

FOODSERVICE 2025: DIGITALIZED, DEMOCRATIZED & DISRUPTED

A LEGACY OF TIMELY WHITE PAPERS

The Hale Group and its staff have a long tradition of looking to the future of the foodservice industry and publishing white papers as a vehicle to share their point of view with interested parties. The intent is to provide those parties with a framework to stimulate their organization's internal dialogues as part of a strategic planning process.

Looking back, one can see The Hale Group's white papers are reflective of the foodservice industry's development. In each of the examples of white papers shown below, The Hale Group anticipated a major shift in the nature of supply and demand within the foodservice channel.



Bill Hale, President

The Hale Group, a strategic consulting firm serving the food industry, is privileged to share its view of the nature of the U.S. foodservice industry as it will exist in 2025.

The research and preparation of this Strategic Initiative, *Foodservice 2025*, was sponsored by The Core Group, a leading national foodservice sales and marketing agency. They sponsored this effort so their clients and those participating in the U.S. foodservice industry would be engaged in preparing for the future.

Enjoy the read and let us know what you are thinking...what you think we got right, what you would modify and what is missing. Send emails to me: bhale@halegroup.com

The Hale Group White Paper	Publication Date	General Theme
Fast Food Industry: Its Future Development	1972	Forecast and implications of a then emerging industry
Home Delivery, Drive-Thru and Take-Out	1985	Future of new service systems
BRANDS ON THE GO	1989	Exploring the deployment of QSR brands in non-traditional locations
Foodservice 2020: Global, Consolidated, Structured	2010	Anticipating the changing structure of operator demand for goods and services and implications

We are at another inflection point regarding the nature of supply and demand as it relates to the foodservice operators' demand for goods and services and how the foodservice manufacturer will provide those goods and services.

Foodservice 2025 anticipates the next major in the conduct of business in the foodservice industry and is intended to enable those doing business in that channel to engage in updating their strategic plans.

BACKGROUND

The need for foodservice organizations to look to the future and anticipate how their world will change is a continued requirement for sustainable success. In many ways, the future operating environments already exists in an embryonic fashion today – though not fully developed, the foodservice industry's future is ready to break out and disrupt existing business models, practices and requirements.

Foodservice 2025 is intended to assist leaders in foodservice organizations begin the debate on the future; form their view of the world to come; and, begin to confidently take steps to prepare for success.

Foodservice 2025 is only the starting point. The finish line is a well-thought-out, vetted strategic plan and pathway to be a winner in the new operating environment which is digitalized, democratized and disrupted.

A QUICK LOOK BACK: FOODSERVICE 2020

In 2010, The Hale Group published a white paper entitled *Foodservice 2020* (which is available on The Hale Group's website www.halegroup.com). The paper presented a point of view regarding the nature of the foodservice operating environment in 2020. Essentially, the themes which would best describe that operating environment as presented in the paper are:

- **Globalization of the Commodity Supply-Chain:** the participants in the foodservice industry would find themselves competing for commodities with other countries who had growing demand for commodities due to the rise of their middle class. This in turn would drive commodity price volatility and change sourcing patterns. In fact, we are seeing higher levels of volatility play out in the markets.



• **Accelerated Rate of Consolidation of Operator**

Purchases: the advent of GPOs and the growth of chains would result in operators aggregating their purchases through professional group purchasing organizations and / or co-ops and increasing their purchasing leverage with their vendor communities. The implications for foodservice manufacturers are bigger customers buying more product from them for longer periods of time at a lower margin. It also has organizational implications in terms of the structure of a manufacturer’s customer portfolio and their go-to-market strategy. In fact, the consolidation of operators’ product and service demand has accelerated since 2010.

Recap: Share of Operator Purchases Through a Centralized Purchasing Organization			
Forecast	2010	2016	2020
Original 2020	62%	73%	79%
Current State 2016	62%	71 - 72%	-
Reforecast 2017	62%	71 - 72%	75 - 77%

Source: 2016 acutal / Tibersoft; other data points /The Hale Group est

The actual rate of consolidation of purchases by the operator forecasted by The Hale Group remains directionally correct and it has had an impact on the foodservice manufacturing community as predicted. This move toward GPOs and co-ops has not fully played out as yet and it will continue.

A strategic implication of the consolidation of operator purchases is the purchase decision is increasingly made at a headquarters-level and the purchase decisions are made by sophisticated procurement professionals. This means a “headquarter-sell followed by a highly-proficient field execution”.

• **More Structured Relationship between Buyer and Seller:**

The third characteristic of 2020 forecasted by The Hale Group in 2010 was the rise in professional purchasing or procurement groups meant the relationship between buyer and seller was about to change as well. The professional buyer would expect and require a more structured relationship and one governed by a formal agreement, i.e. contract. RFPs (request for proposal) and contracts have now become part of the relationship.

The advent of a more contractual relationship has implications such as:



The structured relationship does not mean personal relationships are less important because personal connections are still central to the relationship. What has changed is the relationship is centered on “trust” not whether “we go hunting together.” Trust is central. Will you do as you say? Will you follow through? Will you always respect and protect our data and information?

The body of work associated with The Hale Group’s *Foodservice 2020* and the resulting white paper have been an accurate reflection of the foodservice operating environment. It provided a basis for foodservice industry participants to anticipate and plan for the changes that were predicted and in fact, have occurred.

It is now time to explore the next phase of the foodservice industry’s evolution and prepare for the changing landscape.

LOOKING FORWARD: FOODSERVICE 2025

We believe the next seven to ten years will be far more challenging than the past decade. In the past decade, it was change we recognized and could relate to because it was an evolution. The changes we face in this next decade are far more dramatic: disruption of business models; increased market complexity; far greater reliance on new technology; and, talent needs well beyond what has normally been found in foodservice organizations (and difficult to recruit and retain).

The time to start preparing for 2025 is right now. So, what will 2025 look like?

