



*Meeting the Challenge of Exporting to the U.S.: Trade Practices that Benefit Growers
and Exporters.*

Francisco Arellano¹ and Lourdes Martinez²

Background

Over the last 15 years, the fresh produce distribution system has been one of the most dynamic marketing channels in the U.S. (McLaughlin et al., 1999). Major changes such as retail consolidation, technological change in production and marketing, and growing consumer demand for quality have altered the traditional role of produce suppliers, showing an increase in demand for additional marketing services, as well as increasing demand for volume (Dimitry et al. 2003).

Different trade practices and structure of transactions have characterized the relationship between retailers and produce suppliers. Trade practices include different payments of fees such as volume discounts and slotting fees, as well as services like automatic inventory replenishment, special packaging, and requirements for third-party food safety certification. In term of structure of transaction, there are more long-term relationships or contracts versus daily sales with no continuing commitment (Calvin et al, 2001). Although there is a large number of trade practices and transactions between retailers and wholesalers, this trade practices have not been the same between producers and wholesalers.

Trade practices for wholesalers and producers have been mainly based on verbal agreements and trust between parties. This strategy has worked for agents who have kept a business relationship for a long time. However, for agents who are doing a transaction for the first time there is a significant level of uncertainty about the trustworthiness of the potential partner. Thus, selection of the “right” partner is important for agents to assure product sales.

In some cases, the only information that a supplier has is based on supplier’s “reputation” in the industry. Measure of an agent’s good “reputation” is hard to obtain

¹ PFID Consultant, M.S. Agricultural Economics,

² Research Specialist, Michigan State University. Corresponding author marti617@msu.edu

We would like to thank Robert Summers for his insights about the wholesale distribution system in the U.S.

given that this information is not readily available, and when it is available this information may be incomplete. Finding information about reputation of potential buyers is harder when agents are in different countries because distance carries additional costs to enforce the verbal agreements. Hence, for agents interested in marketing fresh produce in the U.S. it is important to understand the produce distribution system and the role of food distributors before engaging in business that can be costly.

This report is intended to give fresh produce suppliers a guide on developing successful relationships with U.S. wholesalers and distributors of fresh produce. Information was gathered thru interviews with wholesalers and intermediaries in the Miami and Los Angeles Fresh Produce Markets, as well as companies engaged in trading, distributing and marketing fresh produce. In Los Angeles, interviewed companies were Melissa's, Cooseman LA, Davalan Sales, Mission Produce, and Gills Onions. In Miami, interviews included representatives from Southern Specialties, Central American Produce, Cooseman Miami, Caribbean Connection and Tropical Commodities.

The objective of this study is to help minimize market risk for suppliers by improving their knowledge of the market structure, and helping solidify relationships with wholesalers. The report also aims to proportionate information regarding current trends and the trade practices in the produce distribution system in U.S.

Produce distribution in the U.S.

Calvin defined food distributors as “agents that negotiate transactions between buyers and sellers without taking title to the merchandise or physically handling the product. There are also buying distributors that purchase on account for clients and do take title” (Calvin and Cook, 2001). For the purpose of this paper, a food distributor will be also defined as a ‘wholesaler’ who is the first agent a farmer faces in the U.S. with the main function of gathering production to later subdivide and distribute it downstream the supply chain.

One of the major changes in the distribution system in the U.S has been an increasing concentration and competition among retailers which has caused concentration and fierce competition among wholesalers as well. Consequently, this situation has redefined wholesaler functions in the market. Wholesalers of fresh produce no longer

deliver the product offered by the grower/exporter, but today they must offer what retailers demand. However, in the case of some fresh products, retailers and wholesalers need to work together to deliver high valued products to end-customers.

A closer relationship between retailers and wholesalers is based on the fact that: (a) individually, retailers do not have a demand of high volumes of non-traditional products (e.g. passion fruit, plantains, etc.), and (b) farmers do not have the capacity to grow high volumes of products to commercialize them directly to a retailer/wholesaler chain. Due to this characteristic, wholesalers play a key role in the supply chain delivering products.

