less commission and prescribed charge, e.g. Unloading, ripening fees.
Agreements Allowable	Not able to change basis of agreement unless agreed in writing	Not able to change basis of agreement unless agreed in writing. In the absence of an agreement standard terms will apply.
Contractable	Terms of agreement normally negotiated but not necessarily subject in practice to a formal agreement.	Every transaction that is not subject to an agreement will be regarded as an agency agreement. If contracted terms of agreement will define the nature of the transaction.
Payment Period	Normally around 15 working days from date of sell of produce	Normally around 15 working days from date of sell of produce
Documentation	Account sale docket	Account sale docket
Maximum Commission (Deduction)	Subject to negotiation	Subject to negotiations but in the absence of a contract will be subject to a maximum rate.
Transaction GST Applicable	Yes. Currently rarely paid by wholesalers	Yes
Apparent Price Transparency	High	High

<b>Table 6 Merchant Transactions – Current Practice and That Proposed by Horticultural Business Code</b>		
<b>Item</b>	<b>Merchant (Current)</b>	<b>Merchant Transaction (Horticultural Business Code)</b>
Title in Produce	Generally passes to seller when price negotiated and agreed or on delivery whichever is the latter	Merchant buys produce from the supplier for a price agreed in writing prior to despatch of the produce conditional on it meeting agreed specifications. Ownership passes to the merchant on receipt.
Price Returned	Price negotiated between grower and seller, which may or may not be confirmed in writing	Price subject to agreement in writing
Agreements Allowable	Are able to extend time to negotiate prices, time to pay and delivery conditions	Agreements subject to negotiated written agreements between producer and wholesaler. Standard terms will exist. If no agreement exists between parties, the transaction automatically becomes an agency transaction.
Contractable	Terms of agreement normally negotiated but not necessarily subject in practice to a formal agreement	Must be subject to an agreement otherwise will be an agency transaction.
Payment Period	Normally around 10 working days from price negotiation or by agreement	Normally around 10 working days from price negotiation or by agreement.
Documentation	Purchase memorandum note or payment advice	Purchase memorandum note or payment advice
Maximum Commission (Deduction)	Does not have to be disclosed	Does not have to be disclosed
Transaction GST Applicable	No	No

<b>Table 6 Merchant Transactions – Current Practice and That Proposed by Horticultural Business Code</b>		
<b>Item</b>	<b>Merchant (Current)</b>	<b>Merchant Transaction (Horticultural Business Code)</b>
Apparent Price Transparency	Low (generally)	Low (generally)

<b>Table 7: Other Price Transaction Types</b>		
<b>Item</b>	<b>Broker</b>	<b>Agreed Price Setting Mechanism</b>
Title in Produce	Generally passes to the seller when price negotiated or on delivery whichever is the latter	Generally passes to the buyer when produce is accepted by the buyer
Price Returned	Gross sales prices less brokerage fees and deductions for agreed prices	Variable price setting mechanisms. May be contracted price for a period i.e. 1 week, 1 month, whole of season or price negotiated based on market price OR negotiated price within a maximum and minimum price level OR combination of the above
Agreements Allowable	Not able to change basis of agreement	Subject to specific contents of contract
Contractable	Terms of agreement normally negotiated but not necessarily subject in practice to a formal agreement. However more formal agreements are struck with merchant transactions	Terms of agreement are negotiated and agreed to in writing
Payment Period	Normally within 15 working days of sale of produce	Subject to agreement
Documentation	Account sale docket	Purchase memorandum note or payment advice
Maximum Commission (Deduction)	Subject to negotiation	Does not have to be disclosed
Transaction GST Applicable	Yes	No
Apparent Price Transparency	High (generally)	Total

**KEYPOINTS**

**KEYPOINTS**

- There are five types of transactions relationships between producers and intermediate transactors in the supply chain:
  1. Agency
  2. Merchant
  3. Brokerage
  4. Agreed Prices (in advance)
  5. A 'mixture' or 'hybrid' of agency and merchant transactions
- In terms of numbers of transactions, merchant and mixture / hybrid types are the predominant ones.



- GST by law should be paid on agency or brokerage transactions. Particularly in respect of agency transactions this frequently does not occur.
- There are currently considerable industry discussions pertaining to a redefining of the terms of trade between producers and wholesalers in particular with the potential for an enforceable code of conducts and terms of trade being legislated.

#### 5.4 *Producer / Wholesaler Relationships*

It has been quoted widely that the production sector is often dissatisfied with the price transparency that the wholesaler provides to producers. Other issues such as the basis of transactions, payment terms and produce returns have also been raised as issues of concern by producers. In reply, Brismark (the representative body of Brisbane wholesalers) argue that the number of disputations between producers and wholesalers are relatively low, so therefore the mechanism is working well. Section 5.2 outlines a number of reasons why the producer sector may be disinclined to seek remedy to a disputes committee, such as has been established by Brismark and also by the Retail Grocery Industry Ombudsman (RGIO).

It has been noted in a number of cases wholesalers and brokers are providing price transparency through the use of on-line systems. This allows producers the ability to see what produce is sold for and, in some instances, to whom.

If as an industry, price transparency, is a key element to the success of the relationship, wholesalers who take such actions should be acknowledged and supported by the supplier sector.

In discussions with wholesalers it is apparent that the number of 'true' agency transactions whereby each consignment has the same percentage of commission deducted from each transaction are few. Wholesalers may indicate on their price returns that the produce has been sold on an agency basis, e.g. gross sale = \$15.00 less commission of 15% or \$2.25 = Net return of \$12.75, but in effect it is a merchant transaction with the produce being sold for a higher or lower price. Industry discussions also highlighted that wholesalers virtually without exception are not accounting for GST which they would by law have to do if the transaction was agency based.

In effect this describes a fifth transaction type used by wholesalers which is a hybrid merchant / agency transaction.

There is often confusion regarding the 'transaction basis' that a relationship is to be governed by, that is agency or merchant transaction. This is primarily due to the fact that there are few examples of the use of formal agreements detailing the nature, type and rules of conduct associated with the grower / wholesaler transaction. This situation will change if the Horticultural Business Code is implemented over the coming months.

The wholesale sector is still the major channel that produce is marketed through in Australia. It is also the channel that is subject to as an industry the highest level of mistrust, misunderstanding and lack of a combined focus of any other sector in the horticultural chain. Notwithstanding this, there are a considerable number of producers and wholesalers who enjoy excellent relationships.

Some of the reasons given by industry for the variability in the level of satisfaction with grower and wholesaler relationships can be summarised as:

- Business Skills:** Most growers and wholesalers are not actively working together to grow the market of the other. The basis of most relationships is generally price and price alone. Growers frequently argue that the price is not good enough, where as in fact the evidence shows that they in most instances do not really know if the price is satisfactory because they do not know how much it cost them to produce, pack and transport in the first place. Farmers are regarded as variable in terms of financial management skills, which is both surprising and concerning, as frequently the

business operation has relatively high turnovers. In general, like-sized businesses outside of agriculture have an excellent appreciation of the costs of doing business and an active process associated with seeking how to remove or reduce such costs.

An issue raised by some wholesalers is that they do not have an accurate picture of what it costs a grower to produce a crop. For instance, one grower may say it costs them \$8 to land a tray of mangoes on a grower's floor, whilst the next says it will cost them \$12 to produce a similar quality of product. Whilst scale economies and business management practices would state that there will be variability in the costs of production the fact that is a lack of benchmarked or collated industry information is seen as a major weakness.

**Business Practices:** Some and possibly many producers and wholesalers, have been guilty of unconscionable conduct. Incorrect size and quality marking of cartons, putting poor quality produce on the bottom of pallets, are all practices that have all occurred to wholesalers at some stage of their careers. The ability to trust their supplier is important to a wholesaler, as it gives them greater confidence in the selling of a grower's product, in addition to reducing their costs of ensuring compliance and checking. Conversely, some wholesalers have been exposed as keeping "double books", providing misleading market intelligence, suggesting produce does not meet an acceptable standard when in fact it does. Each of these business practices should be regarded as misleading and dishonest. The respective parties will argue that the other one 'deserves it' or similar. The fact of the matter is that increasingly in today's world of modern communication it will be less possible for both producers and wholesalers to engage in such activities. Further it will not be tolerated by customers further up the chain.

As will be discussed later in this report, there are a number of mechanisms that could be introduced that will have reduce the incidence of such behaviour over time.


**Communication Skills:** Many business organisations today outside of agriculture, invest considerable time and expense, in developing their expertise into how to deal with and communicate with customers. The level of this investment in horticulture is low by comparison. Whilst many producers will question the value of such investment, the fact that many organisations do so, suggests its value. A similar proposition regarding low level of communication skills training is also arguable for wholesalers.

**Investing Time in the Relationship:** As discussed previously, many producer – wholesaler relationships are focused on price as the arbiter of a successful relationship. Growers who claim to have an excellent relationship with their wholesaler, often do so, based on the fact that each party has invested time in developing an understanding of each others business often extending to a more personal level. It is unrealistic to expect that every wholesaler will be able to develop a close relationship with every grower, the fact is that as a general issue it needs to be considered. Intrinsically, aligned with the relationship investment are the development of improved communication skills amongst each sector.

**Distance:** Producers and wholesalers are often separated by considerable distances, when if in combination with some or all of the issues above makes the development of a close business and personal relationships difficult.

**Role of Industry Organisations:** Industry organisations are charged with the responsibility of progressing the interest of their members. Unfortunately, in some instances it is the vocal minority, many of whom have 'radical' views who drive industry organisation communications often to the detriment of relationships with other industry chain organisations. In horticulture there appears as a general rule to be a high degree of animosity particularly between producer and wholesaler organisations. This lack of 'leadership' from the top is then often translated or filtered down to the actions of the 'rank and file'.

**KEYPOINTS**

 **KEYPOINTS**

- The key impediments seen by industry impacting on the level of success of business relationships between producers and wholesalers are:
  1. Business Skills
  2. Business Practices
  3. Communication Skills
  4. Investing time in relationships
  5. Distance
  6. Role of industry organisations.

**5.5 Producer / Processor Relationships**

Queensland has a number of processing entities which range in size from conglomerates such as Golden Circle to small family owned enterprises supplying a range of food service and ingredient manufacturers. Most growers supply processors on a seasonal agreed price per volume based on an agreed set of quality parameters (i.e. size, weight, quality, colour, level of defect). Volume contracts / agreements are used but are dependant on the nature of the relationship. For larger processors volume agreements are frequently used (i.e. Golden Circle, Golden State Foods – GSF, Harvest Fresh Cuts).

In most instances, processors receive product that is not to suitable for the fresh produce market. There are a limited number of growers who grow specifically for a processor, except in the case of Golden Circle (for a number of lines, most importantly pineapple) and Harvest Fresh Cuts. In both these instances the processor has an active involvement in breed / variety selection, production extension and logistics.

Most processors set pricing benchmarks to growers based on end price received less margin and manufacturing and transportation costs. Growers have little or no input, with the one or two possible exceptions, in regards to pricing. In fact many growers see processing contracts as a means to recover harvesting and packaging costs and overheads, and not an income stream worthy of significant investment.

Due to the competitive nature of food processing, particularly to commodities that are internationally traded, e.g. juices, purees, dried and some frozen products, there is limited scope for price improvements to producers over time. As a consequence it is unlikely in future that growers will be in a position to grow crops solely for processors.

Whilst the emergence of nutraceuticals and other ‘health extracts’ may be able to provide some short term income benefits to producers as they develop it is likely that the benefits of ‘first to market’ products such as these will be very long.

**5.6 Producer / Retailer Relationships**

As the level of direct trade between producers and retailers increases over time so will the need of the production sector need to develop the skills and awareness of how to do business with the retail sector.

Presently, relationships between producers and retailers are at three levels:

1. **Ad Hoc Direct Purchasing.** Although declining regional buying officers often purchase a proportion of their produce from growers on an ad hoc basis. This is generally done in order to “top up” supermarket supply due to short deliveries from contracted producers or higher than expected demand.

Prices are generally negotiated on a ‘day price’ with an agreed volume of produce complying with an agreed size and / or quality specification. Generally the price negotiated is “shed door” and normally matches somewhere between the gross sale price and the gross sale price less commission.

2. **Contract Purchasing / Supply Agreements.** Emerging more and more, contract purchasing / supply agreements whereby growers / consolidators negotiate to supply an agreed volume of a certain product quality specification.

There is a variety of pricing mechanisms used ranging from weekly in advance, maximum and minimum price ranges and less often used whole-of-season or segment-of-season pricing. Further, in some instances there may be a mixture of some or all of the above for different proportions of the crop.

In most instances under these agreements, the grower is responsible for facilitating the movement of the produce to an agreed location.

With the emergence of consolidation networks, some chain retailers with some product groupings have advocated the supply and logistics to these players. In effect, following negotiations and agreement, these consolidation networks are then responsible for “**supply management**” on behalf of the retailer.

3. **Category Management:** Only just emerging in Australia are where non-retailers through consolidation networks are being given the responsibility of undertaking category management on behalf of the retailers. A category manager is an extension of a supply manager, who undertakes to take responsibility for the merchandising, development of promotion and marketing material, placement and rotation of stock, receipt, analysis and interpretation of scan data. This concept is well advanced in the FMCG category, but less so in produce possibly due to the skills needed to achieve this, the perishable nature of most produce and the relatively large number of lines. Companies such as Perfection Fresh, is an example of a company who has assumed category management responsibilities on behalf of a major supplier.

## PRICE SETTING AT THE RETAIL LEVEL

This study was not able to test a number of theories put forward by the production sector that retail margins are excessive in comparison to the costs or profits that producers receive.

This subject has caused considerable debate amongst all elements of the value chain and so it is recommended that a detailed whole-of-chain margin analysis across a broad range of fruit and vegetables should be conducted, in partnership, with the various levels of the retail sectors and other participants in the sector be conducted.

Mechanisms or actions such as this will then allow an informed debate between value chain members, industry organisations, government and consumer organisations. It will also go some way, hopefully, to rebuilding the ties between some elements of the value chain who have become disenchanted or disenfranchised with those in the retail level.

A number of those producer businesses that deal directly with retailers have indicated a general level of satisfaction with the nature and conduct of the relationship. Some have indicated the “tough but fair” tag may be applicable.

However in discussions with various members of the supply chain a number of observations were made that included:

- Woolworths have for the last two decades been the ‘leader’ in terms of formulating price policy, which other organisations have by and large followed.

- In the early 1990's Woolworths instituted a revised pricing mechanism whereby both individual stores and distribution centres (DC's) were responsible for delivery profits, whereby previous DC's were cost negative / neutral. The impact of this was that overall profitability to the 'Fresh Food People' from produce was improved due to the development of an extra 'revenue centre'. As other retailers followed Woolworths' pricing policy, overall margins to the chain store retail sector increased, consumers paid relatively higher prices, with in most instances no net change to grower margins.
- Individual retail operations, particularly where they are co-located in the same premises, are followers rather than leaders in respect to pricing policy. Although there is a high degree of variability associated with profitability of individual retailers, one wholesaler / retailer commented that the last decade has been a "golden age" for highly professional, well positioned individual fruit shops. The belief being that the general view that 'good' retailers are better able to present their offer, have lower levels of wastage, finer attention to detail in regards to accessing high quality produce, lower operational costs (as many use their own labour) and better quality of produce to offer.

Those consulted expressed the belief that chain store retailers are about to enter a new era in price competition. The drivers to this being:

- Coles belief that increased market share of total operations can be driven by increased competitiveness at the fresh produce section.
- Coles having developed a 'formula' to better meet the needs of its customers, which will drive Woolworths to become more competitive.
- Introduction of new retail players, such as Aldi and possibly others.
- A recognition that by driving the attainment of cost efficiencies through supply rationalisation, development of new retailing formats, logistics and distribution efficiencies, that they can cut costs to the customer whilst maintaining margins.
- The impact of this new era of price competition at the chain store retail level will be that smaller retailers will be faced with increasing levels of competition, with threats to overall profitability. In the eyes of some respondents this may result in further rationalisation of this sector.
- Some non-chain store retailers believe there has been an increased focus by this sector to 'fix' retail prices at the individual store level. This is built on the belief that consumers do not wish to see extreme fluctuations in price movements associated with 'staple' lines, e.g. apples, oranges, tomatoes etc. Whilst prices for these types of products do move with the general trend of the market, they do not respond as 'elastically' as to what is occurring at the wholesale level. Retailers then receive varying margins week to week, which they can absorb. Individual retailers have to be careful with price policy as what they pay is tied to the wholesale price.
- Few retailers are providing Point-of-Sale data, but even access to inventory information and ordering requirements represents a significant improvement for a horticultural producer who previously had no knowledge of the quantity required on the day. The relationship ensures immediate feedback on a holding quality and presentation and feedback is more likely to be consistent when it comes from a category manager for a major chain.

