



Rabobank

Online Bakery: Browsing for Bread

Bakery Producers Look for Success in the Online Channel

Rabo Research

Food & Agribusiness Research and Advisory

Cyrille Filott
 cyrille.filott@rabobank.com
 +31 30 7123814

John David Roeg
 johndavid.roeg@rabobank.com
 +31 30 7121572

far.rabobank.com

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Online grocery is steadily becoming an important distribution channel for ambient, chilled and frozen foods in Western Europe. And contrary to popular belief, fresh products are often among the top-selling items. With that in mind, online retailing poses several challenges and provides various opportunities for the Western European bakery sector. Bakery producers need to take action in order to be successful in the online channel. Rabobank has identified two key ingredients for success: execution—for which it is important to understand the basics of online—and the right strategies to roll out for various kinds of bakery products.

Online grocery is growing fast in Western Europe. Neglecting this trend could translate into a serious loss of share for bakery producers. Contrary to popular belief, fresh and limited shelf-life products are often among the top-selling online categories. A good example is Swiss online-only retailer LeShop.ch, where fresh products account for over 50 percent of online orders. These orders also include bakery products, and, at pick-up locations, shoppers can even collect (just-in-time) freshly baked bread throughout the entire day.

Bakery products are an important category for every food retailer, as they are commonly included in the average grocery trip. The quality and selection of bakery products help a retailer to distinguish themselves and to build customer loyalty. In the online space, things are different, but still important. Therefore, in order for the bakery category to be successful, the relationship between food retailers and bakery producers needs to be reassessed at both ends. By doing so, high-quality fresh, limited shelf-life and long shelf-life bakery products should be widely available online. A potential fresher and/or broader product offer—and consequently, a better sales mix—could also provide some margin relief for both retailer and producer.

ONLINE GROCERY IS STEADILY BECOMING AN IMPORTANT DISTRIBUTION CHANNEL

... AND BAKERY IS NO EXCEPTION

Fresh products are often among the top-selling items

TAKING ACTION IN ORDER TO BE SUCCESSFUL IN THE ONLINE CHANNEL

BAKERY PRODUCERS NEED TO RETHINK

ASSORTMENTS

GAINING AND SHARING KNOWLEDGE WITH RETAILERS



Strengthen relationships and improve online sales volumes

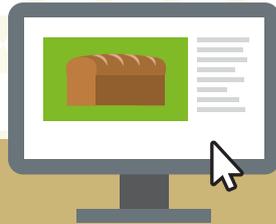
BETTER UNDERSTANDING OF WHAT SHOPPERS REALLY WANT



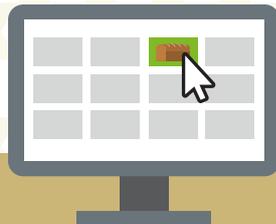
Up-to-date knowledge of health and diet trends

MARKETING STRATEGIES

MORE DYNAMIC WAY OF MARKETING



Invest in product pictures and product descriptions



Ensure products appear at the top of the screen



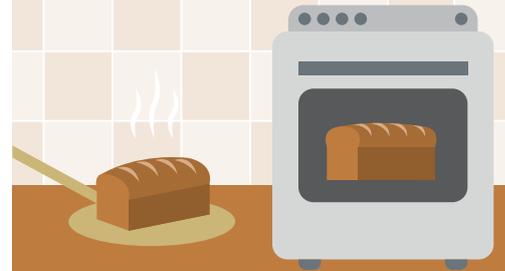
Avoid products being filtered out by retailers



Include 'fresh guaranteed' by showing the production date

SUPPLY CHAIN STRATEGIES

MORE EFFICIENT SUPPLY CHAIN



Start producing close to distribution centres



Develop shipping-proof packaging to maintain quality

CUSTOM-MADE APPROACH FOR VARIOUS MARKETS



Ensure availability of fresh bake-off, potentially in combination with a pick-up window for bread