FOODSERVICE 2025: DIGITALIZED

The digitalization of data, advances in the availability and use of technology and the connectedness of the foodservice industry, starting with the consumer, will play a central role in shaping the foodservice business by 2025. The relationship between the buyer and seller, business practices and activity, and the realization of deeper insights and intelligence are all impacted.

IT ALL STARTS WITH THE CONSUMER

THERE HAS BEEN A GREAT DEAL OF DISCUSSION AND INTEREST IN THE MILLENNIAL GENERATION AND IT IS WELL-DESERVED. For the Millennials, current age of 25 to 40, represent an 80-million-person force to be reckoned with. They represent a generation coming into their higher earning years and household formation phase. They present a new set of attitudes, behaviors and expectations different than the boomers and Gen X generations that preceded them.

Of interest to the foodservice community in terms of the Millennials is their use of technology, the importance of authenticity and transparency, and the value they award to positive experiences.

The use of technology has established their relationship with the restaurants and retailers they interact with. The way they seek information and validation of the acceptability of a restaurant is determined by online approval of friends, trusted influencers and advisors. Their first instincts are to go online with their mobile devices. In this way, digital fingerprints and a data trail are created by the consumer and captured by the foodservice provider for analysis by the operator / retailer and their trading partners. It all starts with the consumer.

Consumers Seek More Restaurant Technology
% of consumers likely to use the following if offered by their favorite restaurant

	All Adults	18-34 yrs	35-44 yrs	45-54 yrs	55-64 yrs	65 yrs +
Look up restaurant location and directions on a smartphone or tablet	67%	88	78	63	60	31
Use a computer to view menus, order food, or make online reservation	63%	82	74	60	54	31
Order takeout or delivery on a smartphone or tablet	52%	74	62	45	39	20
Use a restaurant reward or special deal with a smartphone	50%	70	58	47	38	21

Source: NPD Research

The millennial's use of technology builds data bases by which real insights of consumer behavior can be captured; so, the digitalization and connectedness begin with the consumer. It allows the foodservice operator and their trading partners to shift the relationship between consumer and operator from transactional to relational; and, from shotgun marketing to rifle shot, one-to-one marketing.

DIGITAL RELATIONSHIP AND DATA CAPTURE BY OPERATOR

OPERATORS CLEARLY UNDERSTAND THEIR RELATIONSHIP WITH THEIR CUSTOMERS HAS A NEW DIMENSION TO IT AND THAT IS A DIGITAL RELATIONSHIP. This is evidenced by looking at new organizational positions in many of the major foodservice companies carrying the title of Chief Digital Officer. The CEO of Domino, Patrick Doyle, stated the key to Domino's success has been its technology platform and this will be a strategic focus for the foreseeable future. So, digitalization is key to the relationship between operator and consumer and a key part of future growth.

The accelerated rate of growth associated with off-premise occasions is supported by the use of technology. Delivery and pick-up occasions are most often conducted on a mobile device; the reviews, the menu, the ordering, use of promotions / specials and payments are all conducted via a mobile device.

The expansion of loyalty programs to engage the existing and targeted consumer are facilitated by technology.

This data is digital and available for analysis to gain deeper insight into consumer behavior and thus, provide actionable insights to strengthen the relationship between operator and consumer. At the same time, generate greater demand through tailored and targeted communications.

The operator's relationship with their customers is increasingly digital, connected and mobile.

DISTRIBUTOR'S DIGITAL RELATIONSHIP WITH THEIR CUSTOMER

THE DISTRIBUTOR'S RELATIONSHIP WITH ITS CUSTOMER, THE OPERATOR, IS ALSO MOVING TO A DIGITALIZED MODE. This is the case for both street account customers as well as their multi-unit and national accounts.

What this means for the distributor is their technology infrastructure must be highly advanced and the content they want to share with their customers must be digitalized. This will allow the day-to-day exchange of information without requiring the time and attention of a DSR. The information such as order-guide, product catalogues, product specific information of all types, promotions (general and specific), market and segment trends, new product information, recipes are all available online and do not require a DSR.

In fact, streaming videos can take the place of product cuttings to some extent, demonstration of recipe preparation and all types of other sharing of information all happen without the need for a face-to-face meeting or sales call.

Therefore, there will be fewer sales calls per customer but when a sales call is made it will be more organized, with a targeted exchange of information and a plan focused on agreed-to customer priorities and tailored product information / recommendations.

It's not that the greater use of technology and digital information will eliminate the requirement for, and

value of sales calls; but rather, it will be driven by the customers' interest in / preference for online exchange of information for the conduct of day-to-day business.

B2B Buyers Preference for Online Purchasing				
Age of Buyer	60+	46-60	36-45	18-35
Favor Online Purchasing	29%	45%	68%	90%

Source: Oliver Wyman

Oliver Wyman research illustrates B2B buyer preference for the use of technology. Technomic research has found this same preference exists in the foodservice industry consistent with other industries.

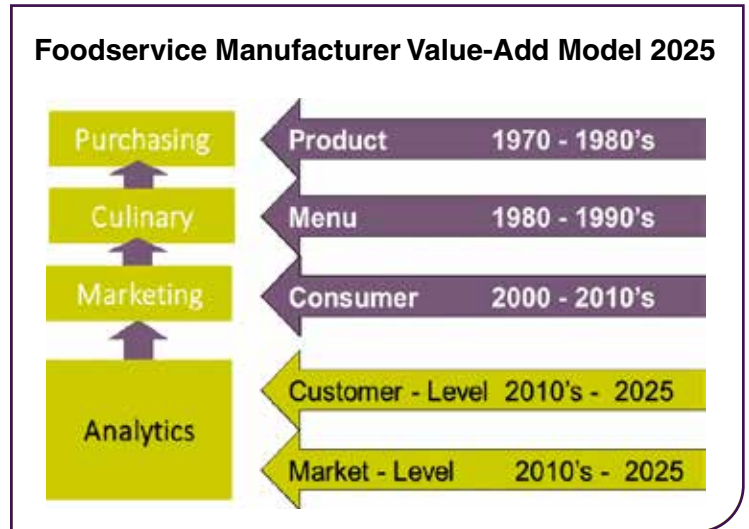
The distributor will be sharing more information with its customers in real time, and it will also be sharing more information with its vendor community. The distributor's customer, particularly its larger customers, want this information shared with the manufacturer to help with supply-chain management and improvement; and, to be analyzed for demand forecasting and preference patterns. The distributor will enable greater transparency and visibility into the marketplace and to operator specific information; this is not necessarily because the distributor wants to share the information, but because the distributor's operator customers require it. Distributors will come to see their information has value and they will look for ways to monetize and capture that value.