#### **KEYPOINTS**

- Retailers and producers have 3 basic transaction types under which they have currently conduct business

##### **1. Ad Hoc Direct Purchase**

**2. Contract Purchasing / Supply Agreements****3. Category Management**

- The development of retail pricing strategies has in the past been largely driven by the Woolworths model, although there is a wide variety of pricing policies followed by both smaller and larger retailers.
- There is an increasing focus by chain retailers on cost minimization activities as a mechanism to maximize revenue growth.

**5.7 Retail Codes of Conduct****BAIRD REVIEW OF THE GROCERY INDUSTRY CODE OF CONDUCT**

In December 1998, the Federal government established a Joint Select Committee on the Retailing Sector to inquire into and report on the degree of market concentration in the retailing sectors, the impact that the concentration had on the competitiveness of smaller revenues and to develop recommendations pertaining to any perceived failures. The report entitled "Fair Market or Market Failure" was released in August 1999 and has since become known as the Baird Report (Commonwealth of Australia, 1999).

The central recommendation from the review was for the development of a Retail Industry Code of Conduct by the ACCC which was mandatory and had enforceability. It was further recommended that the development of a code be extended to relationships beyond just the retailer-supplier base and would, by definition, include the entire horticultural production chain.

The Government, however, at the time did not support the mandatory establishment of the Code and agreed rather to the establishment of a voluntary code with the retention of an ombudsman to administer a dispute resolutions process.

As a consequence the Retail Grocery Industry Code of Conduct Committee was established in February 2000. The committee was heavily retail focused with only one representative from the National Farmers Federation representing producers (and not specifically horticultural) interests.

**RETAIL GROCERY INDUSTRY OMBUDSMAN**

The Retail Grocery Industry Ombudsman (RGIO) has three objectives:

- Promote fair and equitable trading practices amongst industry participants.
- Encourage fair play and open communication between industry participants as a means of avoiding disputes.
- Provide a simple, accessible and non-legalistic dispute resolution mechanism for industry participants in the event of a dispute.

The code is voluntary and is therefore not enforceable under the Trade Practices Act.

The level of usage of the RGIO by the production sector has been low. The reasons for this have been:

1. Lack of awareness. This is in part a producer related issue as this sector do not actively seek out and take up information, unless in many instances there is a compulsion to do so.

2. History. Producers have in the past either conceded it is difficult or not likely to get a just outcome due to previous experiences when disputes with various parties have arisen.
3. The voluntary nature of the Code suggests to producers that it will be too difficult to obtain a fair decision.
4. Fear of retribution whether perceived or actual.
5. Lack of support for the code from the wholesaler sector.
6. Time availability, once again whether perceived or actual, relates to the fact that many producers would rather concentrate on-farm activities rather than go into an arena in which they have discomfort.
7. Pride. Producers are often reluctant to publicise the fact that they may have made a 'mistake' and so may 'sweep problems under the carpet', rather than air them publicly, even though the resolution process is confidential.

Given these issues it is not likely in its current form that the RGIO will receive a high level of support. There are a number of mechanisms which need to be put into place, prior to the RGIO or any other similar dispute resolutions process will be successful.

#### **BUCK REVIEW OF THE RETAIL GROCERY INDUSTRY CODE OF CONDUCT**

The Buck Review of the Retail Grocery Industry Code of Conduct ("The Code") is the first review of the Code since its inception in 1999 following the Baird Review. The review was completed in December 2003 but only released publicly in July 2004.

The Review highlighted that there was wide spread discontent with the performance of the Code's performance in terms of addressing:

1. The transparency and nature of the relationships between market participants (particularly those between producers and wholesalers)
2. Contractual issues
3. Produce and product standards.

In consideration of those areas of discontent the major issues highlighted to the review were:

- The nature of the business relationship between the parties;
- The timing of transfer of ownership of the product or produce;
- The role of market wholesaler or intermediary;
- Appropriate levels of intermediary commission;
- Disclosure of commissions;
- Calculation of commissions;
- Quality of produce sent to the markets by producers and timing of its delivery, particularly in the case of goods sent without prior arrangements;
- The rights of growers to inspect the trail of the produce from the farm gate to ultimate sale;
- The rights of retailers to return produce after accepting delivery;

- Fitness for purpose and the responsibility for ownership of produce determine to be not fit for purpose;
- The power of major retailers, processors and packing in negotiating contracts with producers;
- Claims of actual or perceived retribution if complaints are made or in some cases if written agreements are sought; and,
- Perceptions that complaints are made only be inefficient businesses.

The review made a number of recommendations to the Minister including:

1. That the government take steps to implement a principles-based Code of Conduct underpinned by regulation to replace the existing Code.
2. The principle based code covers businesses involved in the production, preparation and sale of food, beverages and non-food grocery items.
3. This is the key recommendation of the review in that it asks the government to set in place enforceable legislation associated with the way that the horticultural value chain and others do business.
4. That the Code principles include requirements for written documentation which covers all elements associated with a business relationship between two parties, including remedies for action in the event of a dispute. These elements include definition of parties to an agreement, nature of the commercial relationship, basis of supply, product quality assessment, pricing issues and dispute resolution.
5. The Code should apply the dispute resolution model used in the Mandatory Franchising Code.
6. That the value chain continue to develop the Codes of Practice so as to be as far reaching and relevant as possible to all participants.
7. That industry participants, no matter their size, be given practical compliance education to reduce the likelihood and incidence of breaches to fair trading and anti-trust laws.
8. Major players be encouraged to review their trade practices compliance arrangements.
9. That the ACCC with the Office of Small Business prepare and publish a guide to Code compliance including procedures, training materials and an indication of expectations.
10. That a strategic plan be developed with appropriate resources allocated to guide the awareness and develop a promotional strategy for the Code.
11. That the Code be independently reviewed every three years.
12. That the ACCC consider carefully certain retail ownership, branding and acquisition issues.

#### **RESPONSE TO REVIEW BY THE FEDERAL GOVERNMENT**

On 1 July 2004, the Federal government provided its response to the "Buck Report".

The Government contended it agreed with the "majority of industry" that the key recommendation of the report—the implementation of a 'principles-based Code underpinned by regulation'—was not appropriate at this time (Commonwealth of Australia, 2004).



The Government did accept a number of recommendations which focus around fine tuning the existing voluntary Code, education of the value chain about its existence, ongoing funding of the RGICAC and mediation services.

However as discussed previously on the 4<sup>th</sup> October, the Federal Government has changed its policy in respect of implementing an enforceable code of conduct and has confirmed to industry that within 100 days of the new parliamentary terms following the 9<sup>th</sup> October election it will implement a Code of Conduct and agreed definitions pertaining to the Terms of Trade between producers and others in the value chain.

The Horticulture Australia Council (HAC) and National Farmers Federation (NFF) have co-jointly developed a Horticulture Business Code which in their opinion presents industry with a workable model that defines how each party in the horticultural value chain transacts business. The Business Code that has been developed is the subject of negotiation between these agencies and the Australian Chamber of Fruit & Vegetable Industries (representing wholesalers) in association with the recommendations contained in the Buck Review.

## 6.0 CONSULTATION WITH INDUSTRY

### 6.1 Methodology

This consultation sought a wide expression of views and opinions across the whole of the Australian horticultural value chain. Due to the relatively small size of the project budget it was not possible to consult extensively with all sectors of the value chain particularly where it relates to sectors beyond the farm gate. As a consequence considerable effort was spent selecting those in industry who could represent the diversity of views across the sector.

Beyond the production sector, informal discussions were held with participants. Areas discussed included:

- Historical and current supply structures / models within the horticultural produce and value added industries.
- Trends in retailing of fresh and value added produce.
- Key drivers impacting on the trends in retailing and food service sectors.
- Margin structures across the industry.
- Impacts that the key drivers and future development of retailing will have in regards to the supply of horticultural produce.
- Potential organisational and chain structures that will likely develop in the future.
- Key impediments to growth and maintenance of position of companies / sectors across the value chain.
- Role of individual and groups of producers
- Key competitiveness factors for horticultural producers
- Role of industry organisations and governments in assisting the horticultural value chain.

In relation to the production sector, CDI Pinnacle Management with the assistance of Growcom developed a formal survey to collect information from that sector. A copy of this survey is located in Appendix B.

A total of 588 surveys were sent to Growcom members, 340 by email and 248 by post. These members are currently only located / domiciled in Queensland. Following a two week period a total of 60 surveys were returned for analysis. This represents a redemption rate of 10.03 per cent, which given the apparent importance of the subject was low. As a result no statistically significant results can be drawn from this survey, although trends in opinion can be derived and interpreted. These results are discussed in considerable detail in Appendix C.

### 6.2 Consultation List

The survey of growers comprised the Growcom mailing list of its membership. Queensland has approximately 3,500 grower members the balance of which who were not surveyed are not direct Growcom members.

A few of those consulted in the one-on-one process were both growers and also active in other sectors of the value chain. A total of 16 companies were consulted in the one-on-one process, the details of which are provided in Appendix D.

### 6.3 Consultation Findings

The key findings or conclusions identified from this survey are:

- The vast majority of growers grow independently of others.
- There is a moderate level of diversification amongst survey respondents into other agricultural and non-agricultural business activities. However, the survey was not able to determine if horticulture was the principle business activity or not.
- There is a low level of grower consolidation amongst the survey respondents.
- Over 74 per cent of the survey respondents market their production to the wholesale sector.
- The vast majority of production is marketed / consigned to Queensland or New South Wales customers. Just over 11 per cent of produce is sold to Victoria.
- Growers generally agreed with other industry sources that the average rate of deductions by wholesalers from the gross sale price is between 11 and 15 per cent.
- Producers generally have unacceptable systems with wholesalers for the provision of pricing information.
- Producers generally have unacceptably long waiting periods pertaining to the provision of confirmed price advices by wholesalers.
- The majority of growers are dissatisfied with the level of service / conduct of the relationship from their customers / service providers immediately adjacent to them in the chain.

#### TERMS OF TRADE

The terms of trade or 'how businesses do business together' is highly variable across the producer-wholesaler sectors. This has in part contributed to the dissatisfaction amongst producers and wholesalers in regards to their relationships with one another.

Key findings associated with the 'terms of trade' between producers and wholesalers were:

1. There is limited evidence of the use formal contracts or 'standard rules of business arrangement and engagement' specifying the nature of the business relationship between producers and wholesalers.
2. Producers believe that the standard average business charge for wholesalers ranged from 11 – 15 per cent of the gross sale return, although on a consignment by consignment basis, the belief is that the figure does vary considerably. This return is an average level of deduction across all producers over a period of a year.

The average level of business charges charged by wholesalers will vary depending on a number of factors including:

- Variety of produce. High volume lines tend to have a lower business charge in comparison to low volume lines, due to transaction and handling costs.
- Value of produce.
- Breadth of sales prices. Products that have a wide range of prices lend themselves to having a wider range of business charges applied.

- **Producer Knowledge.** Producers who have a greater degree of understanding of how the market is performing and what 'drives' the market on a given day will position them to make more informed decisions on the placement of produce and better negotiation position.
- **Quality of Product Supplied:** Wholesalers value growers who supply high quality produce. Increasingly, as consumers become less and less tolerant of inferior produce, wholesalers will tend to 'look after' good suppliers and become less tolerant of poorer quality suppliers and penalise them by way of returns.
- **Reliability of Produce Supplies:** Due to the nature of ordering of buyers in the wholesale market, wholesalers value growers who can supply regular quantities of produce. They are less tolerant of growers who 'play' the markets and wholesalers, as the wholesaler is less able to develop a lasting relationship with a particular customer.
- **Suitability of Product to Other Markets:** Some products and sizes / qualities of products are better suited to different markets. There is considerable interstate trading of produce amongst wholesalers and brokers. If a product can give a better price in another market, a wholesaler may send it to that market, either with or without the knowledge of the grower.
- Wholesalers may work on a basis that they average a growers return and apply a 'average cost' roughly equivalent to industry commission standards and therefore not necessarily follow the practice of standard commission rates.
- The level of deduction or 'commission' may vary depending on the performance of the market and how the wholesaler performed in that market, prices returned for equivalent standards of produce by other wholesalers, perceived or actual level of knowledge that the grower has about market performance, sales on other market floors in other states, prices paid by chain store buyers and level of competition for additional supplies from a particular retailer.
- Discussions indicate there is a wide spread practice of averaging of individual grower returns across a period, often a week.

#### **PAYMENT ADVICES AND TERMS**

Through this industry survey and other anecdotal evidence there is considerable variability associated with how growers are advised about prices, when they are advised and when they receive payment for their product. This survey highlighted the following:

- Growers are generally advised of prices by telephone, either with or without subsequent confirmation by facsimile. In a considerable numbers of instances the only price confirmation they receive is when they receive payment (26 per cent of all responses).
- Advice on prices returned or sold for, vary considerably from same day (17 responses) to more than 11 days (8 responses) to other (16 responses). This can be explained in part due to the nature of the product that is being sold, in that highly perishable lines will be turned over or sold more quickly than less perishable lines, e.g. hard produce lines. However, other contributors to the explanation of variable price advice include:
  - Producers don't have written agreements detailing acceptable terms;
  - Producers aren't insistent on receiving prices in a timely fashion;
  - Some wholesalers desire to average prices over a period or undertake some other price 'adjustment' activities; and,
  - Advice terms may be acceptable to the grower.

Average payment periods for produce from wholesalers are also highly variable. Of concern is that more than half of growers receive payment more than 22 days after delivery, whereas the accepted industry standard is two weeks after the week of delivery. 'Slow' payment may impact severely on farmers who have limited cash flow reserves or high overheads i.e. Labour intensive farms. Further slow payment will add considerably to financial costs due either to lost interest on credit accounts or higher overdraft / interest charges on debit accounts. Reasons for the slow payment of grower accounts include:

- Poor credit 'management' guidelines employed by wholesalers;
- Growers aren't insistent on payment within terms due to concerns that they may lose a relationship with a wholesaler;
- History determining current practice;
- Cashflow considerations by wholesalers. Some wholesalers if produce is sold to an exporter may not receive payment for six weeks or more. Also some wholesalers may not have adequate financial reserves; and,
- Business viability of wholesalers.

Although not tested, anecdotal evidence suggests that there are a considerable number of growers who receive payment by cheque rather than direct deposit or electronic transfer. In addition to being to delay payment technique (in some cases), i.e. 'the cheque is in the mail', the delays in payment caused by cheque payments rather than direct deposit have an impact on the cash flows of producers.

#### **MARKET SIGNALS AWARENESS**

Although not specifically tested, there is considerable variation in terms of how aware producers are of price signals primarily with wholesalers. On a daily or 'within season basis', the variation extends from:

- Where growers do not actively seek any information apart from that supplied by their wholesaler and so trust the wholesaler to provide correct price signals

#### **TO**

- Where growers seek out information from independent sources, e.g. Ausmarket, other wholesalers, speak or exchange information with other growers and / or speak with other segments of the value chain, e.g. exporters, on a regular basis

In certain instances, large dominant producer suppliers are very active in pro-actively discussing pricing arrangements with wholesalers (and others).

Larger growers are generally more aware of price movements than other smaller growers, presumably as they have 'more' to lose if they are not 'on top' of pricing information. Further, larger growers tends to supply multiple markets and possibly market wholesalers and so are more able to get a broader cross section associated with the supply of prices.

A number of growers highlighted that they wished Growcom to provide wholesale market pricing information.

In each major metropolitan market, there are independent market consultants who on a fee for service basis make available daily quotations on all lines of produce, across a variety of pack sizes and qualities. The survey highlighted that a number of producers are seeking pricing information. This suggests that either growers are not aware of these independent service providers, they are unwilling to pay for the costs of information and / or do not trust the independence of the information given. We suggest that all factors may be relevant to varying degrees. It is warranted, given the high level of responses by producers seeking this

information, that producer organisations should investigate how it may be provided to members.