In the case of imported fresh produce, trade relies heavily on the participation of wholesalers. Thus, understanding the way wholesalers operate in the supply chain is fundamental for growers outside the U.S. who have little or no knowledge regarding food distributors in the US.

Trade relationships between suppliers and wholesaler

Price is a very important issue in the relationship between brokers and their suppliers. Generally, brokers do not guarantee a yearly price and the nature of their business is to work on margins. However, they would engage in certain trade relationships in order to control risk and price fluctuations.

The most common practice among wholesalers and suppliers of fresh produce remains the acquisition of products under consignment. Working on consignment allows the distributor to take advantage of price fluctuations for produce with high seasonal demand while diminishing their risk of quality deterioration for produce with low seasonal demand. The nature of business based on consignments is to make profits through marketing margins, and wholesalers are able to protect themselves against adverse price fluctuation and quality deterioration risks. However, this situation makes the supplier bears most of the price and quality risks, and does not incentive suppliers to deliver product according to quality requirements.

Some wholesalers interested in reducing risks build long-term business relationships with their supplier. This relationship is characterized by a tight coordination in the supply chain (e.g., logistics, cold, packaging, paper work, etc.) to minimize errors along the supply chain and establish responsibilities. Generally, these long-term business

relationships between wholesalers and their suppliers are based on “trust”. All transactions are based on verbal agreements where each party states what they agree to comply with and the benefits; hence, it requires long term business.

More sophisticated relationships are based on strategic alliances with suppliers, which imply a contract agreement. Alliances (i.e., equity-based alliance, relation based alliance or contracts) allow brokers to strengthen their competitive advantage delivering fresh produce.

Wholesaler Trade Practices

Trade practices commonly used by wholesalers include the use of internet and digital photos mainly to control for appearance of products. Some wholesalers have developed written quality standards, but on-site inspection of products is still necessary. Some of the requirements include measuring temperature, color, sweetness, ripeness, pressure of the products, and container’s records of temperature. Other requirements are specification about size, color, varieties, packaging, labeling. For many wholesalers, the emphasis is on the produce presentation; however, increasingly there are more requirements of third party certifications and of traceability systems

In general, during transactions there is a clear specification of responsibilities, which include costs of handling, freight, drayage, inspections, customs, duties, carting, fumigation, customs, retroactive customs assessments, handling fees, sales charges, boxing, packaging, stickers, cratering, repackaging, palleting, re-palleting, cooling costs, legal prosecution expenses, and other costs. Among parties there is a well defined specification of term of payments, which is generally less than 30 days, but can go up to 60 days.

Wholesalers engaged in long-term commitment with suppliers would invest in warehouses and cold rooms on production areas. They would also implement practices such as open books policy which implies both parties to know production costs and selling price. Sometimes wholesalers are willing to assume losses or reduce their margins in order to motivate suppliers to keep a constant flow of produce. In general, wholesalers would have a transparent communication with suppliers about market conditions and both parties would manage all trade information together.

New market structure has affected the traditional role of wholesalers. Nowadays, some wholesalers engage in practices that were not common before. Current practices include:

Brand development: In order to attract the final consumer through brand recognition, some wholesalers have developed their own brand names. Although wholesalers don't necessarily take title of the product they do need to assure a constant quality of the branded crop. Hence, wholesalers have some control over quality attributes and constant volumes of the product thru investments in farming, packing process, and establishment of contracts or production programs with their suppliers. Examples of this kind of agreements are Southern Specialties, Central American Produce, Melissa's and Coosemanas LA.

Alliances with suppliers. When the market is not mature, such the case of some exotic produce, wholesalers may be interested in establishing some kind of alliance, which may or may not necessarily be equity-based alliance, but rather a more relation-based alliance, but still implies the signing of a contract. Doing so, wholesalers control a constant supply of quality desired and take advantage of price fluctuations. Examples of these practices are observed between Caribbean Connection and Mission Produce. Caribbean Connection shares with Mission Produce direct costs of farming and marketing, and Mission Produce works with its growers on consignment.