MANUFACTURERS EMBRACE ANALYTICS AS ITS VALUE-ADD

THE FOODSERVICE MANUFACTURER WILL BE THE BENEFICIARY OF THE DATA ROLLED UP FROM THE CONSUMER THROUGH THE OPERATOR COUPLED WITH DISTRIBUTOR TRANSACTIONAL INFORMATION AND THEN, COMBINED WITH MANUFACTURER PROPRIETY CATEGORY AND MARKET INSIGHTS.

The *Foodservice 2025* environment will be data and information rich. It will be a strategic part of the value-add proposition in 2025.

It is interesting to reflect on the evolution of the manufacturer's value-add model as shown below.



Source: The Hale Group

The primary role of the manufacturer in the 70's was to provide a desirable product consistently. It quickly moved from product to menu application and then to consumer insights to help the operator understand what the consumer in a certain setting and need-state wanted.

We now move to greater and deeper understanding of the consumers' need states and understanding what they want; and, we are also beginning to anticipate consumers wants and behaviors tapping into the value and demand generators for that unique customer in that need state. In 2025, we have moved from the use of crude tools to precision instruments.

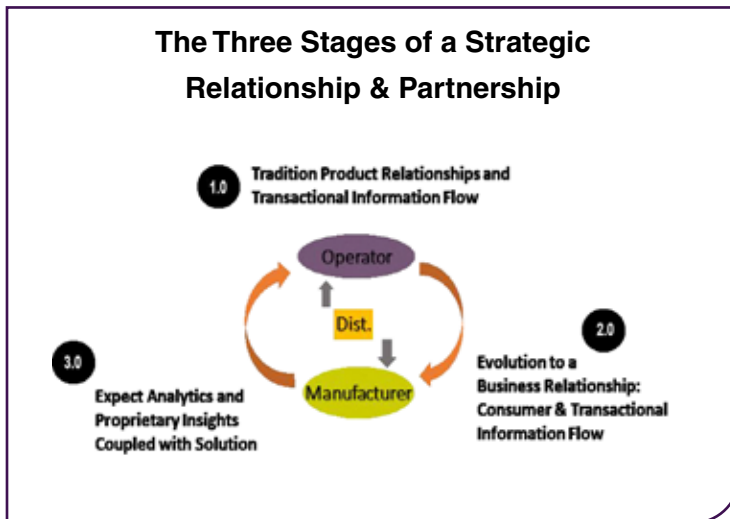
The science of analytics as the new value-add starts with data; and,

- data sources are abundant ... operator, consumer, distributor, competitors;
- data will be converted to insights and intelligence; and,
- insights & intelligence will enable a far more directed approach to opportunity selection & developing structured, actionable approaches / responses to demand creation.

The new analytical instruments and techniques will consider all aspects of the marketplace:

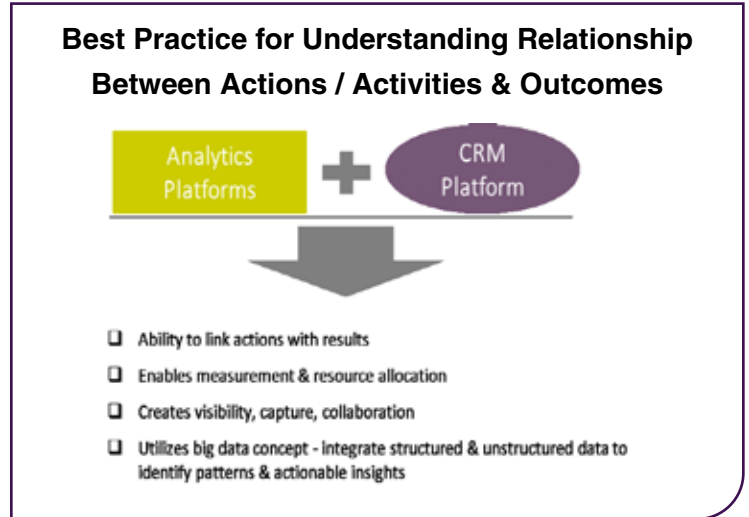
- Consumer-based ... understand behavior, usage, decision-making
- Customer/operator-based...understanding their usage, applications, opportunities, challenges
- Category-based...understanding competition, share gain opportunities
- Market-level ... understanding dynamics, segments, and geographic opportunities

The relationship and expectations between strategic trading partners has changed over time as shown below:



Source: The Hale Group

The analytics coupled with the use of an effective CRM (Customer Relationship Management) program makes it possible to capture activities and program implementation with outcomes as captured by the data.



Source: The Hale Group

By 2025, best practice will be the coupling of CRM and data analytics.

DIGITALIZED FOODSERVICE 2025: GAP ANALYSIS

THE FINDINGS, CONCLUSIONS AND RECOMMENDATIONS ASSOCIATED WITH THE HALE GROUP'S *FOODSERVICE 2025* WERE VETTED AT A ROUNDTABLE EVENT WITH APPROXIMATELY FIFTY FOODSERVICE LEADERS. Their critical review was extremely helpful in both validating the conclusions but also pointing out the gaps. At this roundtable, the participants also began to identify what organizations will needed to embrace and actualize in terms of preparedness to effectively deal with a digitalized foodservice world. There were the several gaps identified by the roundtable participants:

1 Organizational versus individual acceptance of the fact that a digital foodservice world is now a reality. It begins with an understanding of where the foodservice industry is going in terms of technology, data, analytics, the nature of relationships / connectedness, and organizational requirements. Until we accept our new reality, we will not be prepared for success in this new reality.