Prices paid by chain store retailers are still set off the market where prices are reviewed weekly. In most instances the prices paid are based on the wholesale market price inclusive of freight delivered to a specific location i.e. Sydney, Melbourne, Brisbane. Growers are therefore responsible for payment of freight directly.

Growers who are preferred suppliers to chain stores generally go through a range of pricing mechanisms with them based on their levels of experience, type of produce supplying them and the number of other suppliers. Initially prices are generally set on a weekly supply basis in advance, that is, at the end of the previous week prices are offered or discussed between the two parties. Growers are then advised what volumes of produce and destinations they are required to deliver to. Growers may then be contracted for a specific volume over a period, either retaining the weekly price negotiation point and / or having a maximum / minimum pricing model. Maximum / minimum pricing models are where that despite whatever price the wholesale market goes to, producers will receive the maximum agreed price and conversely, growers will receive a minimum price no matter how low the price in the wholesale market goes to.

Discussions with retailers highlighted that the practice of 'cost plus pricing' does not occur in direct relationships between growers and retailers. Cost plus pricing refers to where retailers agree to set a price to growers that is the cost of production of produce plus a 'profit' margin to growers. This situation is now occurring with a few international retailers. It is a relatively more common practice amongst fast moving consumer goods.

## **RISK MANAGEMENT**

Based on anecdotal evidence and the results of this survey, the horticultural industry is not proficient at the use of risk management tools.

The survey results highlighted that:

1. Nearly half of all respondents do not engage in any other form of business activity than growing fruit and vegetables.
2. Only seven (7) producers indicated that they engaged in non-agricultural business activities although there were a further nine (9) who were engaged in a non-specified activity. The other respondents who did engage in non-horticultural activities were still involved in agriculture either in beef, grains and oilseeds or sugar production.

The results highlight the fact that horticulturists generally focus on horticultural production. This may in fact be due to the fact that many producers do not have the financial resources to manage financial risk by diversifying investments. Discussions with relatively high net worth Queensland farmers highlight that many of these people do have considerable off-farm investments, either in agricultural or non-agricultural assets. Also, farmers who are more financially successful generally have the business skills / awareness to not 'put all their eggs in one basket'.

Many growers contend that their farm is their "superannuation". This may be valid if no other family members are coming back to the farm and so it will be sold at some stage in the future. If a family member is going to continue the farm, the ability of this family member/s to do so, will be impacted by their ability to provide a return to the initial owner. Profitability, or lack thereof, and the position that financial institutions have towards many forms of horticulture, suggest that the ability of the next generation to take over the farm may be difficult.

With regards to 'inside the farm gate' risk management strategies, horticultural farmers generally revolve around this around:

- Extending the production season associated with a particular crop;

- producing a variety of crops; and,
- marketing produce to a variety of wholesale markets, to either one or more wholesalers.

Other more sophisticated growers have undertaken a variety of other risk management strategies including:

- Growing product across a variety of regions which are geographically separated from one another in order to minimise the impacts of other adverse weather events.
- Engaging other growers to produce products either within the same or different production regions in order to minimise both the weather and cost of production risk.
- Developing marketing strategies to customer segments where at least some of the price risk is shared, e.g. maximum / minimum pricing.
- Developing forward supply contracts in order to again reduce the supply risk.
- Developing multiple customer strategies.
- Market segmentation - identify customer segments that can take the full range of product sizes and qualities that a grower produces. This effectively results in 100 per cent crop utilisation.
- Engaging in value adding activities either as a stand alone business, in conjunction with other farmers or as a joint venture partner.
- Invest further 'up' the chain in either wholesale, retail or associated service businesses.

Other non-direct farm activities that farmers do not seem to have embraced as extensively as other agricultural business sectors to manage risk include:

- Use of tax legal financial management strategies, e.g. Farm Management Deposits (FMDs);
- Superannuation; and,
- Taking of sound financial advice from people beyond tax accountants.

### **RETURN MAXIMISATION**

In a similar vein to Section 6.4 – Risk Management, growers tend to use relatively unsophisticated strategies to maximise returns.

Production based strategies revolve around extension of production season for a crop, production of multiple crops and in some cases sharing of information and capital.

From a marketing perspective, the range of strategies used include:

- Development of forward orders.
- Segmentation of the geographic distribution of product i.e. Brisbane, Sydney, Melbourne and export.
- Customer segmentation i.e. Direct to retail, sales to processors, different returns.

Due to the unsophisticated nature of these strategies, it may be argued that they in fact result in return averaging.

It can be argued many growers do not necessarily focus on cost minimisation either through innovation, efficiency evaluations or cost monitoring. This is a significant area of

improvement that across the sector growers should focus on in order to achieve maximal returns.



## 7.0 SUCCESSFUL VALUE CHAINS – ESSENTIAL ELEMENTS

### 7.1 Key Drivers in Fresh Produce Value Chains

United Kingdom food retailers are regarded internationally as being at the forefront of innovative developments in value chain management. This has been driven by the highly competitive nature of the food industry, with the majority of the major food chains in the world having a presence either directly or by acquisition within this market.

United Kingdom food retailers are leaders in own-label products, even in the produce industry. The importance and maintenance of the integrity of their brand, as well as highly detailed awareness of consumer requirements, has driven the adoption of new initiatives down the chain.

Fearne and Hughes identified four key factors driving the transformation of the fresh produce industry in the United Kingdom.

#### 1. Supermarket Strategies

- **Differentiation:** Tesco, Sainsbury, ASDA and Safeway account for almost two-thirds of grocery sales and competition for market share is as intense as anywhere in the world. These retailers have found that they cannot continue to grow into non-traditional segments as they did in the 80's and early 90's but rather now have strategies based around differentiation, particularly in the development of own label products. Fresh produce is almost exclusively own label. – hence they can exert considerable influence and control over the rest of the supply chain. Since fresh produce is a destination category – that is one which shoppers will change stores (the other two being meat and wine), achieving success in these categories is seen as critical for the overall business health of the retailer.
- **Store re-orientation:** In a number of supermarkets in the United Kingdom fresh food has moved from the back to front of store.
- **Health & Nutrition:** Further promoting health and nutrition are key drivers and hence major points of differentiation between supermarkets.
- **Costs Minimisation Leading to Prepackaging:** Additionally as retailers have increasingly focused on minimising costs in the chain, the reduction of waste has led to greater levels of pre-packaging. Pre-packaging has provided retailers with greater control over quality, presentation and pack size, in addition to addressing concerns about food safety by retailers.

#### 2. Food safety legislation and supply chain integrity

With the implementation of the 1990 Food Safety Act in the United Kingdom, retailers have increasingly placed downstream pressure on suppliers to ensure they have fully documented and detailed knowledge of their production practices across each segment of their chain. This has led to the adoption of a variety of Assured Supplier Schemes. In Australia, the value chain has been forced to adopt similar standards.

### 3. Rationalisation of the supply base

The United Kingdom supermarket sector has led the way in moving towards working with fewer larger, more technically efficient and innovative suppliers. The initial drivers to this were attempts to minimise the internal transaction costs for the retailer of produce and, secondly, to pass the responsibilities of procurement from internal to others in the value chain.

Over time however, other responsibilities such as quality control, storage and distributions has also been passed down the chain to key suppliers.

With the emergence of initiatives such as The Mercury Program and others it is apparent that beyond just produce supply, cost shifting is being progressed as a strategy by the major retailers in Australia.

This is not unexpected as competition has dictated that margins are not likely to increase from the sales end, therefore in order to become more competitive and achieve greater market share a focus on minimising costs is the key for competitiveness in the future.

### 4. Innovation

Retailers in the United Kingdom are seeking innovative 'angles' in terms of their marketing of fresh produce. Whilst the majority of sales of produce are still commodities sales, there are a number of sources of innovation becoming increasingly evident in the market place. These include:

- Production of ready-prepared salads, vegetables and fruit. These products have a 5-10 day shelf life. Increasingly there is blurring between produce retail and QSR as each segment moves towards the offer of 'convenient' meals in order to appeal to their customers.
- New varieties of produce that are sweeter, juicier, crisper, better looking, with longer shelf-life. Increasingly, these products are being produced in 'closed production systems' whereby retailers are negotiating sole access to varieties that deliver a point of differentiation to other pre-existing products.

In Australia, there is limited evidence of this presently (broccolini, mini-vegetables are examples however). Discussions during the course of this research indicated an increasing focus on this form of competitor differentiation.

- New formats. Again the emergence of pre-prepared mixed salads, stir fry packs are seeking to appease the consumer preference for increased convenience. In some cases this is involving a crossover between traditional retail and that of QSR which historically had dominance over this sector.
- Extended shelf life production efficiency. Retailers are seeking to partner with companies who can provide processing, storage, packaging and logistics technologies which are superior to competitors. Due to the scale of investment that is necessary to develop (or purchase) these technologies it is only the largest players who can develop them.

The issue as identified by Fearne & Hughes (1999) that initiators or drivers of change / innovation, particularly if they are 'new' suppliers is to access enough rewards to make the investment worthwhile. In fresh produce, the 'me too' comes quickly and if a pro-active supplier has an existing relationship with a retailer, they will maintain their relationship. Therefore there is either limited incentive or limited opportunity for new suppliers to become part of these chains; that is, they effectively become closed.

## **7.2 Characteristics of Successful Partnerships in Fresh Produce**

In a paper presented by Dr Andrew Fearne and Professor David Hughes (1999), "Success Factors in the Fresh Produce Supply Chain: Insights from the UK", the authors discussed the key characteristics of what makes a successful produce supplier to United Kingdom supermarkets. This paper was completed following in depth research of a number of the major retailers in the United Kingdom, notably Sainsbury and Tesco.

The United Kingdom retail sector is 'held up' by others in the industry as being the leaders in the adoption of new technologies, sources of innovation across the value chain

Sainsbury and Tesco analysis identified a consistent list of factors that supermarkets regard as key indicators for the development of successful partnerships in the fresh produce supply chain. These lessons gain be applied across any aspect of the chain, not just retail-driven chains. The key success factors identified include:

### **1. Proactive Relationships**

Sainsbury and Tesco are moving away from having exclusive buyer / account manager relationships to relationships with suppliers that extend beyond just the transaction base. Suppliers are encouraged to develop relationships with the promotions department, logistics department, packaging departments of retail operations, so as to ensure a fully integrated focus on delivering to customer expectations can occur.

This would be a major paradigm shift both for produce suppliers and many in the wholesale sector who typically having adversarial relationships and if not this type of relationship, almost totally a focus on the transaction and little beyond this.

### **2. Complete Electronic Integration**

Retailers are insisting that their suppliers are able to communicate electronically with them. At the lowest level this involves electronic communication of orders and supply programs. At higher levels this involves suppliers having access to distribution centre stock on hand records (so as to allow for supply top-ups without retail orders) to allowing suppliers access to scan data so as to allow suppliers to make production, logistics and marketing decisions / recommendations to retailers on a pro-active basis. In the United Kingdom, due to cost reductions these types of IT data collection mechanisms are available to the smallest of suppliers.

### **3. Information Sharing**

Advanced value chains are proactive in sharing information with others with whom they conduct business. Each is committed to the idea that if they share information the costs of doing business and the identification of ways to grow their mutual businesses will occur. Eventually the success of one business drives the success of the other as they become part of closed or exclusive value chains. Mutual dependency then offsets the risk of sharing information with other in the value chain.

Australian horticultural value chains have not developed this level of sophistication, except for a few examples with specific grower and non-grower consolidators. This is in part due to the 'culture' that has pervaded Australian horticulture of mistrust, particularly between the production and wholesaler sectors. Chain store retailers have also been reluctant to enter into closed loop value chains (until now), in part due to concern that those 'down' the chain can deliver and further a culture within their organisations that has not permitted this openness of information sharing. In fact fresh produce could be regarded as the last 'bastion' of truly integrated information sharing between retailers and suppliers.

### **4. Innovation (New Product Development, Marketing, Supply Chain Management).**

In the United Kingdom with relatively few suppliers supplying retail supermarket chains and a desire to further reduce numbers those who can build the business of the retailers through

any form of innovation (new product development, marketing programs, logistics efficiencies, new and improved products, value adding) will be the ones that will be successful in getting the greatest slice of the 'supply pie'.

Generally those producer businesses that have a 'innovative culture' are those who willing to outside the circle, look at how others are doing business (both within and their industry) both domestically and internationally, are willing to take on new information and processes. It is not expected that all businesses will have this culture. The issue is how do we foster those who do have the 'innovation skills' and how do we link with those producers who have the production skills.

The majority of the participants of the Australian fresh produce chain are not innovative. The majority of producers still continue to do business in a similar fashion to a decade, two or many decades ago. Wholesalers have generally the same business practices that they did in the same period. Innovation to date in fresh produce has largely been driven by retailers, in response to consumer needs. The level of true integration between the retailer and others has however not been as sophisticated as has occurred in the United Kingdom. However, when we examine the current strategies being pursued by Australian retailers, as we did in Sections 4.5 and 4.6 it is obvious there is a major culture shift towards developing increasing levels of partnering and closing of chains.

Certainly in Australia, the production sector has two main issues associated with innovation, scale or lack thereof for much of the production sector and secondly, the willingness and ability to access to information.

Culturally, some would argue that Australian producers are often guilty of not being willing to source and then use information. Those who are innovative proactively seek it out. This may then require a major culture shift in how producers (and others) think about their and that of their business partners operations.

## **5. Ability to assist / shape customer's view of the category and its future development**

Australian producers are not actively involved in relationships whereby they seek to alter how a customer things or relates to the fresh produce category. Whilst imagery might be used by some retailers indicating strong strategic relationships the level of strategic involvement is low by comparison with European value chains. The ability of those further down the supply chain to interact with retailers in developing these relationships will largely hinge on the willingness for retailers to allow this to occur.

As certain retailers advocate more and more of a category management role to others further 'down' the chain, their ability to shape the customers view of the category will improve. However, the level of involvement will continue to be tightly controlled by the retail chains.

## **6. Customer specific products, services and investments (supply chain exclusivity)**

Australian retailers are commencing a drive to seek access to products or services that are exclusive to a specific chain. Examples of this include the variety of products that Perfection Fresh Produce produce under license, the Select Melon Co-operative and certain stonefruit varieties. Discussions with retailers indicate a move towards an increasing focus of supply chain exclusivity as a means to achieve an innovative edge with its competitors.

In Europe, there are a number of examples where retailers are the 'owners' of the specific product, service and investment and they contract down the chain access to it. In Australia the ownership tends to rest with someone else, e.g. wholesaler, broker and contractual arrangements exist to supply exclusively to a specific retailer. Chain store retailers will be the only organisations at the retail level who will be able to deliver the scale of order to allow these types of transactions to develop.

## **7. Financial Stability**

United Kingdom retailers conduct detailed examinations of the ability of their suppliers to meet their commercial obligations. In Australia, this level of investigation does not occur, save for the 'rumour mill' which exists across the industry.

The business failure of a supplier will result in considerable loss of intellectual property, time and effort. Therefore in future it would be expected that Australian retailers will increasingly focus on this area in its selection of value chain partners.

## **8. Supply Chain Management (integrity and efficiency)**

As has been discussed in a number of sections of this document, the level of sophistication of supply (value chains) in Australia, in general is poor. There are some exceptions to the rule, but the majority by number who even have an awareness of the basic principles of SCM or VCM are relatively minor.

As has occurred in the United Kingdom not all producers will be able to or be given permission to be exclusive suppliers to retailers. Australian retailers will over time select those who will be able to meet the needs of its business, as discussed in this section. The current 'push' amongst European retailers is chain efficiency, that is the removal of costs from the value chain. At the same time there is an apparent move to explore how innovation can deliver differentiation between retailers and so they are seeking relationships with those suppliers who can 'think outside of the circle', both passively and proactively.

## **9. Cost management**

In the United Kingdom, JS, Tesco and M&S have all developed a detailed understanding of cost structures across the chain with the emergence of their 'own label' products. In Australia the level of sophistication associated with whole of chain costs has not been developed. Presently, the focus has been on having suppliers minimise costs to retailer as much as possible with limited understanding of how this occurs. Conversely, producers and wholesalers have even less understanding of the cost and margin structures of retailers. The 'openness of book' in Australian value chains still has a considerable way to go. This may largely be driven over time with the emergence of closed loop value chains.

