

Fast Facts on Food Processing

Grant Thornton Food & Beverage Practice Part 1 of 6

Supply Chain Pressures

It's been a challenging year for food and beverage manufacturers. The most obvious source of discomfort is an ailing economy, which has pinched consumer demand. But supply chain issues — including ingredient availability and vendor pricing — also are squeezing margins.

Grant Thornton LLP, the audit, tax and business advisory firm, is collaborating with *Food Processing* magazine on a series of six bimonthly surveys — *Fast Facts on Food Processing* — to provide a pulse check on business performance challenges and opportunities in the food industry. The first survey — *Supply chain pressures* — examines the vendor issues impacting food and beverage manufacturers today. This review of the responses from 157 companies received in June and July (see participant profile at the end of this report) offers insights to help your firm overcome margin pressures and remain competitive.

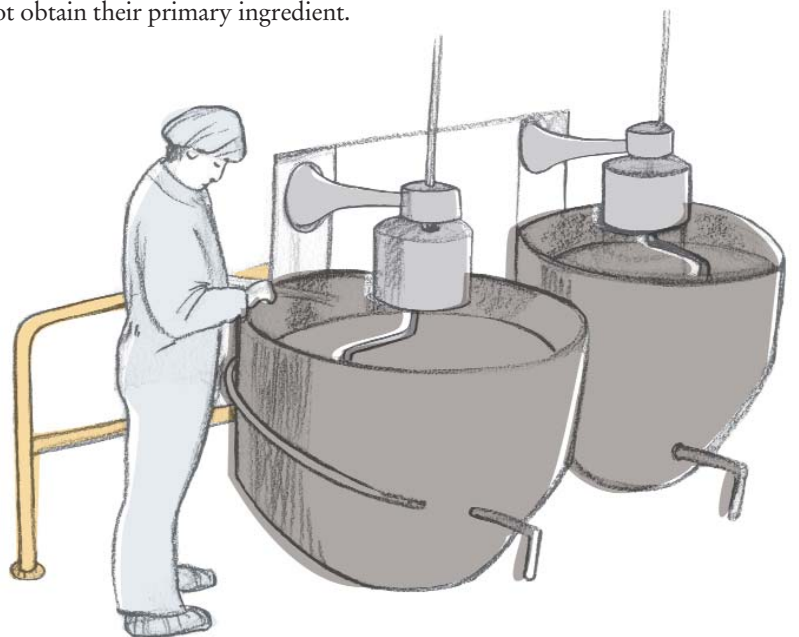
Availability

Few factors are as important to food and beverage manufacturers' success as the ability to obtain materials/ingredients from suppliers when needed. Food and beverage manufacturers report that the typical availability of their primary supplier materials/ingredients is either "readily obtainable" (44%) or "somewhat obtainable" (49%). Six percent of respondents indicate that their materials/ingredients are difficult to obtain, and one company indicates that they could not obtain their primary ingredient.

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Unavailability of ingredients is rare but potentially devastating. For example, in the past year many breweries found themselves unable to attain hops specific to their brands. And for brief periods, various ingredients have been unobtainable due to natural or manmade disasters. One executive comments, “Several spot shortages of raw materials caused us problems because our volume demand was higher than the original forecast on seasonal raw materials.” Others note that the unreliability of materials causes them to carry more inventory: “We must buy in advance because products are not readily available.”

Not surprisingly, large food and beverage manufacturers have more clout in getting the ingredients they need: More than half of food and beverage manufacturers with annual revenues exceeding \$100 million (54%) report that their primary ingredient is readily obtainable and 46% report somewhat obtainable; only 39% of smaller firms (revenues of \$100 million or less) report their primary ingredient is readily obtainable.