2 Willingness to make the investment required. Investments required on the front end to build an organization capable of undertaking a more analytical approach to the business which includes talent, systems, work process and a very different sales and marketing model.

3 Talent that is highly proficient and competence in a digital, technology-enhanced environment and relates to a more contemporary approach to establishing, developing and retaining vibrant, productive business relationships. This talent will not necessary look at the foodservice industry as its “first choice” so the industry will need to market itself to those new talents the industry needs to move forward.

4 The reliance on data, connections and networking, and operating in a **digital world means “standards” are a predicate.** Data standards will make the industry and connectedness far more productive, for without standards there are always added steps to “prepare” the data. The roundtable participants had another area where standards would improve productivity and creditability, and that was among research and data providers. There are wide variations by industry trackers as to their measurement techniques and the information they report-out / provide; there are variations in the location data, segmentations, and other facets of the data provided. The lack of clarity around “how and what” makes credibility and usefulness come under question. This is an industry-wide need and thus, a task the industry should undertake to bring standards to the world of data.

5 How to build an e-commerce based strategy is not a well understood body of work. Where to begin? How to be a fast follower rather than living on the “bleeding edge” of the transformation period in the foodservice industry?

This is a brave new world. The winners and losers in the new digitalized world will be those that have clear vision; a culture that accepts new ways to do business versus “that’s not how we do it” mentality; and, an informed strategy with the capabilities...talent, systems, work process...in place to succeed in the new world.

FOODSERVICE 2025: DEMOCRATIZED

Democratization of the marketplace at virtually every level will change the nature of the industry. A democratized market is one in which democratic systems and principles are in place and working; everything is accessible and available to everyone. The gatekeeper’s authority is greatly reduced and the power structure is “bottom-up” versus “top down.

DEMOCRATIZATION STARTS WITH THE CONSUMER

AGAIN, WE GO TO THE CONSUMER WHO IS A MAJOR CHANGE AGENT IN SHAPING *FOODSERVICE 2025*.

There is a new consumer in town, a new sheriff with new rules and expectation, and sheriff’s name is Millennial. The millennial as mentioned has technology and the internet as a connection to their world. The millennial engages with their food in a personal and scrutinized way. They want their food to be real, authentic, healthy, experiential, have an “origin story” and demonstrated “social impact”. Granted there are occasions when their choice is not based on health and wellness but based on indulgence; if it is an indulgence occasion, it must really deliver on that trait.

The implications of real, authentic and healthy include, but are not limited to:

- less likely to have a legacy brand as their preferred brand – not authentic or real;
- customized to fit their definition of good, healthy, experiential and these definitions are influenced by trusted friends or accepted advisories / experts...a new set of influencers is springing up and taking on the traditional role provided by paid advertising;
- want quality, taste, authenticity, transparency so they are assured what they are eating and drinking are good for their body – food with a story and a benefit;
- prefer local, natural, organic, lack of additives, fresh, food products with a “clean label”;
- prime drivers of the emergence and growth of specialty foods.

Growth of Specialty Foods (billions of dollars)

	2013	2014	2015	2016	2020 (p)	AACGR 2008 - 2016	AACGR 2016 - 2020
Retail	78.5	86.1	94.0	99.7	159.7	9.4 %	12.5 %
Foodservice	20.9	24.3	26.5	27.7	47.6	12.7 %	14.5 %
Total	99.4	110.7	120.5	127.4	207.3	10.1 %	12.9 %

Source: Mintel & Specialty Food Association & The Hale Group Estimates

The growth of the specialty foods in both the grocery and foodservice markets is propelled by the Millennials and affluent boomers according to Mintel research. The GenZs are expected to add further boost to growing this specialty market.

Major branded CPG food companies are and will be part of the specialty market as they make strategic acquisitions to buy into this growth area. For their legacy brands, they will move to

“clean labels” and remind the new consumer of the “story and heritage” of their brands.

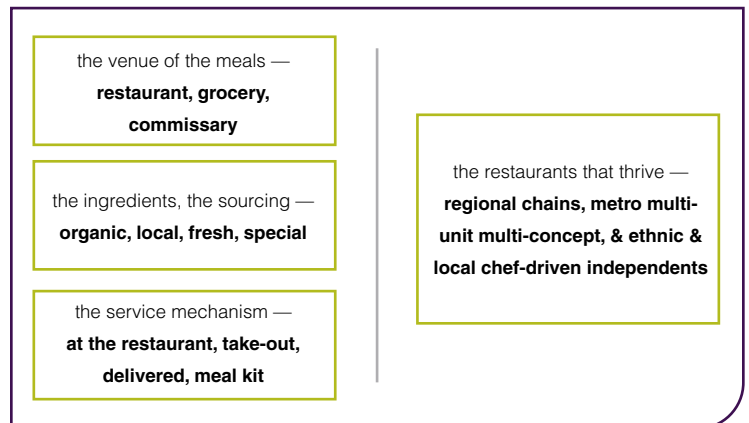
The consumer is increasingly conscious of the food they eat and the result is a move from “food” to “something special”; it has a culinary as well as healthy component.

The new consumer, the Millennials, are using their voting power to reshape the food and foodservice landscape. It is democracy activated in the food kingdom.

DEMOCRATIZATION IMPACTS THE OPERATOR LANDSCAPE

THE OPERATOR LANDSCAPE AND THE NATURE OF WINNERS AND LOSERS IS BEING MOLDED BY THE NEW CONSUMER. Their choices are based on the importance they place on real, authentic, experiential (ambience and culinary) and healthy. Now, add their use of technology and there is the blueprint for major change.

The new landscape already taking root is highly diverse in terms of the variety of concepts, routes to reach the consumer and mechanisms for the consumer to source their food, meals and snacks. For example:



The metro, local, regional multi-unit brands / concept operators speak to the wants of the new consumer while, for example, the large legacy casual restaurant chains in some ways are the antithesis of the wants of the new consumer thus, sorting of winners and losers.