Australian retailers currently have a major focus on cost management in order to enhance competitiveness. However, many of the strategies being developed have largely occurred independent of others in the chain.

Therefore if cost management through transparency is a critical element of chain success, the Australian horticultural industry has a considerable room for improvement.

It is not realistic to assume however that value chains will share this information with others 'outside'. Therefore unless an organisation is part of a value chain that values transparency those on the outside can not expect to share the information that it develops as this is a major source of competitive advantage.

## **10 Product Range Management**

Product range management is the 'highest' level of category management currently in existence. Even in the United Kingdom it is a relatively new development in fresh produce as retailers consider that the dynamism associated with it will make it difficult for a non-retailer to perform these services.

It is unlikely based on our experience to suggest that major Australian retailers will embrace product range management in the short to medium term. Moreover, it is unlikely a producer, wholesaler or consolidator will have the skills necessary to perform this role.

## **11 Promotion and Merchandising**

Even in the United Kingdom retailers tend to be responsible for the development of promotion and merchandising strategies in fresh produce. In FMCG suppliers are increasingly the drivers in the United Kingdom.

In Australia, the same situation exists. Suppliers to major retailers generally contribute to promotional campaigns, but have little or no impact on their development. Retailers are generally responsible for promotions development o generic campaigns i.e. Store or product focused. There currently is no evidence of brand promotions within fresh produce.

Indications from retailers suggest that this situation is unlikely to change in the near future, although certain producers may be asked to contribute more proactively to the development of promotional material and merchandising material in the future.

Fearne and Hughes (1999) argued that “the last two points are of less importance in the fresh produce category than they are for branded manufactured products. Financial stability and electronic integration may be considered prerequisites rather than differentiating elements and commitment to specific customer investments (products, processes and people) is something which is desirable on the part of the retailer but not a necessary condition for success”.

#### **The Vision for the Future**

According to Fearne & Hughes (1999), the future of United Kingdom value chains is for a steady move away from traditional commodity trading, with its emphasis on price, towards integrated supply chain partnerships, with much greater emphasis on value added and return on investment to all members of the supply chain. At the grower / pre-packer interface, the need for further volume growth will mean further rationalisation of the supply base with the largest and most professional growers being rewarded with whole crop marketing agreements on a cost plus basis, which in turn will lead to much greater product differentiation and market segmentation.

As United Kingdom retailers get market share close to 80 per cent the 20 per cent of the independent retailers will make it hard to get further gains. Therefore market information will become a key driver in the future, so that consumers can choose between (a) and (b). This will lead to increased market segmentation...will require an even greater knowledge of consumer behaviour in the store.

Issue will be the raising of entry barriers. In FMCG there is proprietary ownership, either of brands or technology. In produce there is a lack of brands and technology is available industry wide, plus there are many small companies who cannot achieve the economies of scale that multinationals can achieve.

In 2000, the Bureau of Rural Sciences an analysis of the supply chain capability of some of Australia’s agricultural and fishing industries based on 11 chain attributes. The results highlighted the relatively low level of preparedness and capability of our horticultural chains. The results of this work are presented at Appendix D.

## 8.0 HOW WILL QUEENSLAND HORTICULTURE LOOK IN THE FUTURE?

In determining what an industry and its participants require to be competitive in the future, we firstly need to gain a picture of what the industry will look like in the future and why. Only once this has been determined can we look at what resources, skills, programs and strategies are needed to ensure that each section of the industry can achieve its destiny.

The key driver to how horticulture will develop in the future is the issue of chain reversal. Consumers, by way of purchasing power will determine what is produced, in what form and what quantity. This will be influenced by advertising and the trend development. Fresh produce is not a driver of trends but rather a by-product of the impacts of trends. For instance, healthy eating it can be argued, is the result of medical evidence to suggest humans will live a longer life if they eat fresh produce, or fashion dictates that in order to achieve a preferred body shape a person needs to eat less 'fattening foods'. Further, as consumers tend to focus more on convenience in order to have more time on recreational, family or work activities, fresh produce needs to be delivered in such a way to meet these requirements.

End food marketers, whether they be retailers, processors, QSR or other food service providers, are all in the 'solution business', eg. providing meal solutions to the eating needs of consumers.

Their business success is dependant on firstly understanding, then meeting the needs of the consumer and then attracting the consumer away from other suppliers.

Therefore end food marketers can then be expected to be the arbiters of change in the horticultural chain. This will occur for two reasons, firstly due to their position in the chain as discussed above and secondly, due to the structure of the chain, where we have relatively few players at the 'top' of the chain with relatively many players at the intermediate (wholesalers, brokers, providers and consolidators) and 'bottom' of the chain (producers).

### 8.1 Horticultural Industry Characteristics and Needs

It is a difficult task in forecasting how an industry may be structured in the future due to the large number of externalities which exist in them and the impacts each might have. This report has drawn on value chain developments that are occurring in other countries, particularly Europe, which appears to be a leader in new chain developments. Further, information has been drawn from a wide number of Australian parties who are either commercial players or are observers or service providers to the industry.

Based on the high degree of consultation and the knowledge of the consultants, the 'best bet' structure and nature of the Australian horticultural value chain may be:

#### PRODUCER SECTOR STRUCTURE

Over time the production sector will have:

- Fewer horticultural farmers.
- Average size of farms or turnovers will increase over time, with the predominant movement out of the industry being of smaller sized farmers.
- Smaller growers with identifiable market niches who have a strong focus on costs management and good management / business skills will continue to have a strong future.
- A continual movement in and out of the sector of new entrants, only some of which may remain in the industry over time.

- Greater levels of consolidation of produce either at the production level through grower consolidators or through consolidation further up the chain either by non-grower consolidators or retail 'in-house' consolidators.
- Growers will tend to increasingly specialise in the crops that they grow, particularly in the vegetable industry.
- Full or 100 per cent crop utilisation will become a focus of producers.
- Some producers will seek to partner with those further up the chain either in processing and / or marketing enterprises. The success will depend on the level of business management skills of the producer.
- More successful growers will have closer relationships with wholesalers, processors or retailers and will seek to exchange greater levels of production, supply and marketing information to the benefit of all
- Increasingly growers or grower consolidators will become part of closed chains, involving input providers right up to processors and retailers.
- Varieties subject to plant variety rights or trademarks will become integral to closed chains.
- The average level of business skilling of the producers will rise, particularly in terms of business management, financial recording, data collection, communication and market investigation / development strategies.
- Producers will be expected to be leaders in innovation, rather than followers particularly in terms of gaining access to new varieties, development of innovative marketing concepts and strategies.
- Producers will increasingly be required to undertake activities that were considered the preserve of others in the chain. The main example of this will be in terms of supply and logistics management.
- Successful growers will be those who can identify points of differentiation or innovation from their ability to collect, analyse and action information either provided by others or sourced directly.
- Producers will be faced with increasing levels of compliance either from within the chain or those external to the chain i.e. Governments. It is unlikely given the given the current political climate that government will develop enforceable codes of business conduct across the value chain. Non-enforceable codes of conduct will continue to have mixed success unless embraced by the whole chain.
- Water access, impacts by others on producers farming practices, government legislation and access and management of labour will be the critical on-farm issues that will impact on farmers beyond value chain issues.
- Producers will need to continually seek to identify cost efficiencies that can be gained inside the farm gate, so as to be able to be more cost effective over time.
- Producers will be forced over time to increase with a wide range of imported fruit and vegetable products.
- Unless major structural and cultural changes occur in the horticultural export value chain, Queensland will have a mixed future in terms of export finance.



## WHOLESALERS

Traditional wholesalers will increasingly have to focus on the development of strong relationships with their customer base at both ends of the chain, achieve greater operational efficiencies and become more pro-active and innovative in the conducting of their businesses.

An examination of the wholesaling sector both in the United Kingdom and the United States shows a weak sector as the level of transactions that goes through this sector continue to decline. Some wholesalers will need to change their business model to reflect the changing needs of their customers (chain retailers, independent retailers, country order buyers, providers and exporters). Developing a customer orientation and then a 'downstream supply system' whereby the wholesaler provides value both to their customers and suppliers will be critical for the long term success of their operations. Some of these model types that may be developed over time include:

1. Non-Grower Consolidators
2. Whole of Category Managers
3. Packaging / Formatting Consolidators
4. Specialist Wholesaler (to smaller market segments)
5. Broker / Producer Chain Manager

Alternatively, wholesalers may seek to direct invest in down stream supply relationships either in the form of joint ventures or sole ownership models.

## PROCESSORS

The processing industry may or may not achieve greater levels of aggregation over time. The ongoing challenge for them, like for many sectors, will be to deliver to the ever exacting needs of their customers (as their customers' customer becomes more demanding) and to provide value to that customer. Another issue will be that in certain market segments processors will have to meet the challenge posed by imported products.

This study has not conducted an in-depth investigation of the processing sector beyond discovering a set of issues that impact it and the nature of the relationship with the production sector.

## RETAILERS

This study has highlighted, particularly in Section 4.0, a number of key competition issues and drivers that will impact the nature of the retail marketing sector in the short to medium term. What the structure may be of the sector and the relative shares and positions of those in the sector is to complicated to forecast.

As discussed previously it will be the chain retail sector that will be the major change or paradigm shifters in the sector and down the chain. This will be in response to the changing desires of the customer base.

Increasingly, the division between retail and food service will become hazy, particularly as it pertains to consumer meal selection. Retailers will increasingly provide alternative meal solutions to consumers and in return food service will supply fresh food options that previously were the preserve of retailers through their fresh food category.

## 9.0 HORTICULTURAL ENTERPRISE RE-ENGINEERING OPERATION

The central question this study has sought to answer is:

**How do Queensland producers become part of the effective operation of value chains now and into the future?**

This study has highlighted three key issues for Queensland (and Australian) horticulture:

- The horticultural value chain is dynamic, evolving and its structure will mostly be determined by the decisions of the consumer and retailers in future;
- The production sector is generally unprepared for the evolution; and,
- Industry leadership / entrepreneurship will be a critical element for the ongoing success of the production sector.

The answer is not as simple as the problem is multi-faceted. The production sector has a wide diversity of business operations in terms of scale, capability and nature of relationships with those further up the chain. As a consequence there exists a wide range of solutions that must be tailored to a diverse group of growers.

Producers have long afforded blame for the failure of the chain to deliver appropriate rewards to them, to others. This program if implemented will result in the development of an industry sector that has the necessary skills and focus to become pro-active, long term contributors to the horticultural value chain.

The Horticultural Enterprise Re-engineering Operation (HERO) seeks to give individual enterprises the skills, systems, programs and strategies necessary to become efficient, effective members of world class value chains.

Queensland should be regarded as the test arena / pilot for the implementation of the program. This will allow for evaluation of its success and fine tuning so that it delivers on the needs of the value chain. HAL, DAFF, the commercial elements of the value chain, State Government Departments and Growcom are all critical players to the financing and successful implementation of the program.

Growcom, as a strong industry organisation, with the physical and financial assistance of others is best positioned to take a lead role in the delivery of the program.

### 9.1 Key Development Areas and Issues for Queensland Producers

This study has highlighted that the key issues that the sector must address in order to achieve a viable and prosperous horticultural production sector are:

Issue Areas	Key Issues
Entrepreneurship & Industry Leadership	<ul style="list-style-type: none"> <li>▪ Industry has a lack of commercial leaders who have the requisite skills to be relevant to upstream chain members, as value chains develop over time.</li> <li>▪ Exposure of industry leaders to best practice examples in business entrepreneurship, both inside and outside the sector.</li> <li>▪ Development of an industry culture that supports leaders and entrepreneurship as the mechanism that will drive overall industry benefit.</li> </ul>
Information Provision	<ul style="list-style-type: none"> <li>▪ Develop collection mechanisms for information pertaining to production costs and returns.</li> <li>▪ Provide access to wholesale market volumes and prices for all commodities in a easy</li> </ul>

Issue Areas	Key Issues
	<p>to access mechanism and at low cost.</p> <ul style="list-style-type: none"> <li>▪ Develop greater knowledge and then dissemination of information on whole of chain costs and returns – (develop the tools to dispel the myths).</li> <li>▪ Provision of information on value adding, innovation initiatives and trends (consumer and retail) further up the chain.</li> <li>▪ Development and circulation of case studies (domestic and international) of successful new business initiatives and development.</li> <li>▪ Advice provision on standard business issues and developments i.e. BAS, ATO, WPH&amp;S.</li> <li>▪ Promotion of chain awareness i.e. New developments in chains, how they may impact on the production sector.</li> <li>▪ Have knowledge of and access to information providers and contacts that industry may require over time.</li> <li>▪ Gain access to and provide information concerning consumer preferences and desires, how they 'think' and what they will require in the future.</li> </ul>
Marketing and Business skills	<ul style="list-style-type: none"> <li>▪ Access, develop and disseminate knowledge of new markets / opportunities.</li> <li>▪ Identify and facilitate skills delivery systems in developing both domestic and international business relations.</li> <li>▪ Communication of best practice standards in business management from horticulture and sectors outside of it.</li> <li>▪ Training in business negotiation and general communication.</li> <li>▪ Facilitate a general awareness of standard business operational procedures with others further up and down the chain.</li> </ul>
Development of linkages & synergies	<ul style="list-style-type: none"> <li>▪ Provide or facilitate services that develop the ability to identify good fit strategic partners (vertical alliances) and implement business development strategies.</li> <li>▪ Provide or facilitate services that develop the ability to identify good fit strategic partners (horizontal alliances) and implement business development strategies for same.</li> <li>▪ Provide linkages to service providers who identify new business opportunities for production sector and others in the chain.</li> <li>▪ Promotion of initiatives that foster the development of knowledge of the chain beyond the farm gate i.e. Meet the wholesaler, retailer, exporter, logistics.</li> <li>▪ Development of an improved and more co-operative culture between different sectors in the chain.</li> </ul>
Financial skills	<ul style="list-style-type: none"> <li>▪ Development of benchmarking systems – production and whole of chain focused pertaining to costs and returns.</li> <li>▪ Development of a base financial reporting standards / mechanisms.</li> <li>▪ Assist growers develop skills to make informed financial investment decisions, on farm and off-farm.</li> <li>▪ Communicate information on investment strategies and options. Also have ability to refer to sound investment partners.</li> <li>▪ Communicate information on changes to laws / regulations that will impact financial management of individual farms.</li> </ul>
Business mentoring, coaching and	<ul style="list-style-type: none"> <li>▪ Provide professional assistance so as to allow businesses to have analytical and strategic analyses of their business – business diagnostics</li> </ul>

Issue Areas	Key Issues
support	<ul style="list-style-type: none"> <li>▪ Provide access to qualified succession planning services</li> <li>▪ Assist with the formation of linkages with existing service providers.</li> </ul>
Systems development	<ul style="list-style-type: none"> <li>▪ Develop standard terms and conditions contracts for producers dealing with other elements in the chain.</li> <li>▪ Develop of a pro-forma set of communication documents across the chain (focus on increasing returns transparency).</li> <li>▪ Develop and communicate information on standard business communication systems.</li> </ul>
Agri-policy	<ul style="list-style-type: none"> <li>▪ Maintenance and gaining increasing power in the chain for the production industry.</li> <li>▪ Provide assistance to the production community pertaining to market access issues (both export and import).</li> <li>▪ Prevention / lobbying on unfair trading practices within the chain.</li> <li>▪ Promote standard terms of business / trade developed in consultation with the chain to the production sector and others.</li> <li>▪ Promote development of enforceable business systems across industry (if appropriate).</li> <li>▪ Promotion to other sectors of the value chain beyond the farm gate of production sector issues / concerns.</li> <li>▪ Assist with / involve itself in government policy and initiatives for producers who wish to exit industry.</li> <li>▪ Lobbying with government to lower the costs of transacting and compliance.</li> <li>▪ Strategy and policy formulation to develop internationally competitive value chains i.e. Reduction of costs of transacting international business, addressing industry concerns of imports only along quarantine or phytosanitary lines.</li> </ul>

The concept of leaders and followers in an industry is important to understand and apply to horticulture. The adage “5 per cent of the industry want to lead and 95 per cent want to be led” is critically relevant when we examine the evolving value chain for horticulture (in Australia and across the world). Customers have dictated they will deal with fewer and fewer producers over time, so not all the producers will be at the front of the queue dealing with chain stores, large independent retailers and processors. Those who have access to the customer will be ‘king’. Those who do lead will have to have a highly developed package of collective skills that enables to be relevant to their customers and their customers’ customer.

