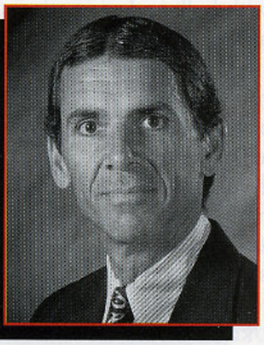
Breaking The Barriers

By Edward McLaughlin

Since the dawn of the contemporary food industry, the trade has separated itself into two competitive but not always parallel tracks: retail grocery food and restaurant or foodservice food. For most of their history, both industries have snubbed any suggestion of horizontal integration. Other than the occasional in-store eatery, grocery operators have generally dismissed restaurant activities, and, similarly, virtually no foodservice operators have made any serious attempt to open retail shops. Today, such separation appears myopic.

Over the years, business consultants reinforced this polarity by advocating that the key to corporate success was "sticking to your knitting." Academics were as guilty. Cornell University saw fit to keep its justly world-famous Hotel and Restaurant School separate from the retail-oriented Food Industry Management Program, located across the campus. Never once was a course or lecture even offered concurrently.

Ironically, both of these food delivery institutions have had the same basic missions: to satisfy consumer food needs in a healthy, safe and tasty manner at a fair price. But, as history shows, the methods by which they chose to execute this mission have differed dramatically. What's more, despite much new posturing, the vast majority of firms in these two food delivery channels still follow nearly opposite strategies. This can be explained, in large part, by the structure of today's incentives.



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The long-term success of the grocery store must be attributed to its high volumes. The retail grocery institution has endured by offering relatively low-cost goods to mass markets. Indeed, analysts who cite the low percentage of disposable income that Americans spend on food — the lowest in the industrialized world — as an indicator of the enviable efficiency of the American retail food distribution system are fundamentally right!

Restaurants have followed a different tack. Their outlets are not constructed to maximize distribution efficiency and traffic flow. Whereas an average supermarket may find cause for alarm when it only conducts 8,000 customer transactions on a given Saturday, the cozy restaurant down the road may be ecstatic because it served as many as 85 dinners on the same night. The latter can survive, indeed thrive, on low meal volumes because it appeals only to particular segments.

Today's supermarket carries more than 20,000 different products (SKUs). Many superstores with pharmacies carry more than 60,000. Retailers have been encouraged to offer "one-stop shopping" to solve all shopping needs.

Restaurants have elected to solve the consumer's variety needs differently. They make no presumption to offer all choices. Rather, most allow consumers to make the variety choice before they walk in. The initial restaurant selection decision establishes the boundaries of the meal order. Menu choice is limited.

Of course, to achieve their volume requisites, supermarkets maintain low relative prices. There are few supermarkets that do not purport to be the "lowest priced" store. Further, supermarkets have a strong tradition of using deep discounts as their primary promotion strategy. They trumpet "free coffee" and "29¢ sliced ham" on the front page of their weekly flyers and in their windows. They create their own worst enemy: the price-oriented shopper.

As industry walls come tumbling down, new incentives are required for managers to build store-wide competencies.

Restaurants have had a different plan. Instead of creating an image of "the lowest priced meal in town," most of the industry has emphasized quality. Even low-priced segments tend to focus on fun and convenience more than on low price. As a result, the same consumer adopts a different mentality in a restaurant than in a supermarket: in the former, decisions are usually based on taste, ambiance and quality, while in the latter, decisions are based on price.

Although these contrasting strategies have succeeded admirably, the rigid historical industry boundaries excluded a large share of business from the other's channel. Reward systems were structured to reinforce industry walls. In addition, department managers within the same firm competed with one another for scarce resources.

Now, of course, there are very few restaurant or supermarket chains in the U.S. not attempting to capitalize on the exciting opportunities for fresh prepared foods and home meal replacement programs. However, as industry walls come tumbling down, incentives encourage separation. Suppliers have oriented their sales forces to be either "retail" or "foodservice." Most restaurants have limited ability to respond to volume orders. Retail deli managers are frequently prevented from using their foodservice suppliers for certain products. Often, for example, fresh produce items must be procured from their own produce departments, sometimes at full retail price, even when these items may not be optimal.

Such practices reflect "old school" thinking. Many companies today report that "turf" problems prevent them from advancing more aggressively into genuinely innovative meal solutions. To move forward, managers require cross functional training and need to be rewarded for building new storewide competencies and for their contributions to companywide success.

Consumers think in terms of meals. Most food industry mangers still think in terms of channel and departmental boundaries. To respond to the challenges of contemporary consumers, companies need to emerge from industry and departmental myopia and put new incentive systems into place that encourage experimentation and cross-border cooperation within stores. DB