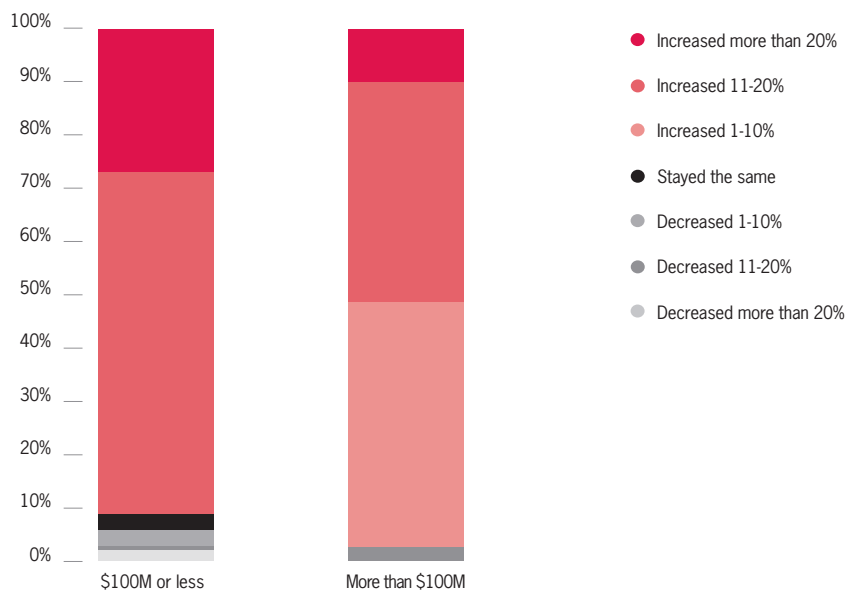
“Complete unreliability for the small manufacturer,” says one executive about vendor dependability. “[Suppliers] will get ingredients ordered to you ‘whenever’ and ‘maybe’ or promise them over and over, but the ingredient never shows. And good luck if it shows up and is to spec.”

The same small manufacturing firm executive continues, “Special orders are shunned, even if you’re willing to pay a premium. And orders of less than 11,000 pounds are treated with what verges on contempt, which translates to a complete unwillingness on the part of ingredient suppliers to help a small concern grow into a giant one — very shortsighted of them!”

Food sectors where ingredients were least likely to be readily available were dairy products (27% of dairy product manufacturers report readily available); meat, poultry and seafood (35%); and snacks (37%). The sector where ingredients were most likely to be available is confectionery products (55%).

Price change for primary materials/ingredients

% of participants by annual revenues



Pricing

While materials/ingredients are generally available, food and beverage manufacturers are finding them at dramatically higher prices, in some instances at costs that put margins in jeopardy. Nearly all participants (94%) report that the price they paid for materials/ingredients in the past year increased: 31% report increases of 1-10%; 39% report increases of 11-20%; and 24% report startling increases of more than 20%.

One food executive notes, “Ingredient costs (grains) have risen over 400%.” Only 5% of food and beverage manufacturers report that prices had decreased.

All food and beverage manufacturers were subject to steep price increases, but larger firms were more successful at keeping costs in check. Approximately 51% of food and beverage manufacturers with annual revenues of more than \$100 million report that prices increased more than 10%, while 65% of smaller firms (revenues of \$100 million or less) report price increases of more than 10% (see chart).

Not surprisingly, price increases pose the biggest problem for food and beverage manufacturers (cited by 64% of respondents); 30% indicate product availability is their biggest problem; 15% late/wrong deliveries, 13% quality, and 12% lack of communication/information.*

* Participants were able to select more than one answer category.

Delivery and quality

Late/wrong deliveries may not be the biggest problem for food and beverage manufacturers, but it is easy to see why some companies are concerned by this poor service. Only 7% of food and beverage manufacturers indicate that deliveries are 100% on time, with the vast majority (69%) indicating that deliveries are 76-99% on time.

That still leaves one-quarter of food and beverage manufacturers that report deliveries of 75% on time or less. The quality of performance by suppliers is slightly better; 8% of food and beverage manufacturers report that quality is 100% to specifications, 78% report at the 76-99% range, and 14% at 75% or worse.

No issue is more prominent in the food and beverage industry than food safety. Most food and beverage manufacturers (and the public) are highly aware of this as they strive to improve internal processes and pursue a variety of practices to ensure the safety of purchased ingredients (see bar chart): 60% conduct testing of incoming ingredients at their own site, 53% prequalify/precertify suppliers, and 44% conduct periodic on-site audits of suppliers using company staff.*

* Participants were able to select more than one answer category.

What is surprising, given the broad awareness of food safety issues, is that 10% of food and beverage manufacturers report having “no systems in place” to ensure the safety of purchased ingredients.