## ***9.2 Tier Elements of the Horticultural Enterprise Re-Engineering Operation***

The challenge facing those who will consider this report is how to provide programs and services that addresses all of the issues discussed in Section 1.6.

In developing a multi-tier level of services and programs that will address the changing face of horticulture in Queensland (and Australia) in future. Over time, there will be fewer growers who will be supplying the major customers for fresh produce. Chain store retailers, processors and some independent chains have stated categorically they will be dealing with fewer and fewer growers. Further, as the demands of these sectors increase particularly in regards to cost shifting down the chain, category supply and management, proactive development of marketing and information programs, use of information technology, the skill sets required by those who ‘access to the customer’ will be entirely different to those required by smaller producers supplying produce to the wholesale markets or are part of some form of consolidation model.

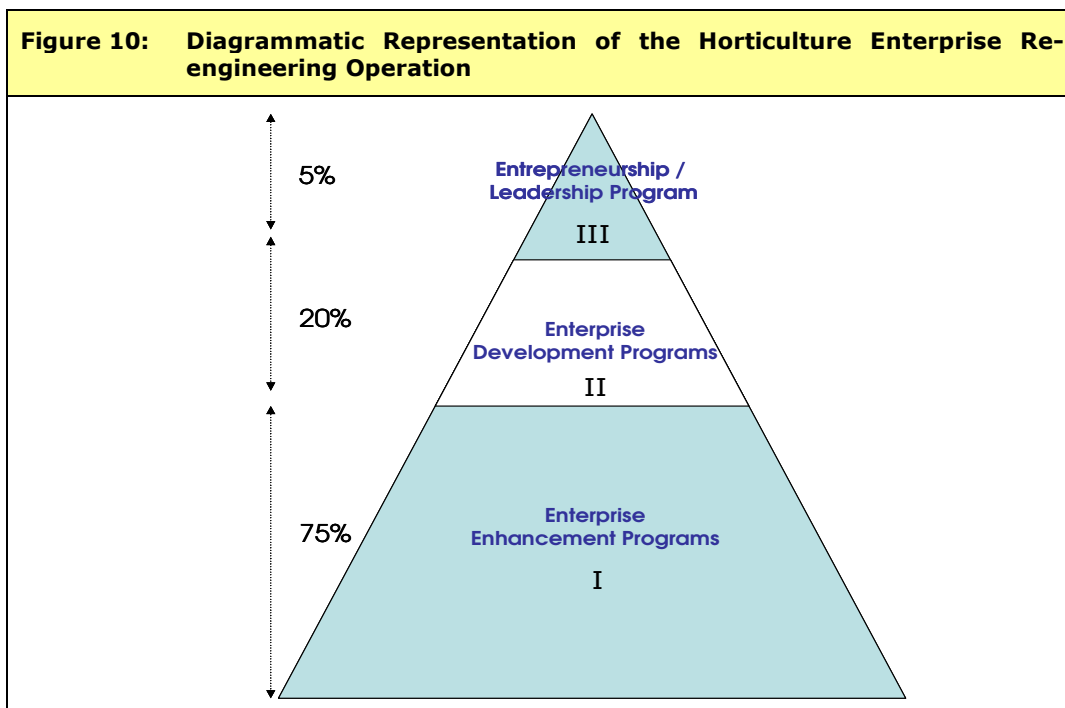
Horticulture is a diverse industry with a wide range of large and small growers, with a wide variety of business skills. Their connectivity to and knowledge of the value chain beyond the farm gate is varied across the sector. It is not necessarily dependent on business size.

As a result of the research conducted in this report and as discussed in Section 1.6 the breadth of issues that industry needs to address to become more 'value chain competent' is vast. The challenge facing industry organisations is how to take these issues and develop services and programs that can be delivered to their members or industry in a form desired by the producers in a cost effective manner.

This report recommends the implementation of a three tier system of service provision by Growcom. In short, HERO will seek to provide commercially relevant services and programs to all 'levels' of the production sector.

This report recommends the implementation of a three tier system of service provision by Growcom. These tiers will correspond to the level of skill sets that are possessed or required by different producers.

1. Tier I – a combination of strategies and programs that focus on delivering to producers improved profitability / viability for their businesses. Customers of Tier 1 programs may be expected to be satisfied with their current role in industry but wish to develop knowledge or gain access to information that allows them to be more sustainable. The focus to Tier 1 programs will generally be on smaller business operations who may not previously had access to these strategies and programs, for whatever reason.
2. Tier II – a combination of strategies and programs that seek to build the capability to have larger and more profitable businesses. These businesses may wish to develop a different role or position within the sector that they operate in. In many instances they may be part of collectives or closed or semi-closed marketing systems.
3. Tier III – strategies and programs that seek to foster the entrepreneurship or leadership of those firms and individuals who for reasons of their position in the value chain or position within industry are seen by others to be 'leaders' either in commerce and / or in industry leadership roles. Diagrammatically the HERO may be represented as follows:



## **TIER I SERVICE DELIVERY**

Growcom has recently developed a product called 'People Pak'. This pack contains information, fact sheets and practical advice and solutions for people management issues. Growers also receive regular updates on changing legislation and other issues. Subscribers also receive access to practical on-line advice when required. The practical approach taken in regards to the content of the material is a critical success factor in its success in the eyes of producers.

Tier I service delivery could be achieved by the development of a similarly focused delivery tool which could be called 'Enterprise Pak'. Some suggested elements that may make up Enterprise Pak are:

- Standard terms and contracts for growers dealing with other elements of the chain.
- Suggestions / hints of how growers can improve communication with customers / other service providers.
- Development of a pro-forma set of communication documents suitable for the rest of the chain.
- Access to pricing and supply information, e.g. Market Information Services information.
- Regular updates / reminders regarding major government compliance events, e.g. BAS, Provisional tax, superannuation.
- General advice on standard business issues and developments.
- Facilitation of a general awareness of standard business operational procedures with other further up and down the chain.
- Information on access to business management / advice practitioners for taxation, accounting, business and succession planning.
- Provision of industry frameworks for recording of gross returns, costs and margins for subsequent financial analysis.
- Development and circulation of case studies (domestic and international) of successful new business initiatives and development.
- Circulation of other relevant information as identified by the delivery team and from communication with growers.
- Hotline or service line for growers to gain access to information, e.g. Terms of trade, potentially industry accredited wholesalers, sources of information available to growers to seek remedy to marketing issues etc.

These are just suggested service areas that may be able to be provided. There will likely be many more. As part of the developmental process for the Enterprise Development Unit (EDU) further consultation with industry is recommended to identify other sources of untapped service provision, preferred methods of delivery and other structural issues.

Significant elements / components of the Tier I services are already available and in existence but through a variety of service providers, in-house information already held and government agencies. The missing element is the achievement of the bundling of these services to provide a 'first stop shop' for information provision. The HERO merely is the collective mechanism for the bundling of these services and Growcom is the funnel through which it is delivered.

Inside farm gate issues such as variety development, planting and harvesting advice are all well advanced in terms of service delivery by other agencies and so should not form part of Tier I service delivery.

## **TIER II SERVICE DELIVERY**

Tier II service delivery focuses on providing a bundle of services that build the capability of individual enterprises to develop new and expanded business opportunities. Specific services that could or may be provided, but not limited to include:

- Development of whole of chain costs and returns models for industry for subsequent use in the development of benchmarking systems between individual enterprises and average industry performance standards.
- Development of a methodology accessing information on value adding, innovation and new trend initiatives both within Australia and overseas and then disseminating this to Tier II 'subscribers'. Development of case studies on innovative business activities both within and outside the farm gate would also form part of this service.
- Development of databases of quality service providers who can assist individuals and collectives of same, identify and develop sustainable relationships with 'good fit' strategic partners either in the production sector or across the chain.
- Promotion of initiatives that foster the development of knowledge of the chain beyond the farm gate.
- Development of a business facilitation / linkage service whereby organisations whose responsibility is to identify and foster new business and trade opportunities may be directed to qualified growing enterprises. Conversely, growers would be able to gain access to networks / contacts / services who wish to develop new business opportunities.

Developing in-house expertise in these areas is not warranted at least initially as Growcom needs to 'test' the market place for the willingness of the production sector to pay for such services.

Similarly to Tier I delivery, the elements that may make up Tier II service delivery may or may not be in existence elsewhere in the market place. Organisations should not attempt to duplicate services and information that may be already available but rather facilitate their bundling in a way that is easily accessible to the production sector.

## **TIER III SERVICE DELIVERY**

It is not industries that develop over time but rather enterprises that drive industries forward. Supporting commercial and industry leaders assists a 'pull' mentality in terms of development rather than the traditional 'push' mentality where all in a sector must be seen to be pushed at the same rate.

There currently exists a range of programs that seek to foster and develop the leadership and entrepreneurship skills of industry leaders / formers. Examples of these include the Queensland Enterprise Workshop, National Enterprise Workshop, a variety of programs run by Achaeus, Blue Storm, the Australian Rural Leaders Program and Monash University's Produce Executive Program (supported by HAL).

Each of these programs seek to develop within participants a range of professional and personal leadership skills development, that will benefit their own individual business and the industry in which they operate. Importantly, these programs will develop a culture within the individual that is more forward thinking, seeking of innovation and new ways of doing business and development of a more global outlook. It is these leaders who will ultimately drive the commercial success of the industry (as they are the leaders in the growth elements of the industry). Over time, these entrepreneurs are also encouraged to develop industry leadership roles in peak or representative organisations.

The additional benefit to organisations such as Growcom/HAL is that it will allow it to 'engage' with the commercial and industry leaders, who if supportive of the industry organisation, will then promote its involvement to others.

Growcom should seek to interact / negotiate with a selected group of these leadership / entrepreneurship program developers so as to develop a program directly relevant to horticulture. We have conditionally called this, "**The Australian Horticultural Leadership Program**".

This program should be developed in consultation with a selected group of industry leaders. Growcom should seek external funding for the development, implementation and management of this program for a minimum period of five years. Depending on the uptake and independently assessed success of the program this program should be rolled out over time across Australia. Queensland should however be the trial site for the program.

### **9.3 Horticulture Enterprise Re-engineering Operation Implementation**

#### **PHILOSOPHY OF HERO**

The driving philosophy of the HERO is to provide a range of service, strategies and initiatives that will be relevant to the ongoing business success of all growers.

Each tier of service delivery is very important, but the successful development of Tier III service provision should be considered a primary focus of the program.

#### **GOALS OF HERO**

Further goals for the HERO should be developed in consultation with others but the primary goals this report considers for the program are:

1. Provision of services, strategies and initiatives to industry that will allow industry businesses to become more relevant, profitable and sustainable within the sector that they operate in.
2. Development of a forward, outlook looking and vibrant industry that has a culture of 'can do' and self-reliance.

#### **KEY ISSUES FOR SUCCESSFUL IMPLEMENTATION OF HERO**

The key issues that this report has identified which may impact on the successful implementation of HERO.

1. Access to and provision of adequate financial resources over a period long enough to prove the relevance of such a program.
2. Program marketing. Development of an appropriate marketing strategy that ensures the attainment of 'sales' goals for the program.
3. Grower apathy and overcoming perception of irrelevance by production sector of the program.
4. Gaining support from other value chain members.
5. Gaining support from other service providers.
6. The ability to integrate the program into the internal operations of the Growcom.



## **NEXT STEPS**

In order to 'test' the principal recommendation of this report, that is the formation of the Horticultural Enterprise Re-Engineering Operation, and the various elements that constitute it, the report needs to be supported by HAL and Growcom.

If this occurs, it is proposed the next steps should be:

1. Development of an Implementation Strategy for the program, including identification of the major elements of the program, potential support and information services, potential service deliverers, funding sources and role of the various government and industry support agencies.
2. Development of an interim operational model for the delivery of HERO.
3. Consultation with industry to discuss the various elements of HERO and preferred service delivery methods.
4. Adjustments based on industry consultation feedback to the Operational Model for HERO.
5. Resourcing of HERO.
6. Implementation of HERO.

It is strongly recommended that as the principal state horticultural industry representative organisation, Growcom should be the lead 'agent' responsible for the implementation of the recommendations of this report. Further, Growcom is best positioned and has the greatest level of knowledge about Queensland's industry participants. In addition it already has in existence a resource structure, through its regional offices to be the most effective mechanism to assist with the implementation of the HERO.

However, there are numerous organisations which can add considerable value to the implementation of the HERO, either through resource or service provision or funding. These organisations include Queensland Department of Primary Industries & Fisheries, Queensland Department of State Development and Innovation, FarmBis and the Department of Agriculture, Forestry and Fisheries. These organisations as a minimum are those that should be consulted as part of Step 3, discussed above.

The suggested timeframe for implementation of HERO would be 9 to 12 months, with an initial focus on service delivery to be Queensland centric.

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## APPENDIX A: COMMUNIQUE OF OUTCOMES FROM MEDIATION BETWEEN NFF, HAC AND ACFVI

### **Communiqué of Outcomes from 29<sup>th</sup> September 2004 mediation between NFF, HAC and the Australian Chamber of Fruit and Vegetable Industries regarding establishing a clear Terms of Trade to improve transparency and accountability in the fresh fruit and vegetable industry**

**Points in *italics* could not be agreed**

**This is an agreed true representation of the final state of negotiations between the parties**

#### **A FRAMEWORK FOR A MINIMUM TERMS OF TRADE**

1. Traders must trade as either an agent or merchant in accordance with the following definitions:
  - a. An agent sells the suppliers' produce for an agreed commission. The supplier retains ownership of the produce until sold at which point ownership transfers to the buyer. The agent is required to act in the interests of the supplier. A sale under an agency agreement is from the supplier to the buyer. The commission on the transaction is subject to GST as it's a payment for a service.
  - b. A merchant buys the produce from the supplier for a price agreed in writing prior to despatch of the produce conditional on it meeting agreed specifications. Ownership passes to the merchant on receipt. The merchant is then entitled to whatever profit made on the sale, or conversely must accept the loss.

The Chamber could not agree with the above definition of a merchant on two grounds:

- a) Ownership - That in accordance with the Sale of Goods Act and existing practices parties may wish to retain the option of a method of merchant trade that allows for ownership to change just prior to the sale of the produce to a third party;
- b) Price - That this method of merchant trade allows for price to be determined by the marketplace after the produce is in the possession of the merchant.

*NFF/HAC could not agree with proposed use of the alternative merchant option because:*

- a) *The use of a alternative merchant option perpetuates the existing relationship ambiguity and commercial disadvantage to growers.*
  - b) *There is no price security for growers as price would be determined after the produce had passed into the control of the merchant thereby preventing reconignment to another trader or renegotiation of price.*
  - c) *The grower continues to carry all commercial risk from the time the produce is dispatched to acceptance by the merchant's buyer;*
  - d) *If the merchant doesn't wish to operate as a merchant as defined by NFF/HAC the merchant has the option to act as an agent; and*
  - e) *The trader would have the sole right to determine the method of merchant trade to be used*
2. The election of how the trader acts (as an agent or merchant) in regard to a specific transaction, or seasonal transactions, shall be a matter of written agreement between the two parties. Irrespective of any agreement between the two parties, it is how the trader acts in regard to that transaction, not how he purports to act, that defines by

which arrangement he has operated.