Local and Multi-Independent Restaurant Operators such as:

WINNERS

- **Mainstreet Ventures** 21 locations, multi-brand concept (12), regional footprint, full service restaurants
- **Fox Restaurants** 15 concepts, 50 locations from pubs to fine dining

LOSERS

Non-descript, full service restaurant chains lacking highly-coveted, signature product, great service and attractive ambiance

- **Ruby Tuesdays** 540 locations, menu similar to competitive set

The characteristic sorting winners and losers in the 2025 landscape are:

Legacy, Casual Full Service

- Industrial approach to menu & preparation
- One brand, predictable & limited culinary
- Experience is neutral, not engaging
- Consistency the name of the game
- Experientially efficient, supported by fairly rigid supply chain

LOSERS

New, Casual Full Service

- Local & artisan approach to menu
- Multiple, distinctive local to regional brands
- Experience is key to establishing local - "your restaurant"
- Local, high quality, distinctive taste, great service - service & experience the product
- Flexible and adaptable operations and supply chain

WINNERS

This is not just about the casual full-service restaurant segment. These characteristics will affect all segments. While at first glance, it would seem as though these attributes are for moderate to upscale meals and snack; however, as we have

seen in the current market, the removal of antibiotics or food additives from the moderate and upscale chains is working its way across all price points and venues.

FOODSERVICE MANUFACTURERS WILL FOLLOW THE NEW CONSUMER

DEMOCRATIZED FOOD AND FOODSERVICE MARKETS ARE THE RESULT OF A CONSUMER, MORE SO THAN IN THE PAST, CLEAR ABOUT WHAT THEY WANT AND VOTING WITH THEIR SPEND. The new consumer has an expanded range of options readily accessed through technology. if not in the store or restaurant. New players will gladly accommodate and deliver what's wanted.

- So, the democratized marketplace means food manufacturers and foodservice operators will reshape their product portfolios to the demands of the new consumer.
- There is greater importance of having an effective metro/ independent multi-unit chain strategy in place. Able to reach and affect these operators with information, culinary assistance and services. Doing so in a cost-effective manner which likely leverages technology and local resources such as sales and marketing agencies or dedicated services in place.
- Recognizing the importance of culinary solutions versus just food product applications.

A democratized marketplace will mean the suppliers of food, beverage, meals and snacks will be far more consumer-centric than customer-centric. In a democratic world, it all starts with the voter and then moves to the provider and solution offered.

FOODSERVICE 2025: DISRUPTED

The foodservice industry and the supply-chain serving foodservice operators has been in place in a well-defined manner since early 1970s. The boundaries which defined the “foodservice industry” were clear; the roles of participants in the foodservice supply-chain were clear; the business practices and business model were established. In *Foodservice 2025*, supply-chains will be characterized as boundary-less, ubiquitous, and perhaps foodservice as an industry will be non-existent as a unique industry, channel and supply-chain.

In the *Foodservice 2025* world, technology, economic pressures and new business models will cause serious disruption to traditional roles, relationships, business practices and organizational design.

ELIMINATION OF CHANNELS; BIRTH OF OMNI-CHANNEL STRATEGIES

AS WAS SAID REGARDING DIGITALIZED AND DEMOCRATIZED, IT STARTS WITH THE CONSUMER. THE CONSUMER IS CHANNEL AGNOSTIC. THE FOOD INDUSTRY HAS BEEN THE CHANNEL CREATOR IN MANY WAYS. Channels arose to address the unique needs of each type of food retailer and operator; so, the major channels that developed were: grocery / supermarket, clubs, convenience stores, foodservice and industrial. Food manufacturers created a go-to-market organization to create demand and serve the demand for their products / services in each channel. The go-to-market channel organizations were created with the resources, knowledge and infrastructure required for success.

These channel organizations and strategies have worked well for manufacturers for the last 50 years or so. For many, this author included, this is the only go-to-market approach

witnessed. The consumer and the retailers / operators perpetuated this model by staying in their respective lanes or channels; however, “staying in your channel” is no longer the way forward. Consumers do not recognize channels so the retailers and operator are moving across multiple channels, thus giving the food industry a need for an Omni-Channel Strategy.

Consumers can now source their prepared, away-from-home meals and snacks from a wide range of retailers, operators or online vendors.

Range of meal / snack options have & will increase

- **Restaurants** - both free-standing and on-site
- **Grocerants** - meal solutions in grocery store & c-store venues
- **Delivered Meal Kits and Solutions** - Amazon Prime, Blue Apron, Plated, Hello Fresh, Uber Eats
- **Trucks, Food Halls, Pop-Ups, Events** - anytime, anywhere
- **Prepared Food and Frozen Meals / Components** - high quality, high flavor profile, premium packed meals

Retailers and online vendors who were not originally in the prepared, away-from-home meals and snack business are now pursuing these consumer occasions with speed and investment. The reasons are quite clear:

- it allows the retailer and online vendors to compete for business they did not have, in other words, an expanded market opportunity; and secondly,

- the prepared, away-from-home meals and snack business is significantly more profitable than selling packaged goods for these retailers.

A supermarket enjoys higher gross and operating margins on prepared, away-from-home meals and snacks than on packaged goods:

Supermarket Financial Model		
	Prepared Meal Solutions	Overall Store Financial Model
Sales	100%	100%
Cost of Goods	46%	66%
Gross Profit	54%	34%
Operating Expenses	43%	28.3%
Operating Margins	11%	6%

Source: The Hale Group Estimates

The economic advantage of prepared, away-from-home meals and snacks also applies to the experience of C-store operators. C-stores are migrating to prepared meals and snacks because these products generate more gross and operating profit. Economics will continue to drive this trend of ubiquity in foodservice.

For food manufacturers serving the foodservice industry, an issue that arises in this situation: how will they leverage their foodservice knowledge and products across an omni-channel foodservice marketplace? The existing manufacturer organizations with their traditional channel boundaries tend to resist cross-channel efforts. Territorial and financial motivations tend to impede internal cooperation and collaboration; yet, to be successful in an omni-channel foodservice marketplace collaboration, knowledge and resource sharing will be a strategic issue.