Financing costs. Some wholesalers make cash advances to suppliers, and specifically to producers in order to cultivate and ship specific products. For example, Southern Specialty makes cash advances to pay labor and boxes, Coosemans financed the production of baby vegetables, and Caribbean Connection finances the production of certain roots and vegetables.

Advantage of new market structures on trade relationships

Although traditional ways of conducting business are still predominant in trade relationships between wholesalers and their supplier, rapid changes in the fresh produce industry imply readjustment of business practices among all participants of the supply change. Some of these changes are increasingly driving suppliers out of business, while others represent advantages to increase sales or enter new markets. Requirements such as

quality differentiation, specific variety of products and satisfaction of retailers are just some examples of opportunities that can be addressed by suppliers to enter this competitive market.

Quality differentiation. When a wholesaler is relying on quality differentiation, it is important for his business to assure that he is the only one with that specific product and also that the product with the specific quality requirement is not delivered to competitors. The strategies in this case are to have control over the farming or packaging operations through investments or to require exclusivity from suppliers through contracts. Examples of these are Southern Specialties with a new asparagus variety, Caribbean Connection with the unique variety of okra, Melissa's with the dragon fruit.

Specific variety. If a wholesaler needs a specific product variety, he/she would proportionate seeds to producers or agree to buy the entire production. Wholesalers manage that producers cannot sell production and control product specifications by signing contracts with suppliers. Example of this practice can be seen between Melissa's and Gills Onions

Filling retailer's order. Retailers like Walmart require a 98.5 percent order filling to continue the deal with wholesalers, which means that wholesalers can fail to supply all the required products only in 1.5 percent of the cases, which increases the necessity of wholesalers to assure a constant supply of fresh produce. In order to satisfy their customers, wholesalers are willing to create programs with their suppliers to manage quantities and delivery dates. Some of these practices require wholesalers to take title of the product, brand development and exclusivity over a variety. Wholesalers take title of products either through contracts, joint ventures, or relation-based alliances. In these situations, the risk of volume fluctuation and quality deterioration are shared between wholesalers and suppliers.

Conclusion

Changes in fresh produce demand are imposing new directions in the way wholesalers establish relationship with producers. Several factors are important for wholesalers to maintain their share in the market, and these factors can represent advantages for their suppliers. Some of these factors are:

a) Rapid changes in consumer demand and consolidation of retailers. Wholesalers are forced to act according to their customers demand; hence, verbal agreements and emphasis on the “reputation” of agents poses high risks of mistakes in delivery of products and does not guarantee of long-term success of a deal with customers.

a) Reassurance of quality products to retailers at a competitive cost. Finding alternative sources for specific crops, with the quality attributes, such as specific color and size represents extra costs for wholesalers. Also, seasonality, market maturity of the specific crop, need of frequent shipments, and different procurement strategies encourage wholesalers to establish more long term relationships with their suppliers.

Current practices and structure of transactions in the produce industry emphasize more commitment from wholesalers and producers. Although these practices represent challenges for small and medium size growers and exporters, they also represent an opportunity to work closely with wholesalers, diminishing price and quality risks and increasing the possibilities of long-term profitability.

Reference:

Calvin, L., R. Cook, M. Denbaly, C. Dimitri, L. Glaser, C. Handy, M. Jekanowski, P. Kaufman, B. Krissoff, G. Thompson, and S.Thorns bury. 2003. *Fresh Fruit and Vegetable Marketing: Emerging Trade Practices, Trends, and Issues*. Washington DC: U.S. Department of Agriculture, EDERS Agr. Econ. Rep. 795

Dimitri, Carolyn, A.Tegene and P. R. Kaufman. 2003. *U.S. Fresh Produce Markets Marketing Channels, Trade Practices, and Retail Pricing Behavior*. Washington DC: U.S. Department of Agriculture, EDERS Agr. Econ. Rep 825.

McLaughlin, E.W., G.M. Green and K. Park. 1999. *Changing Distribution Patterns in the U.S. Fresh Produce Industry: Mid/Late-70s to Mid/Late-90s*. Department of Agricultural, Resource, and Managerial Economics. College of Agriculture and Life Sciences. Cornell University, Ithaca, NY 14853.