**The Chamber could not agree to the following sentence under 2:**

- a) *In the event that a trader accepts a consignment of produce from the supplier without having agreed to a specific method of trade, that method shall be deemed to be an agency agreement.*
3. Traders shall not act under any agreement that combines any other of the features of both in relation to the same trade. In the event of it being agreed in advance that a consignment shall be split with the two parts sold under agency or merchant transactions, each will be treated as a separate transaction.
  4. Agents are responsible for ensuring that at the time of sale a record containing the following is prepared and that a duplicate is delivered to the supplier as a tax invoice either within 24 hours of the produce being sold or at the time of payment.
    - a. The date of the first point of sale
    - b. The type, quantity and count or size of the produce traded.
    - c. Price received for each grade/size
    - d. Commissions and other deductions, including any GST component
    - e. The purchaser of the produce
  5. Merchants are responsible for providing a record that details the purchase of the produce from the supplier at a time agreed to by the parties. Such a record would include:
    - a. The price agreed
    - b. Date of receipt by merchant; and
    - c. Any deductions that were agreed by the two parties
    - d. Any statutory deductions (eg levies)
  6. Traders will be responsible for making and keeping stock records in respect of each consignment handled by them specifying the identity of the supplier, details of produce traded, the price received and the identity of the buyer. In accordance with ATO requirements, these records must be retained for five years.
  7. Traders will publicise with all reasonable particularity the Terms of Trade of which they conduct their business in respect of consignments and ensure that all their suppliers receive a copy of the current Terms of Trade, which will be reissued whenever the Terms of Trade change.
  8. Traders will agree with suppliers all fees and charges that the trader's may charge for services such as commission, stacking, sorting and storage fees and the like. Such fees and charges will not include statutory levies or costs, such as freight, that are the responsibility of the supplier. Agreements with suppliers will specify in writing the deductions agreed by the parties. Costs not so specifically agreed shall be met by the trader.
  9. Traders shall advise their suppliers of any required produce specifications. Such specifications shall be in clear language and reflect the specifications of the trader's principal retail buyers.
  10. Suppliers are responsible for ensuring that their produce meets the agreed specifications, for accurately describing to the trader the produce being consigned (including quantity, grade and size) and for identifying any specification shortfalls known at the point of consignment.
  11. Any agreement between the two parties shall carry an implicit warrant by the supplier that he has free and unencumbered right to sell the produce consigned and that it meets relevant food safety standards.

12. Suppliers shall advise the trader, preferably in writing, the intention to consign produce and the details of the consignment. The supplier shall not supply produce without the agreement of the trader and the trader's agreement on the method of trade and the price if to merchant. The supplier shall confirm in writing to the trader the despatch of each consignment, consignment note number and the transport details.
13. Where parties agree a minimum price for the produce in an agency transaction the agent shall not sell below this price without the approval of the supplier.
14. In the event of a dispute between suppliers and traders, there should be a genuine attempt, consistent with the Retail Grocery Industry Code of Conduct, by the two parties to resolve the matter between themselves within a reasonable period. If this is not possible the matter may be referred to either the RGIO, another means of dispute resolution or for hearing by a court of competent jurisdiction.
15. When a dispute is notified to the RGIO, both parties shall upon written request of the RGIO provide all documents relating to the transaction including those required under clauses 4 (for agents only) and 5 (for merchants only). In the event of either party refusing to enter into mediation, supply relevant documents and any other assistance, the matter shall be decided in the other party's favour.
16. Any claim by a trader that produce received is out of specification will be forwarded by fax or email to the supplier within a timeframe agreed to in advance in accordance with specifications and product characteristics.
17. In the case of dispute regarding produce quality, either party has the right to appoint (where available) by the close of business the same day or by a time otherwise agreed by both parties a mutually agreed and qualified third party to provide an independent and binding assessment of the quality of the produce to determine whether the produce is or is not within specification. The assessor shall report by noon the following day. The party that receives the report from the assessor will forward a copy to the other party. The supplier will meet the cost of the assessment if the produce is deemed to not be within specification and by the trader if it is within specification.
18. In the event the produce is shown by independent assessment, or is agreed by the supplier, to be out of specification, the supplier and trader shall decide if the produce is to be disposed of (and disposal certificate provided to the supplier as requested), returned to the supplier, or sold at a lesser price. The supplier shall meet the cost of disposal, or of any required rework.
19. Legal action is to be taken in a court of competent jurisdiction from the State in which the action is initiated.
20. Agreements between suppliers and traders shall specify the means and timing of payments, the last being no later than 28 days.
21. All suppliers and traders shall implement and maintain a HACCP-based food safety and quality system that is subject to an annual independent audit.



**APPENDIX B: QUEENSLAND PRODUCTION SECTOR QUESTIONNAIRE**



**FAX BACK SURVEY OF HORTICULTURAL GROWERS**



A CDI Pinnacle Management Project for QFVG Ltd

Know-how for Horticulture™

- Horticultural Value Chain Analysis & Policy Development -

**PRIVACY STATEMENT:** The aggregated results of this survey will be used by QFVG to assist in the QFVG/HAL project *HG03071 Horticultural Value Chain Analysis and Policy Development*. Authorised QFVG officers and the survey consultants will have access to this information but your personal details are not requested in this survey. If provided, your personal details will not be disclosed to a third party without your consent unless required by law. All personal information will be deleted from the survey records before their release by the consultants to QFVG. No names, addresses or telephone numbers will be used for marketing purposes.

1. At what postcode is your principal business location? \_\_\_\_\_

2. What are the major crops you grow?

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3. Within your industry, what size growing operation would you consider yourself to be? (tick one box only)

- Very small grower
- Small grower
- Medium grower
- Large grower
- Very large grower

4. In respect of your production, do you do any of the following? (tick all applicable boxes)

- Grow independently of any other growers
- Grow as part of a supplier network
- Have other growers who supply you
- Grow as part of a cooperative
- Other (please specify) .....

5. Do you produce / grow or involved in any of the following other business activities? (tick all applicable boxes)

- Sugar
- Beef
- Grains / Oilseeds
- Aquaculture
- Non-agricultural activities
- Other (please specify) .....

**What percentage (%) of your overall horticultural sales turnover is sold to the following by you?** (total should equal 100%)

- ..... % Wholesalers (agents/merchants)
- ..... % Brokers
- ..... % Retailers (directly)
- ..... % Processors
- ..... % Packhouses owned by other growers – on spec
- ..... % Packhouses owned by other growers – on contract
- ..... % Exporters
- ..... % Direct to the public
- ..... % Other (please specify)
- .....
- .....

**6. Based on the last 12 months, what percentage (%) of your product is delivered to these market destinations?** (total should equal 100%)

- ..... % Local
- ..... % Queensland
- ..... % NSW
- ..... % Victoria
- ..... % SA
- ..... % WA
- ..... % TAS
- ..... % Export

**7. How would you rate your satisfaction with the following aspects of dealing with particular customers in the supply chain, on a scale of 1 to 5 (1 being very poor and 5 being excellent)?** (Only rate those sectors with which you deal).

Aspect	Satisfaction rating (1=very poor, 5=excellent)			
	Wholesaler	Exporter	Processor	Retailer
Adding value to your business				

Knowledge of markets				
Price transparency				
Giving you consumer feedback/market signals				
Communication of information				
Providing information on new products / packaging / other sources of innovation				
Maintaining the integrity of the QA/cool chain				
Being active in assisting you make planting / harvesting decisions				
The cost of doing business (fees, marketing etc)				
Overall satisfaction				

**Please provide reasons for your overall level of satisfaction with the service provided by each of your customers in the supply chain.**

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**8. If selling your product to a wholesaler, what do you believe is the percentage (%) of the gross sale price they deduct from your return? (tick one box only)**

- 5-10 %
- 11-12 %
- 13-15 %
- 16-20%
- 21-25%
- More than 26%

**9. How are you advised or have confirmed to you prices to be paid by a wholesalers? (tick all applicable boxes)**

- By phone

- By fax
- By internet / email
- When payment is received
- Other (please specify)

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**10. From arrival time at the moment, how long on average does it take for you to receive confirmed prices from your wholesaler? (tick all applicable boxes)**

- Same day
- 1 day
- 2-3 days
- 4-5 days
- 6-10 days
- Greater than 11 days after delivery
- Other (please specify)

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.....

**11. What is the average period that it takes a wholesaler/s to pay you for your produce? (tick one box only)**

- 1-7 days after delivery
- 8-14 days after delivery
- 15-21 days after delivery
- 22-28 days after delivery
- 29-42 days after delivery
- Greater than 42 days after delivery

**12. What is the average period that it takes a processor/s to pay you for your produce? (tick one box only)**

- 1-7 days after delivery
- 8-14 days after delivery

- 15-21 days after delivery
- 22-28 days after delivery
- 29-42 days after delivery
- Greater than 42 days after delivery

**13. What is the average period that it takes an exporter/s to pay you for your produce?** (tick one box only)

- 1-7 days after delivery
- 8-14 days after delivery
- 15-21 days after delivery
- 22-28 days after delivery
- 29-42 days after delivery
- Greater than 42 days after delivery

**14. If given the opportunity, what would like to see changed in the way that others do business with you in terms of marketing of the produce that you grow?**

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**15. What are the main trends you see affecting the way you do business in the next 3 to 5 years?**

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16. Are there any services or information that QFVG could provide to you that would assist you in the marketing of your produce, e.g. information provision, skills training, consumer information, group formation?

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17. Additional comments

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**END OF SURVEY, THANK YOU!**  
**PLEASE FAX BACK TO (07) 3217 6905 OR**

MAIL TO CDI PINNACLE MANAGEMENT, PO BOX 1800, MILTON Q. 4064

## APPENDIX C: INDUSTRY CONSULTATION RESULTS

### SURVEY RESPONDENT LOCATIONS

Sixty surveys were completed identifying the location of respondents by postcode. The results are shown below in Table 8. They indicate the spread from across Queensland's horticultural region, albeit with some poor response rates from some areas.

<b>Table 8: Survey Respondents Location by Region</b>			
Region	No. of Responses	Region	No. of Responses
Brisbane	4	South Burnett	1
Lockyer / Fassifern	12	Central Burnett	3
Granite Belt	3	Wide Bay Burnett	6
Eastern Darling Downs	1	Central Coastal / Inland	2
Western Darling Downs	2	Bowen/Gumlu/Whitsundays	1
Cooloola / Sunshine Coast	12	Burdekin / Charters Towers	3

### MAJOR CROPS GROWN

Respondents indicated the diversity of the horticultural industry with a total of 42 different crops being produced by the 60 respondents. A further 4 non-horticultural crops were also produced. Based on the 113 crop type responses this equates to just under three different crops per enterprise.

<b>Table 9: Crops Grown by Survey Respondents</b>			
Crops grown	No. of respondents	Crops grown	No. of respondents
Apples	1	Pawpaw	1
Avocados	7	Parsley	1
Bamboo	1	Passionfruit	1
Bananas	5	Peanuts	2
Beans	1	Persimmon	2
Beetroot	2	Pineapples	2
Brassica	3	Potatoes	10
Cabbage	3	Pumpkins	5
Carrots	3	Rambutans	1
Celery	1	Silverbeet	2
Chillies	1	Snowpeas	1
Chokos	1	Soybeans	1
Citrus	5	Squash	1
Cucumber	3	Strawberries	5
Dolichos	1	Swedes	1
Leafy vegetables	1	Sweet corn	5
Lettuce	1	Sweet potato	2
Low chill stone fruit	5	Table grapes	5
Lucerne	2	Taro	1
Lychees	1	Tomatoes	3
Mangoes	7	Watermelon	4
Melons	1	Wheat	1
Onions	2	Zucchini	1

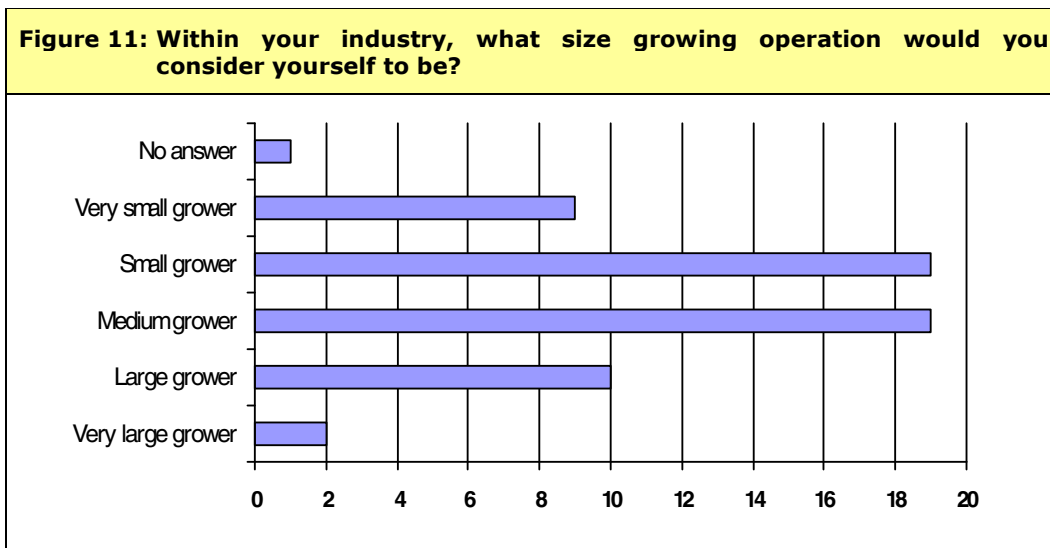
As demonstrated in Table 10 there is a relatively equal mix of fruit and vegetable crops produced by the respondents. This means in effect no bias towards one grouping or another.

<b>Table 10: Crops grown by survey respondents?</b>		
<b>Crops grown</b>	<b>No. of responses</b>	<b>% of all responses</b>
Fruit	53	45%
Vegetables	60	51%
Non-horticulture crops	6	4%

### SIZE OF OPERATION

The majority of survey respondents are either small or medium sized growers (19 each; 63 per cent collectively) with an equal share (10) being either very small or large growers. Whilst no comparative statistics have been compiled previously using these characteristics to describe the size of business operation, it is apparent that we received input from a broad range of business sizes for this survey.

Producers are often reluctant to provide details on the size or turnover of their farming operations, even if using turnover bands.



### STRUCTURE OF BUSINESS OPERATION

Fifty-three of the 75 respondents (71 per cent) are growers who produce independently of all others. Interestingly however were the 11 respondents who indicated that they were growers who were part of a supplier network and, conversely, six growers had other growers who supplied them. These results highlight the high level of independency of growers. However, it is also useful to note that there is an emerging consolidator / network grower type of business model being developed within Queensland.

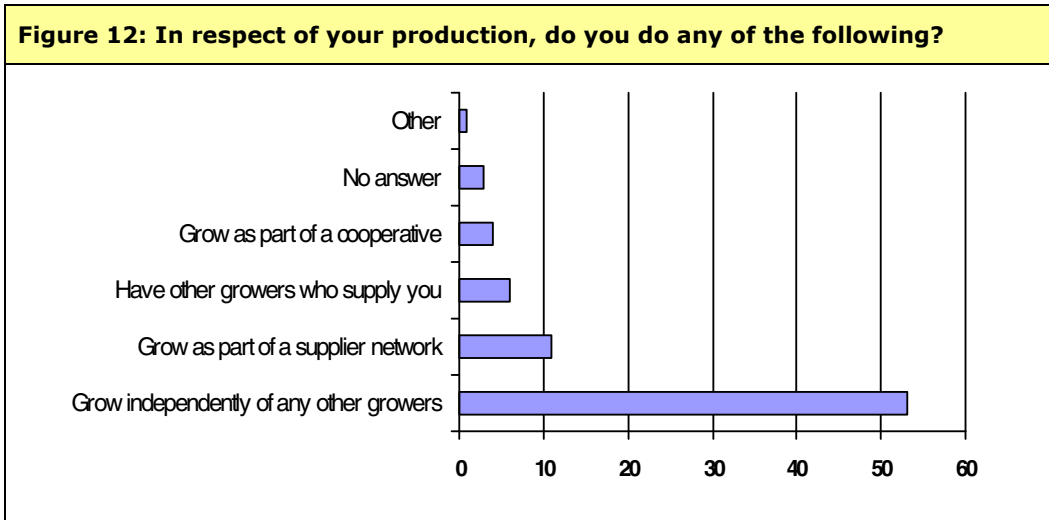
Anecdotally, consolidator / network grower models are continuing to emerge across Queensland, mainly in response to the increasing desire by the major retail chains to source product directly from suppliers and / or to use fewer suppliers.

The Lockyer Valley has a number of consolidators / very large growers including Mulgowie Farms, Hood Farming, Vege-Fresh, Quali-Pak and Durham Farms, all of whom who have some level of consolidation in their farming activities.

Other examples of consolidation through branding and / or sharing of capital include Sweetee Citrus and Gaypak, Table Grapes Australia, Australia Fresh Mango and Select Melon Co-op.



Whilst not tested, industry has also suggested that there is currently a dearth of expert assistance available to assist with the formation of new entities that involve collective grower action. This is an area that warrants further investigation.