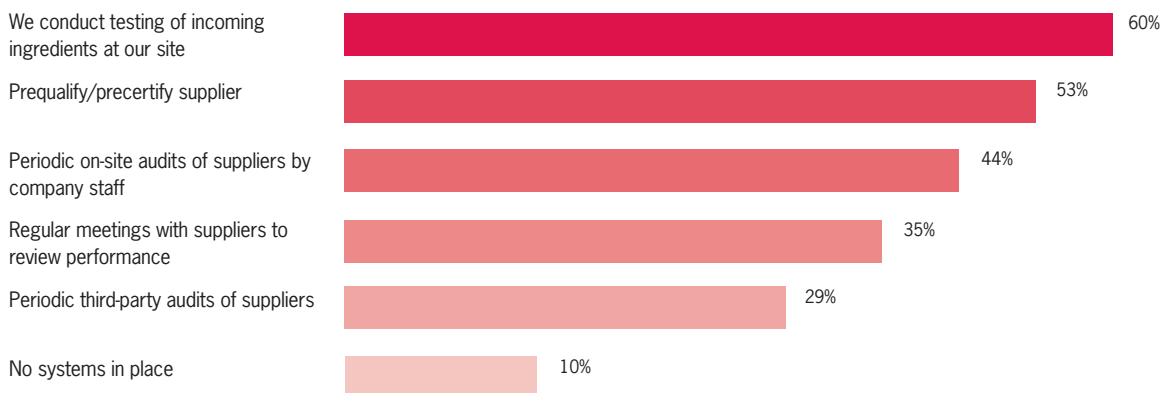
Many survey participants expressed confidence in quality and safety throughout their supply chains, such as, “We have a good commercial relation with our supplier because they are our partners to increase the safety and quality in our goods” and “Certified suppliers ensure that the quality of products meet specifications before shipment to us.”

Yet some manufacturers are concerned and looking for regulatory answers: “I wish at my level there was a lot more [involvement by] the government FDA/USDA [for] safety, security and oversight. I know this sounds odd to global business corporations, but I would welcome my government to be able to protect me and my clients.”

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Price change for primary materials/ingredients

% of participants by annual revenues



About suppliers

Survey participants report that a median 80% of suppliers (average 70%) are located in North America (U.S., Canada and Mexico). The next highest location of suppliers is Europe, with an average of 11% (median 0) (see table). Surprisingly, food and beverage manufacturers with the lowest revenues (\$100 million or less) were slightly less likely to have their suppliers located in North America than large companies (more than \$100 million): median 80% (average 67%) vs. median 83% (average 77%).

Most food and beverage manufacturers have not yet consolidated their supply bases. Only one-fourth indicate that 25% or less of their suppliers account for 80% of materials/ingredients (modern manufacturing theory suggests that 20% of suppliers should provide 80% of materials). Approximately 31% of suppliers report that 76-100% of suppliers account for 80%, indicating that most suppliers in the industry are highly specialized.

In the end, food and beverage manufacturers must resolve problems with suppliers and optimize supply chain management or face larger business issues. One small-firm executive outlined both the challenges and opportunities: “The price of my ingredients and packaging has gone through the roof! As a boutique, relatively new company, I am having a very hard time keeping it all going. All in all, the name of the game is perseverance, tenacity and good attitude.”



Location of suppliers

	Average	Median**
North America	70.0%	80.0%
Latin America	3.4%	0.0%
South America	3.2%	0.0%
Europe	11.1%	0.0%
Asia (not China)	5.7%	0.0%
China	4.9%	0.0%
Australia	1.1%	0.0%
Africa	0.7%	0.0%

** A median of 0.0% indicates that at least half of these respondents do not have suppliers located in these countries.

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Profile of participants

A diverse group of food and beverage manufacturers are represented in the results of this survey (first in a series of six). While a majority of companies (51%) have revenues of \$25 million or less, 17% report revenue higher than \$500 million. Approximately 40% of companies produce processed foods, the largest food group represented, followed by meat, poultry and seafood (33%), bakery products (29%) and beverages (29%).* Two-thirds of respondents (67%) are involved with purchasing ingredients, 44% equipment, and 35% “other.”

* Participants were able to select more than one answer category.

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About Food Processing

Established in 1940, *Food Processing* is the premier publication for the packaged foods industry. *Food Processing* writes for the entire management team about the critical issues in bringing a product successfully to market, exploring the latest trends in new product development, marketing, process optimization, packaging and workforce management.