CHANGING ROLE OF THE FOODSERVICE DISTRIBUTOR

THE BROADLINE FOODSERVICE DISTRIBUTOR WILL CONTINUE TO BE A KEY MEMBER OF THE FOODSERVICE INDUSTRY IN 2025, BUT THEIR ROLE AND BUSINESS MODEL WILL MIGRATE TOWARD BEING A LOGISTICS \ DISTRIBUTION PARTNER VERSUS A “WHOLESALE”. The distributor may be among the most impacted by ecommerce and the consolidation of operator demand as described in The Hale Group’s *Foodservice 2020*.

The system distributors, specialty distributors, cash & carry wholesalers will be affected by the online vendors and ecommerce, but to a lesser extent than the broadliners.

The forces changing the role of broadline distributors include:

- Continued consolidation of the operator demand...fewer, bigger operators or surrogate buyers, i.e.GPOs, chains and multi-unit
- Changing needs of the distributor’s customer; from wholesaler to logistics role;
- Economic pressures: trade income shrinks; new pricing models kicks-in; lower cost e-commerce models compete;
- Transparency enabled by digitalization and networking;
- Manufacturers shifting focus from the distributor to large operators; and programs with operator and operator-purchasing surrogates.

In 2025, over 70% of operator purchases of goods and services will be governed by a contract between the operator purchasing entity and a manufacturer. This will reduce the role of the distributor in the product purchase decision and that is major change in the distributor’s role.

Foodservice Broadline Distributors

Old Role 2010	New Role 2025
<ul style="list-style-type: none"> ❑ Determine Product Portfolio Offered ❑ Pricing Controlled by Distributor ❑ Primary Influence on Operator Purchases (other than chain business) ❑ Controlled Access to Operators ❑ Controlled Access to Operator Purchases information 	<ul style="list-style-type: none"> ❑ Over 70% of business manufacturer negotiated product & pricing at HQ <ul style="list-style-type: none"> • executed through designated distrib. ❑ Manufacturer receives purchase information direct from operator <ul style="list-style-type: none"> • has visibility to purchase / use data ❑ Distributor is a logistics partner for 70% of their business <ul style="list-style-type: none"> • execution of operator / manuf. prog.

The changing role also effects the degree of leverage the distributor can exert in the purchasing function.

As the operator purchasing decision moves to a negotiated contract between operator purchasing entity and the manufacturer, the foodservice chains have changed how they compensate the distributor for their role and efforts. As the distributor becomes a logistics partner instead of a wholesaler, the chains have gone to a logistics fee-for-service model; so, the distributor revenue model is now a fee-per-case model versus a mark-up model.

Foodservice Distribution Revenue Model

2010 Revenue Model	2025 Revenue Model
<ul style="list-style-type: none"> ❑ Multiple Revenue Streams ❑ Pricing Based on a Mark-Up <ul style="list-style-type: none"> ▪ DSR Established ▪ Cost-Plus ❑ Rebates and Growth Programs a Major Source of Profitability 	<ul style="list-style-type: none"> ❑ Limited Revenue Streams ❑ Pricing on a Cost-to-Serve ❑ Revenues based on "Fee per Case" <ul style="list-style-type: none"> ▪ Contract Based ❑ Started with Chains, but Now Well Beyond Chains ❑ Rebates/Growth Programs Limited

There are other implications of the changing distributor revenue model. One implication is the organizational capabilities / proficiencies that lead to success, i.e., a sustainable financial return.

Foodservice Distribution Revenue Model... Organizational Components Success Model

2010 Revenue Model	2025 Revenue Model
<p style="text-align: center; font-size: small;">Skills & Competencies Important to Win Historically</p> <ul style="list-style-type: none"> ❑ Purchasing Capabilities ❑ Street Salesforce ❑ Merchandising 	<p style="text-align: center; font-size: small;">Skills & Competencies Important to Win in the Future</p> <ul style="list-style-type: none"> ❑ Logistics Management ❑ Contract Negotiation ❑ Operations Excellence ❑ Analytical Skills ❑ Strategic Relationship Management

Along with new competencies, a second implication of the changing revenue model is the importance of "through-put", so productivity becomes a critical measure of success. If the fee is based on moving cases, then being able to move cases and lots of cases in a highly efficient manner becomes top-of-mind for distributors. Thus, turns, elimination of "dead inventory", vendors that make distributor operations more productive are all factors in achieving highly efficient through-put.

A third implication deals with the loss of the "trade promotional monies" traditionally provided to the broadline distributor by manufacturers to gain a favorable position for their products. As more of the distributor's business is logistically based, the trade monies go away; in most instances, the trade monies are restricted by the contractual relationship between operator purchasing entity and the manufacturer.

To replace the trade monies, broadline distributors will increase their exclusive brand business. These will be products and brands developed and owned by the distributor. They will be supported in the same fashion as a foodservice manufacturer supports their brands. This is not private label; these exclusive distributor brands will have unique attributes and benefits.

GROWTH OF ECOMMERCE IN THE FOODSERVICE DISTRIBUTION SPACE

IF BROADLINE DISTRIBUTORS WERE NOT ALREADY UNDER PRESSURE TO CHANGE THEIR BUSINESS MODEL, ECOMMERCE IS ON THE SCENE AND EXPECTED TO PLAY A FAR BIGGER ROLE IN FOODSERVICE DISTRIBUTION IN 2025. As mentioned earlier in this paper, the digitalization and technology of the foodservice marketplace is the default preference of the consumer and operators.

A major research project undertaken by Cleveland Research found that approximately 50% of operators are already using ecommerce to purchase some of their products and went on to find 70% of operators expect to use ecommerce purchasing solutions by 2025. Amazon was among the ecommerce sites already being used by 13% of the operators.