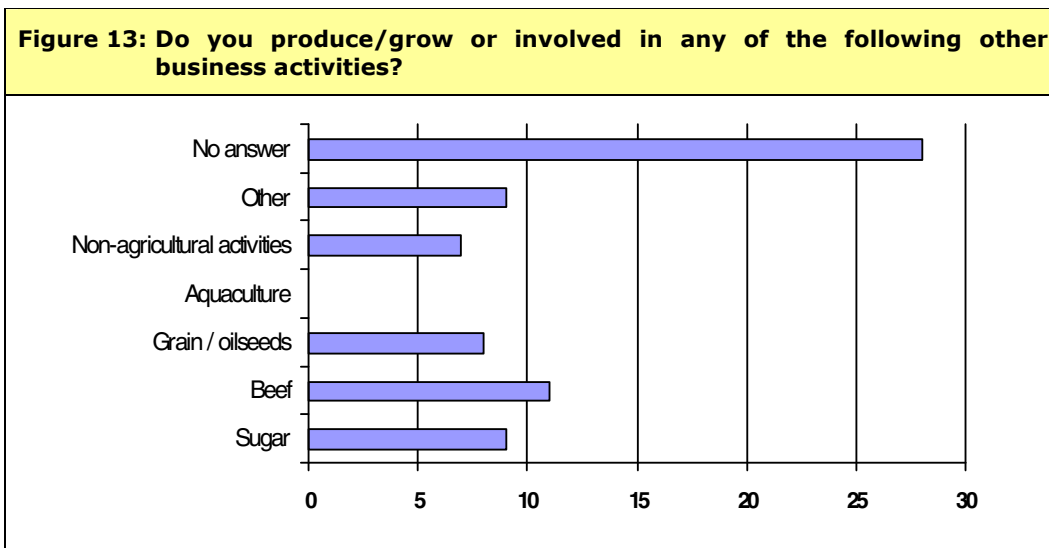


**OTHER BUSINESS ACTIVITIES**

More than half of the respondents have business activities other than just horticulture. Between eight and 11 respondents were involved in either grains / oilseeds, beef or sugar production, with a similar number involved in unspecified or non-agricultural activities.

Diversified businesses allow for greater risk spreading, particularly in horticultural businesses that produce without having firm orders for the products that they grow.

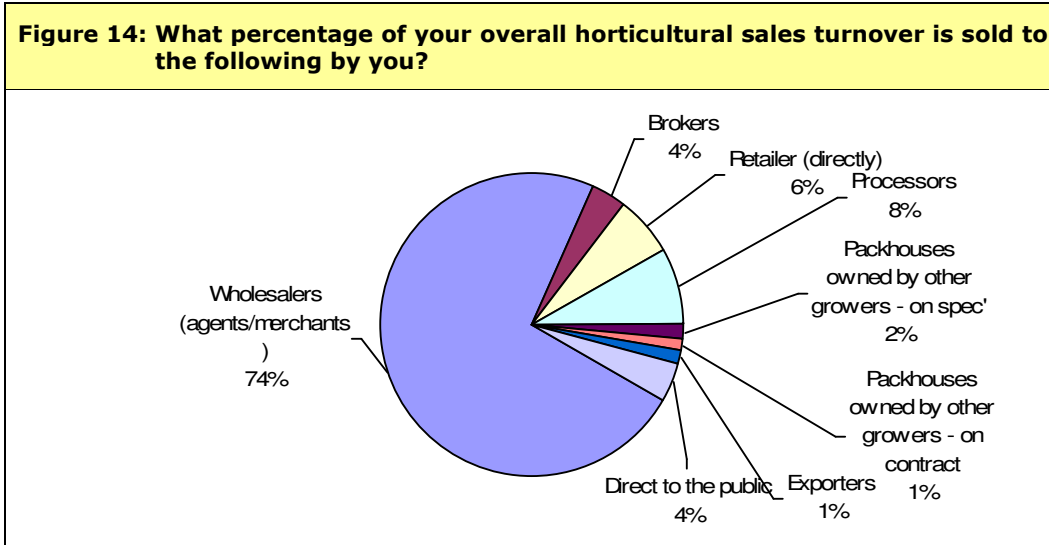
Some concern has been raised in relation to the entry of formerly non-horticulturists into a marketplace already heavily oversupplied. The recent poor performance of the sugar industry has industry leaders concerned about the movement of growers from that sector to horticulture, especially vegetable crops.



**WHERE IS PRODUCE SOLD?**

Of those surveyed, 74 per cent of the horticultural sales turnover were sold to wholesalers with the next most significant groups being to processors, direct to retailers, brokers and then the public.

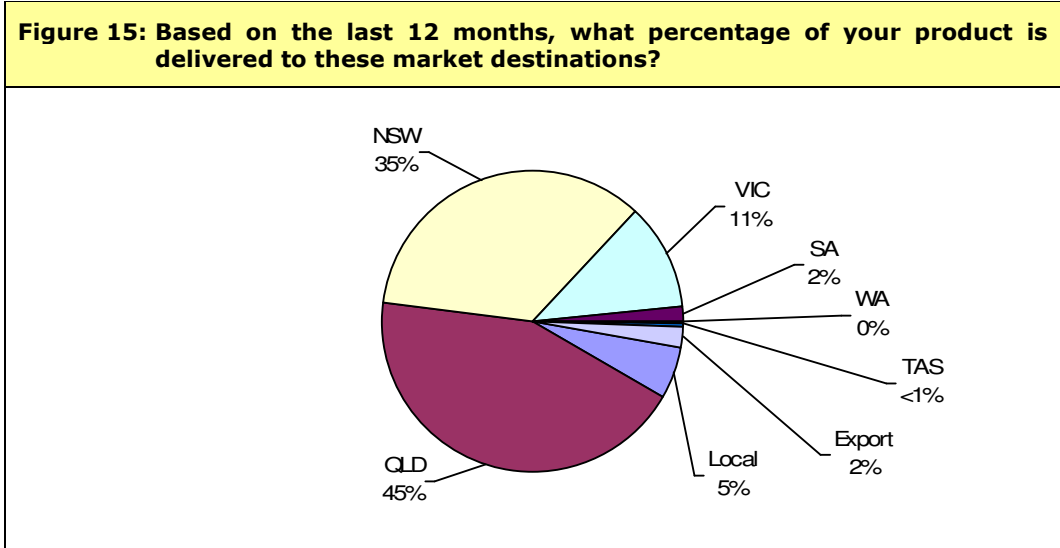
These figures do not include sales which are effectively direct to the retailer, using the wholesaler solely as a transaction / distribution point.



**PRODUCT DESTINATIONS**

Queensland remains the principle market destination for produce produced in Queensland, followed by New South Wales and Victoria. Interestingly only 2.2 per cent of the survey respondents indicated that their produce was exported, as compared with a national average of 13.3 per cent. This can in some way be accounted for by the prevalence of exporters purchasing product off the wholesale market without the knowledge of the producer.

Upon closer examination of producer size versus market destination there is evidence of a decreasing quantity of produce being sent to nearby markets as producer size increases. This suggests, but not confirms, that larger producers have a greater awareness of market signals and / or propensity to explore sales options beyond Queensland borders. These arguments are consistent with general industry beliefs in this area.



**Table 11: Cross-tab of percentage of product that is delivered to these market destinations by relative grower size?**

Size of Grower	Local	QLD	NSW	VIC	SA	WA	TAS	Export
Very small grower	12.2%	37.8%	41.1%	8.9%	0.0%	0.0%	0.0%	0.0%
Small grower	6.1%	47.8%	33.2%	10.7%	1.1%	0.8%	0.0%	0.3%
Medium grower	5.0%	39.7%	39.6%	8.6%	0.8%	0.0%	0.0%	6.3%
Large grower	0.7%	55.6%	19.4%	17.1%	5.2%	1.0%	1.0%	0.0%
Very large grower	0.0%	25.0%	45.0%	20.0%	5.0%	0.0%	2.5%	2.5%
<b>Percentage of Totals</b>	<b>5.5%</b>	<b>43.7%</b>	<b>34.9%</b>	<b>11.3%</b>	<b>1.7%</b>	<b>0.4%</b>	<b>0.3%</b>	<b>2.2%</b>

**PRODUCERS SATISFACTION WITH CUSTOMERS**

The level of satisfaction of dealing with the various customers of producers was tested across a number of aspects. Whilst 56 responses were received in relation to wholesalers only nine were received about exporters. As a result caution must be expressed in taking too much out of the results for exporters.

Overall the results indicated that the producer sector is generally not satisfied with the performance of their customers. This result may not be surprising to some but there are a number of results which may be contrary to industry opinion. These include:

- Wholesalers are regarded quite highly (rating = 3.6, the highest score) for their knowledge about the markets and marketing system.
- Price transparency (or lack thereof) was relatively consistent across the four marketing channels.
- Wholesalers ranked highest in terms of their ability to give market signal or consumer feedback. It is expected that the market signals aspect of the question was the reason for the high ranking.
- Retailers are regarded worst at communication of information with processors and wholesalers ranking relatively highly.

- All customer groupings ranked poorly (ranking = 1.6–2.3) in their ability / willingness to provide information on different forms of innovation which producers can utilise in their businesses.
- Processors were ranked highest in terms of their ability to maintain the cool chain, with the other sectors ranked between 2.4 and 2.8, which should be regarded as unsatisfactory.
- Processors would be expected to be highly involved in assisting producers to make planting and harvesting decisions, so hence the ranking of 3.0. Why the ranking was not higher is possibly due to the fact that many processors source product from growers effectively as a by-product of the 'fresh for market' operation. In other states such as Victoria and New South Wales it may be expected that this rating would be higher for processors due to the higher predominance of dedicated processing growers. The low ranking for retailers involvement in making planting and harvesting decision is possibly not surprising.
- All groupings ranked poorly in terms of their ability to provide good return for costs of services provided, although no one sector stood out as being particularly bad, if we discount the exporters ranking

In total each customer segment ranked relatively poorly, suggesting that there is considerable room for improvement across a broad range of areas. However, when spoken to, these four sectors also commented unfavourably about the business skills of producers. This confirms previous views that the level of co-operation and satisfaction of each of the sectors with the others is not high. This further suggests that there is considerable scope for collective improvement.

<b>Table 12: How would you rate your satisfaction with the following aspects of dealing with particular customers in the supply chain, on a scale of 1 to 5 (1 being very poor and 5 being excellent)?</b>				
Total responses = 48	Average score (1 being very poor and 5 being excellent)			
Aspect	Wholesaler	Exporter	Processor	Retailer
<b>Number of responses</b>	<b>56</b>	<b>9</b>	<b>15</b>	<b>19</b>
Adding value to your business	2.5	2.4	2.6	2.4
Knowledge of markets	3.6	3.1	3.5	2.9
Price transparency	2.6	2.3	2.5	2.7
Giving you consumer feedback / market signals	3.0	2.4	2.5	2.3
Communication of information	3.0	2.7	3.1	2.4
Providing information on new products / packaging / other sources of innovation	2.0	1.9	2.3	1.6
Maintaining the integrity if the QA / cool chain	2.8	2.4	3.5	2.8
Being active in assisting you make planting / harvesting decisions	2.6	1.9	3.0	1.9
The cost of doing business (fees, marketing, etc.)	2.5	2.0	2.6	2.7
<b>Overall satisfaction</b>	<b>2.9</b>	<b>2.4</b>	<b>2.9</b>	<b>2.4</b>

## **PRODUCER REASONS FOR DISSATISFACTION WITH SERVICE PROVIDERS / CUSTOMERS**

Producers offered a wide variety of reasons pertaining to their level of satisfaction / dissatisfaction with their current service providers / customers.

The key issues highlighted by the survey were:

1. Lack of price and channel transparency, primarily at the wholesaler level.
2. Communication (both good and bad).
3. Limited impact / power in the value chain.
4. Supermarket power and returns policy impacting on growers and wholesalers.
5. Provision of information that will add value to a producers business.
6. Relationship development (both good and bad).

In discussing these results with a number of growers representatives it was commented that the issues raised would have been very similar if the same questions were asked a decade or generation ago, with the possible exception of the impact of supermarkets.

In making recommendations about how these issues might be able to be addressed, they should be considered in the light of other questions and responses from this survey.

These issues can be summarised in a few key words: **communication, information, systems and relationships.**

1. **Communication:** A central barrier to good communication are good interpersonal and people management skills. Producers, like all sectors, have a variable level of skills in these areas, but the development of which is central in today's world for the development of successful businesses.
2. **Information:** Gaining access to information, whether it be market prices, access to the latest farming techniques or management issues, is critical success factor in today's business environment. In years past, producers relied on others to supply all the information that they needed. Gaining an 'edge' was not as critical as most growers were able to earn a respectable income, since information and logistical technologies effectively isolated growers from other regions. Production technologies were not as well developed so yields were lower. Post-harvest technologies were not as advanced so losses were more frequent and higher. Government departments, input supply companies had the on the ground resources to assist farmers on a regular basis. This has now all changed and producers must now increasingly go out and be more pro-active in seeking information. The main issue for many farmers is how do they start accessing this information.
3. **Systems Development:** Once again the production sector is increasingly being forced into the awareness and development of systems. This can include maintaining greater numbers of records for workers, quality assurance scheme compliance, 'recipes' for the production of fruit and vegetables. Some producers have embraced the challenge associated with developing such a mindset, others have struggled. It has been commented that in many instances they do not know where to start. This may be a role where others need to assist the production sector.
4. **Relationships:** Some growers believe that they consider they have excellent relationships with their customers whilst others do not. Why? Some would argue that some growers do not have the necessary tools to firstly identify a customer who can add value to their business and secondly, do not have the skills to nurture and develop that

relationship. Concurrently, it may be argued that others in the supply chain also may not have communication and relationship management skills.

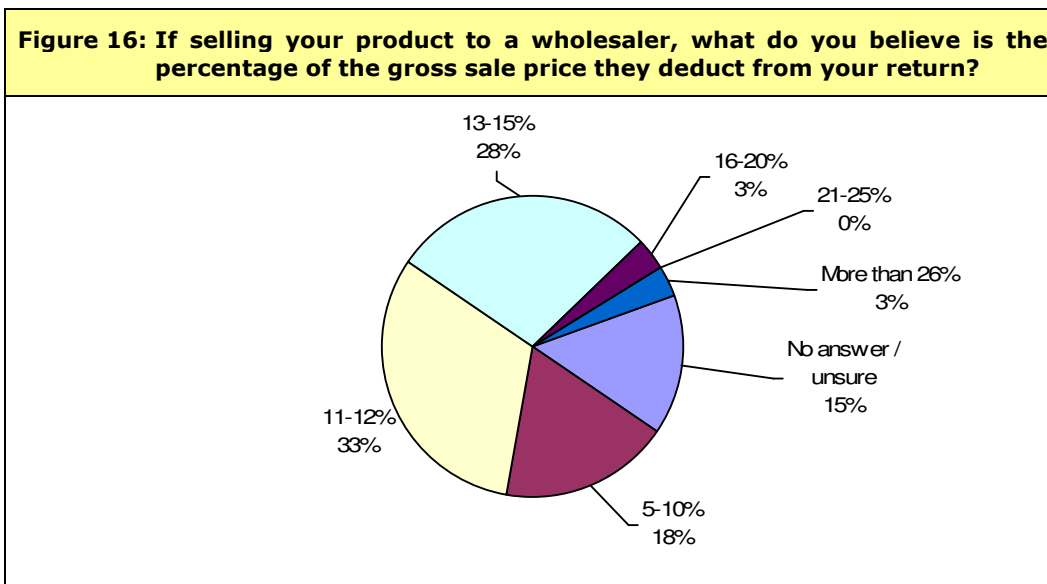
Relationship and negotiation management skills both from the results of this survey and other anecdotal evidence for producers are key skills areas that producers require assistance with.

**WHOLESALE MARGINS**

The majority of producers (61 per cent) believe that wholesalers deduct between 11 and 15 per cent on average of the gross sales price. It must be noted that this in general is a perception (as opposed to detailed knowledge) due to the generally low level of price transparency between these two sectors. Other anecdotal evidence confirms that the average figure (in Brisbane) is in the range of 12.5–14.0 per cent. Figures are slightly higher in Sydney and Melbourne based on industry accounts.

Interestingly and not surprisingly, 15 per cent of respondents were unsure of the level of deductions that wholesalers made from growers returns.

Also 18 per cent of respondents of indicated wholesalers on average took 5–10 per cent in deductions. This response might indicate the lack of knowledge some producers have regarding wholesaler deductions, as no wholesaler will over a period be expected to take these figures and be expected to be viable.



**PRICE ADVICE BY WHOLESALEERS**

The survey asked respondents how they are advised or have confirmed prices to be paid to them by a wholesaler. A total of 48 respondents answered this question with multiple responses allowed. Telephone confirmation of prices received the highest number of responses with 67 per cent, followed by fax with 29 (60 per cent) and 'when payment is received' with 26 (54 per cent).

Many producers receive price confirmations by phone and then have prices confirmed subsequently by fax or when payment is received. The problem with confirmations by telephone are that in the event of disputation, phone notations on prices are not an accepted method of evidence.

Producers are regularly urged to ensure that they receive a hard copy of the prices received either via facsimile, internet or by mail.

It would be of concern to industry organisations the number of responses indicating that payment is only confirmed when they receive the cheque / deposit.

In light of the 'information age' the very low figure for confirmations by email / internet (6 per cent) suggest that either producers and / or wholesalers are being slow in adopting these methods to advise / confirm prices.

Price confirmation therefore remains as a critical area of improvement for the producer – wholesaler relationship.

**Table 13: How are you advised or have confirmed to you prices to be paid by a wholesaler?**

Method of advice	No. of responses	% of respondents N=48
No response to question	4	8
By phone	32	67
By fax	29	60
By internet / email	3	6
When payment is received	26	54
Other	6	13
Total*	100	48

\* includes multiple responses, total no. surveys = 48

### PRICE CONFIRMATION TO PRODUCERS FROM WHOLESALERS

There was a wide response in the average time period that wholesalers take to advise growers of prices received for product. Twenty-three per cent of respondents indicated they were advised on the same day of delivery, with a relatively equal percentage up to more than 11 days (6.8–12.2 per cent).

Industry sources suggest that the average turnaround time for the sale of produce varies depending on the nature of the product, from same day for highly perishable commodities to 3-5 days for less perishable commodities.

**Table 14: From arrival time at the market, how long on average does it take for you to receive confirmed prices from your wholesaler?**

Time taken to receive confirmed prices	No. of responses	% of all responses
No response to question	7	9.5
Same day	17	23.0
1 day	6	8.1
2-3 days	9	12.2
4-5 days	6	8.1
6-10 days	5	6.8
Greater than 11 days	8	10.8
Other	16	21.6
Total*	74	100%

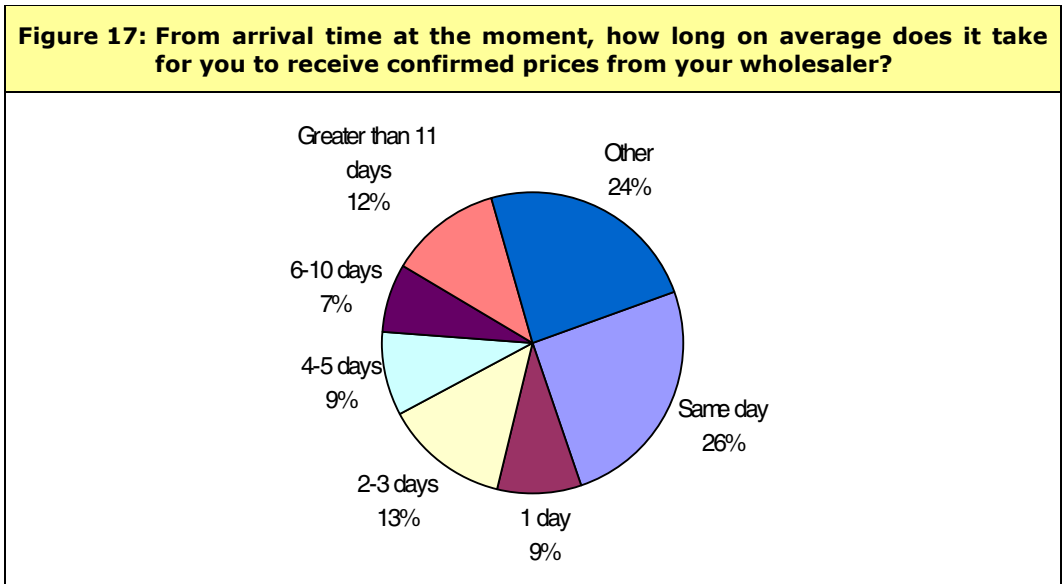
\* includes multiple responses, total no. surveys = 60

Wholesalers sometimes do not advise growers immediately of prices received for produce in order to examine movements of prices over a longer period. In effect some wholesalers will

seek to 'average' prices over a period, often a week, so as to ensure a reasonable return to his business.

For instance, as one wholesaler commented, a wholesaler may be able to sell produce at an above average price early in the week but may be forced to sell product at a lower price than what the grower might expect later in the week for a variety of reasons. The wholesaler is concerned about maintaining the relationship with his grower, so will have a tendency to average the price, rather than display a high variability in prices.

Significantly there were a high number of responses indicating an 'other' response in terms of time period to notification. This suggests that either growers are not advised of prices which may be possible given the high response rate to the previous question about how prices are advised to growers.



**PAYMENT PERIODS BY CUSTOMERS**

Only the responses for wholesalers should be considered to this question given the low response rate to processors and exporters.

Over 75 per cent of responses indicated that wholesalers on average paid growers more than 15 days after delivery, the normally 'acceptable' period by industry.

Generally accounts in other industries are either 14 or 28 days. If the latter is viewed as acceptable, still more than 27 per cent of wholesalers are on average outside of these payment terms.

This lack of credit management by producers, often by businesses that have high turnovers due to high labour costs should be regarded as both unacceptable by the production sector and an area for improvement.

Producers lack of credit management can be attributed to in many instances the lack of and enforcing of agreements which detail acceptable terms of trade.

**Table 15: What is the average period that it takes a wholesaler/s, processor and/or exporter to pay you for your produce?**

Average Time Period	Wholesaler	Processor/s	Exporter



**Table 15: What is the average period that it takes a wholesaler/s, processor and/or exporter to pay you for your produce?**

No answer	3	42	52
1-7 days after delivery	2	0	0
8-14 days after delivery	11	2	1
15-21 days after delivery	12	2	1
22-28 days after delivery	19	1	0
29-42 days after delivery	13	9	4
Greater than 42 days after delivery	5	4	1

### **ASSISTANCE IN BETTER VALUE CHAIN PERFORMANCE FOR PRODUCERS**

Producers highlighted a broad range of areas where the value chain can perform better to their and others benefit.

The key issues highlighted by the survey were:

1. Lack of price and channel transparency, primarily at the wholesaler level.
2. Enforceable government regulation or action – chain performance, imports, quality assurance, price regulation
3. Communication – interpersonal, pricing
4. Supermarket power and returns policy impacting on growers and wholesalers
5. Provision of information that will add value to a producers business
6. Relationship development with others in the chain
7. Supply chain co-ordination
8. Compliance – workers, quality assurance, quality
9. Promotion of fruit and vegetables.

Issues associated with government regulation and 'power of supermarkets' pre-suppose that the government has the willingness to introduce regulation into the marketing system. Experience shows with the Baird and Buck report outcomes that government are focussed on self-regulation. This extends to imports as well, beyond where there are demonstrable impacts on quarantine matters.

### **FUTURE TRENDS IMPACTING PRODUCERS BUSINESSES**

Producers identified a number of trends that impacted the way that they do business in the future. These can be summarised as:

- Imports
- Sustainable production systems
- Shortened value chains
- Supply management issues, e.g. oversupply, all year round supply
- Increased production costs - general
- Wage availability and costs
- Innovation –varieties, packaging

- Compliance
- Water availability.

#### **ROLE OF GROWCOM IN PROVIDING ASSISTANCE**

Producers identified a number of areas where industry organisations such as Growcom could / can be of assistance to them. These assistance areas can be summarised as:

- Providing access to information, e.g. pricing
- Negotiations on behalf of producers on whole-of-industry matters, e.g. mandatory codes of conduct, wage negotiation
- Skills training
- Industry and product promotions
- Solutions provision / development, e.g. achieving greater returns for producers
- General information provision.

## APPENDIX D: CONSULTATION LIST

Surname	Christian Name	Firm / Organisation
Brewer	Trevor	Market Information Services
Confidential		Chamber of Fruit & Vegetable Industries Inc. NSW
Clarke	Robert	Favco Pty Ltd
Confidential		Woolworths
Confidential		Inner City Based Independent Fruiterer
Dunn	Rodney	Bunya View Gardens
Gray	Robert	The Harvest Company
Morton	Robert	Favco Pty Ltd
Neeland	Ian	Coles Myer Pty Ltd
Panitz	Mark	Growcom
Scurr	Gavin	Pinata Marketing
Shields	Noel	ActiveX
Silman	Ian	Private Industry Consultant
Simonetta	Michael	Perfection Fresh
Walsh	Tony	Market Gardeners Pty Ltd
Young	Andrew	Brismark Ltd

## APPENDIX E: AUSTRALIAN VALUE CHAINS – HISTORIC PERFORMANCE

The Bureau of Rural Sciences study, Chain Stocktake of Some Australian Agricultural and Fishing Industries (Peterson et al., 2000), undertook a stocktake of the competitiveness of Australia’s agrifood sector in an international context. The study used a ‘score card’ of eleven chain ‘attributes’ in its analysis of 15 selected industry chains.

The details of this report are summarised in the following sections.

### *Case Studies – Horticulture*

Table 16 below highlights the perceived performance of two groups focussed on horticultural exporting, an individual owner and Riversun Export, a consolidator of fresh citrus.

<b>Table 16: Report Card for Export of Fresh Fruit and Vegetables (Individual Exporters and a Consolidated Exporter)</b>				
	<b>Independent Owners</b>		<b>Riversun Export Pty Ltd</b>	
<b>Success Factor</b>	<b>Score (1-4)</b>	<b>Comment</b>	<b>Score (1-4)</b>	<b>Comment</b>
Awareness	3	Variable. Most production is by arrangement with an exporter and in accordance with a customer specification, though few growers would have direct contact with the customers, indeed, it is in the exporter’s interests to keep the parties apart.	4	All members of the chain, growers, packers’ etc, are committed to the export customer, and are well aware of their place in the chain.
Trust	2.5	There is a level of distrust between growers and exporters; exporters provide little value for the service they provide. While the success of the business largely depends on trust between the exporter and the importer, these relationships are often strained by poor performance at either end.	3	Transparent pricing arrangements and well developed communication systems contribute to a high level of trust along the chain.
Business Integration	3	There is little formal through-chain integration, though the use of committed growers and the cultivation of long term relationships between exporters and importers provide a strong element of business integration	4	This is a well integrated chain. While this is not expressed through ownership at various levels in the chain, the operation from production through packing, exporting, and importing is finely tuned and integrated.
Efficiency	2.5	These chains are often opportunistic and reactive, and prone to failure.	3.5	This is a well developed and managed chain with no unnecessary steps.
Customer Focus	3	The commodity focus of these chains detracts from the customer focus.	3.5	This chain is dedicated to meeting customer needs of quality, price and service. Growers are export focused to the extent of producing larger fruit for the US, and some visit the market, though this tends to be the committed few rather than the industry norm. the single-desk importer model strengthens this focus.
Transparency	1.5	There is little transparency in these chains, and in fact the parties are deliberately separated to preserve the interests of the exporters.	3	Information is freely exchanged between Riversun and its upstream and downstream partners.
Rewards	2	The reward/penalty system generally reflects market prices.	4	All participants are rewarded on the basis of their contribution to the success of the chain.

<b>Table 16: Report Card for Export of Fresh Fruit and Vegetables (Individual Exporters and a Consolidated Exporter)</b>				
Leadership	3	The chains are dominated by the exporters.	4	Strong and effective leadership provided by Riversun and its US partner, and supported by AHC who facilitated the establishment of the initiative.
Planning	1.5	There is some planning between the exporter and the grower, but through-chain planning is uncommon.	3.5	Strong planning involving Riversun and all of its up and downstream partners.
Relationship	3	The exporters select and cultivate growers and importers on the basis of performance.	4	All partners are selected and retained on the basis of their performance and contribution to the success of the enterprise.
Optimisation	2	This is a largely reactive trade that offers limited opportunity for optimisation.	3	This arrangement offers many opportunities for optimisation as a result of the added scale of operation, and its relationship with the sole importer in the US.

Source: Peterson et al., 2000

**Table 17** shows the results of a value chain analysis completed in the fruit and vegetable processing (minimal) industry.

<b>Table 17: Report Card for the Processing Fruit and Vegetables Industry</b>		
Success Factor	Score (1-4)	Comment
Awareness	3.5	Chains are short and growers are familiar with their field services, specifications, newsletters, factory visits and feedback on individual deliveries, and in many cases, through board participation and/or share ownership
Trust	2	Growers often distrust the companies, who they believe drive price and quality at the expense of grower returns
Business integration	3.5	The processing industry is highly integrated, with a high level of reliance on contracted production and dedicated supply arrangements, involving growers, storage and transport arrangements and processing. Processors do not own farms, nor usually the transport or storage facilities. Under these arrangements, production inputs (fertiliser, seed) is often also arranged by the company, or some form of grower alliance. The industry tends also to be well integrated into the research network.
Efficiency	3	While the chain has some weaknesses it is short and effective in delivering quality and value to the processors. Further efficiencies are possible through increasing the size of supply units (grower alliances?), vendor assured supplies etc.
Customer Focus	4	This chain is totally focus on the customers' needs, perhaps at the expense of other partners
Transparency	2	Companies seldom share with their suppliers, except where it suits a particular purpose. Suppliers are usually loath to share their information with their customers. SPC is the exception because of its historical origins and strong grower involvement
Rewards	4	The reward/penalty system closely reflects quality and service performance.
Leadership	3.5	The processors are dominant chain leaders.
Planning	3.5	Chains are planned by consultation between processors and suppliers.
Relationships	4	Suppliers are selected on the basis of their skills and knowledge, and ability to consistently meet company objectives of quality and service. Failure usually leads to rejection from the chain.
Optimisation	3.5	Processors use all of the optimisation tools in their drive towards best practise supply, international and industry benchmarking, research integration, field services etc.

Source: Peterson et al., 2000

### Case Studies – Domestic Supermarket Chains

Table 18 details the results based on a series of criteria the value chain performance of supermarket retailers. It must be noted that this study was completed in 2000.

<b>Table 18: Report card for domestic supermarket chains of fresh fruit and vegetables</b>		
<b>Success Factor</b>	<b>Score (1-4)</b>	<b>Comment</b>
Awareness	3	Variable. Committed growers (for supermarkets) are fully acquainted with their customer need, but there are still numbers of growers who produce 'on spec' for sale through the wholesale market system, and are therefore remote from the customer
Trust	2	Generally the level of trust is low; growers distrust the supermarket chains and (often) their market agents. Supermarkets do not enjoy the high regard of growers
Business Integration	3	Also variable. The supermarket supply chains are generally well integrated through contractual and other arrangements involving the wholesalers. There is little evidence of integration in the independent retail chains
Efficiency	3	The supermarket supply chains are judged to be 'reasonable efficient' given the wider roles of wholesalers and through-chain management. There are no obvious areas for efficiency improvement in these chains. The central market is a useful mechanism for small producers and independent retailers but it adds inefficiencies to those chains.
Customer Focus	4	The chain has been developed around the requirements of the supermarkets and their customers. Pre-prepared salads and fruit salads, snack packs and convenience packaging are clear examples of an industry response to the customer's needs for convenience and variety
Transparency	2	These are not transparent chains; supermarkets generally share information on a needs basis and suppliers will also share on a needs only basis. This varies between supermarket chains.
Reward System	3	The rewards/penalty system reflects quality and service performance, though there is widespread supplier disquiet about how this is managed.
Leadership	4	The supermarkets are dominant chain leaders, though this is translated via the wholesalers, whose role and profile in the industry are undergoing change.
Planning	3.5	Chains are planned by consultation between supermarkets and wholesales, then between wholesalers and growers. Chain partners are not equal in this process.
Relationships	3.5	Depends on the chain, but relationship management is becoming increasing important as wholesalers assume wider responsibilities (e.g. as category managers, and as managers of company quality systems). Strong relationships at all levels in the chain are important to Franklins, but the other supermarket chains have a wider and more remote grower base. The key relationships are between growers and wholesalers, and between wholesalers and retailers. Participants are selected on their ability to consistently meet quality and service requirements defined by the retailers.
Optimisation	3	This is an area of potential improvement.

Source: Peterson et al., 2000