This research included survey results from manufacturers, distributors and operators. One of Cleveland’s research conclusions was distributors and manufacturers are well behind the operator in the acceptance of ecommerce. If manufacturers and distributors do not prepare themselves for this shift, they will be left behind.

A picture of the foodservice distribution industry is shown below. Ecommerce challenges both broadline distributors and cash & carry. Of course, both broadline distributors and cash & carry could evolve into ecommerce distribution solutions.

Share of Operator Purchases of Expendables %

	2010	2015	2020	2025
• Broadline Dist.	58%	59%	55%	51%
• Top 10	48	51	50	46
• System Dist.	11	11	12	12
• Specialty Dist.	19	17	15	13
• Cash & Carry / Clubs	11	13	12	10
• E-Commerce	nil	nil	6	15
TOTAL	100%	100%	100%	100%

new source of goods for operator

The foodservice broadline distributor will undergo change as technology and the redefinition of relationships reshapes the foodservice landscape. However, the foodservice distributor is not going away because they play a very important role in making foodservice work.

FOODSERVICE 2025 ROUNDTABLE DEFINES THE FUTURE ROLE OF THE DISTRIBUTOR

AT THE *FOODSERVICE 2025* ROUNDTABLE EVENT, THE PARTICIPANTS CLEARLY RECOGNIZED THE IMPORTANCE OF THE DISTRIBUTOR, but they also saw a distributor of the future as a logistics provider versus the wholesaler role... a role they’ve played historically.

The roundtable team addressing this issue provided their view of the distributor:

SUMMARY OF THE TEAM’S VIEW OF THE ROLE OF THE DISTRIBUTOR 2025

Function the Distributor Performs	Relative Importance in 2025 v. 2017
Getting the goods to the operator across the “final mile”	This is and will be their primary role
Bundling a wide range of goods for a “one-stop” delivery	This is a major benefit of the distributor versus individual products delivery
Assuring traceability for all goods their stock and sell	This will remain an important role for distributors
The ability to provide committed volume to the manufacturer for supply-chain efficiencies	There is an opportunity for a better forecasting; this can be a real benefit in managing the supply-chain
Provide the operator with financial support	This will remain an important role the distributor plays

SUMMARY OF THE TEAM'S VIEW OF THE ROLE OF THE DISTRIBUTOR 2025 CONTINUED...

Function the Distributor Performs	Relative Importance in 2025 v. 2017
Control of and access to operator data	This will be an important data source, but increasingly it will come from data providers or from the operator or operator groups
"Consultative Selling" and providing key information / knowledge to the operator	While proving information to the operator to improve their business, it is unclear whether the distributor will play this role in the future. It may be the broker and \ or manufacturer using technology
Creating and owning the order guide	This will less of a role for the distributor as the operator or their procurement entities control and dictate the order guide content

FUTURE ROLE OF AMAZON OR AMAZON-LIKE PLAYERS IN FOODSERVICE

WITH ECOMMERCE KNOCKING ON THE DOOR OF THE FOODSERVICE INDUSTRY, THE NEXT QUESTION IS WHETHER AMAZON WILL BE A FULLY ACTIVE SUPPLIER TO THE FOODSERVICE OPERATOR COMMUNITY. There is an increased interest in Amazon's intentions as they recently acquired Whole Foods.

Amazon has and will have strong working relationships with food and foodservice manufacturers so the jump from consumer focus fulfillment to operator demand fulfillment may be a logical next step supported by Amazon's current set of food manufacturer partners.

However, the questions are:

- Given operator's current expectations, will the margins realized be sufficient to sustain Amazon's interest? Current "street business" gross profit margins are 16 to 20% and mid-size chain business at 12 to 15%?
- Amazon 10-K shows current fulfillment expense is 13% of sales and marketing, technology, G&A accounting for another 19% of sales.
- Since the "final mile" and the "bundling of multi-products orders" are a major benefit of existing foodservice distributors, how will Amazon accomplish those roles? Through their existing distributor centers or by acquiring a fulfillment company such as Sysco or US Foods?

It is not clear at this point whether Amazon will be a major factor in the *Foodservice 2025* landscape, though it is hard to think they will not be. What is clear is there will be operating ecommerce models, similar to that successfully developed and commercialized by Amazon, and they will be a major factor in reshaping foodservice distribution.

FINAL THOUGHTS ON DISRUPTION IN THE FOODSERVICE MARKETPLACE

THE NEW CONSUMER, TECHNOLOGY, ECONOMICS AND THE BREAKDOWN OF THE FOODSERVICE CHANNEL BOUNDARIES ARE ALL FACTORS CREATING DISRUPTION AND MOLDING THE NEW MARKETPLACE.

The participants at the *Foodservice 2025* roundtable did not debate the fact the industry is ripe for disruption. The advice included:

- 1 Get your organization prepared for the changes that have already occurred and those that are coming;
- 2 Work to get organizational preparedness in place, be an agile and quick-follower rather than being part of the “bleeding edge”. Much of what will be coming at foodservice organizations is new news; so, observe, test, understand, make mid-course corrections and act boldly.
- 3 Figure out who are the best strategic allies to navigate through the changing digital and disruptive state of the business; and then, form working relationships with those allies.

IN HIS SONG “THE TIMES THEY ARE A-CHANGING”, BOB DYLAN SAYS “THE TIMES THEY ARE A-CHANGING...FOR HE THAT GETS HURT WILL BE HE WHO HAS STALLED”.

Preparedness for change will be a critical success factor for those that prosper in 2025.

FOODSERVICE 2025: STRATEGIC IMPERATIVES

The operating environment your organization must be prepared to deal with is already firmly rooted in the existing marketplace. For preparedness, The Hale Group has identified six areas of focus or strategic imperatives.

- 1 **ECOMMERCE STRATEGY: A CLEAR UNDERSTANDING OF WHAT AN ECOMMERCE OPERATING ENVIRONMENT WILL LOOK LIKE AND HOW IT OPERATES; AND HOW YOUR ORGANIZATION WANTS TO BE POSITIONED IN THE SPHERE OF BUSINESS FOR SUCCESS.**

Preparedness starts with informing and educating your

organization’s leadership, so they understand what will it takes to be successful in an ecommerce world. Then creating a strategic plan / pathway so the organization is fully prepared to successfully participate in ecommerce.

2 ORGANIZATIONAL DESIGN: A LEAN GO-TO-MARKET ORGANIZATION EQUIPPED WITH THE NEW TALENT REQUIREMENTS OF A DIGITAL AND CONNECTED FOODSERVICE MARKETPLACE.

Preparedness starts with having the right talent with the right attitude in place able to address the new marketplace. Getting ahead of the advent of foodservice ecommerce, the *Foodservice 2025* roundtable team identified what they believe is required for success.

FOODSERVICE 2025: CHARACTERISTICS OF A SUCCESSFUL FOODSERVICE ORGANIZATION

	Structure	Competencies	Culture
Digital	<ul style="list-style-type: none"> Ecommerce organization for strategic customers and top partners Dedicated data management 	<ul style="list-style-type: none"> 360 view / data / drivers on demand GS1 Understand the complexity; simplified the message 	<ul style="list-style-type: none"> “on-demand” nimbleness Knowledge transfer for all Career pathing / mentoring
Democratized	<ul style="list-style-type: none"> Subject matter expertise availability Channel expert availability Expertise imbedded in the organization that goes beyond the operator to the consumer 	<ul style="list-style-type: none"> Insights that are consumer-centric X-functional understanding of operator / retailer’s needs Solid project management skills End-to-end thinking 	<ul style="list-style-type: none"> A business management culture versus a sales culture
Disrupted	<ul style="list-style-type: none"> Eliminated a “siloeed” structure A “heavy” IT presences “Role-sorted” so we have clarity Innovation / R&D / Culinary presence Integrated supply-chain team 	<ul style="list-style-type: none"> “GM” mentality Strong analytical skills A cross-functional team approach Financial core for understanding of both working capital needs and actual costs involved. 	<ul style="list-style-type: none"> Agility in a matrixed and complex world Generational adaptive Talent development Investment in horizontal org. development

3 ORGANIZATIONAL CULTURE: HAVING A DATA-DRIVEN CULTURE THAT MEASURES, SCRUBS FOR OPPORTUNITIES AND SOLUTIONS AND TAKES ACTIONS BASED ON THE DATA AND INSIGHTS.

Research demonstrates data is a more reliable and better source of insights and answers than opinions and experience from a different time. Measurement is also very helpful in understanding what works and what is not working. Measurement is empowering to understand where there is underspend or overspend.

4 OPERATING PHILOSOPHY: UNDERSTANDING THE BUSINESS IS NOW A SOLUTION AND PROGRAM-FOCUSED BUSINESS STARTING WITH THE CONSUMER AND TAILORED FOR THE SPECIFIC SEGMENTS AND / OR ACCOUNTS SERVING THAT CONSUMER OCCASION.

“Solutions” have three components: **a product** (the tangible element of a solution); **a service** (which could be training, a promotion, analytics or some other service) and **information** (consumer trends and insights, segment trends, business update, recipes, etc.). It starts with the consumer, but does not end there. Successful organizations must be prepared to provide the answer to the consumer’s need state.

5 GROWTH SEGMENT: HAVING AN ACTIONABLE “INDEPENDENT MULTI-UNIT RESTAURANT STRATEGY”

As traditional full-service restaurants stagnate, they are replaced by local / metro / regional multi-unit restaurant operators. These operators are growing. They gravitate toward specialty and locally-sourced products. They also have greater interest in culinary input in their menu items.

The multi-units have been more difficult to reach and influence than high-visibility national or large regional chains. So, organizations will need to develop strategies that reach and influence these growth actors. Streaming videos, mobile restaurant-focused TV such as *Foodables*, use of social media are all parts of an independent multi-unit strategy. The other part is a well-designed and structured approach to deliver the “solutions and programs” by market-level teams, such as multi-unit focused broker teams.

6 OPEN MARKETPLACE: HAVE AN EFFECTIVE OMNI-CHANNEL APPROACH TO MEAL AND SNACK SOLUTIONS WHICH MARSHALS THE FULL KNOWLEDGE, EXPERTISE AND CAPABILITIES OF THE ENTERPRISE ACROSS THE ENTIRE FOOD MARKETPLACE VERSUS A SOLOED APPROACH.

Since the new consumer does not see nor acknowledge channel boundaries, the manufacturer’s omni-channel strategy should remove their barriers to deploying foodservice resources.

7 OPERATING EFFICIENCIES: HAVE AN ONGOING FOCUS ON REMOVAL OF UNPRODUCTIVE COSTS AND ADOPT TECHNOLOGY AND WORK PROCESS DESIGN TO IMPROVE EFFICIENCIES AND PRODUCTIVE OF ALL RESOURCES / ASSETS.

Foodservice 2025 will not present an opportunity in most cases to improve margins. The margin pressure is a reality and just a condition. The remedies for this condition are a constant, focused and funded effort to remove unproductive costs / spends and find new ways to deliver value. Technology and innovation will contribute to efficiencies. The “3G” effect will not be going away.

FOOD SERVICE 2025

FOODSERVICE 2025: CLOSING THOUGHTS

THIS WHITE PAPER ENDS THE
WAY IT BEGAN.

The need for foodservice organizations to look to the future and anticipate how their world will change is a continued requirement of sustainable success. In many ways, the future operating environment already exists in an embryonic fashion, not fully developed but ready to break out and disrupt existing business models, practices and requirements. *Foodservice 2025* is intended to assist leaders in foodservice organizations to begin their own debate on the future; form their view of the world that is coming; and, begin confidently taking steps to be prepared to succeed.

Foodservice 2025 is only the starting point. The finish line is a well, thought-out and vetted strategic plan and pathway to be winning in the new operating environment which is digitalized, democratized and disrupted.

Foodservice 2025 outcomes are rooted in today's operating environment, so the time to be prepared for 2025 is today. The starting point is preparedness.