ONLINE GROCERY IS SET TO CONTINUE ITS ROBUST GROWTH

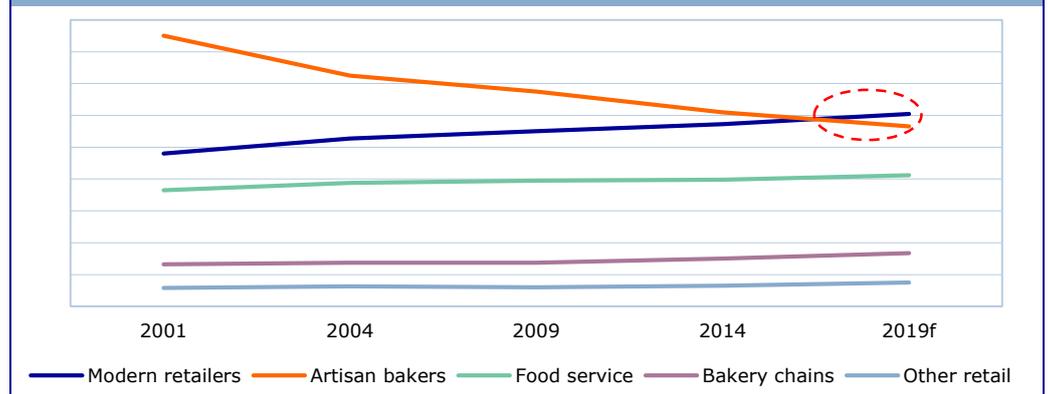
Box 1: UK retailers are leading in terms of online bakery offering

Whereas the UK and France both stand out in terms of online grocery adaptation—with penetration rates nearing 5 percent—there is a clear difference in terms of bakery product offering. The six leading UK online grocery groups have an average bakery assortment of 850 items, compared to more traditional France, where the number reaches ‘just’ 150. In a relatively underdeveloped online grocery market like the Netherlands, the average offering amounts to 275 items. There are a number of reasons that help explain the difference between the UK and France: British consumers buy more limited and long-life bread when compared to the French, which allows for a greater online offer; in general, order fulfilment in the UK is at a higher standard, which allows for a greater fresh offering; lastly, the French buy a greater share of their bakery products at artisanal bakeries.

Modern retail continues to take share from artisan bakers

As you might have noticed, your corner bakery has either gone under, is massively struggling or has been converted into a trendy coffee spot. This trend has been going on for a while now, and it’s driven by food retailers focusing on the bakery segment, in combination with changing consumer preferences, such as one-stop shopping (see Figure 1).

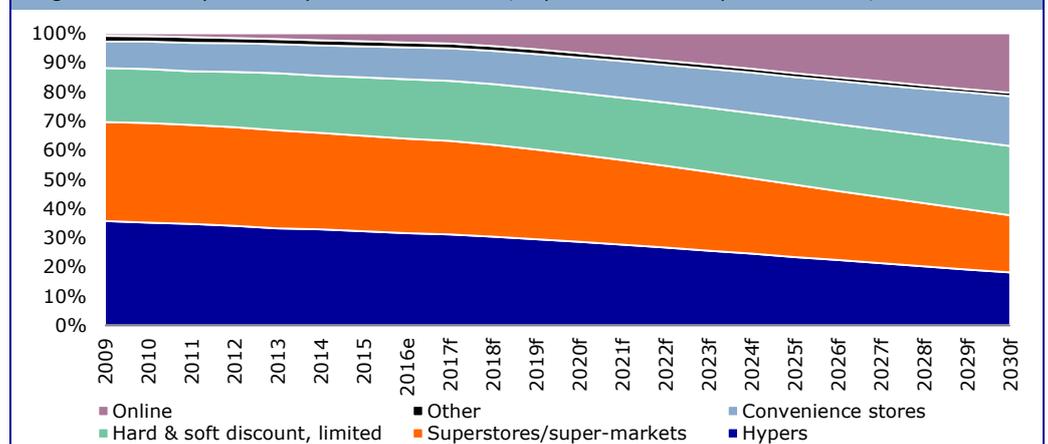
Figure 1: Historic bread purchase channel trends, 2001-2019f (thousand tonnes)



Source: Rabobank, adapted from GIRA, 2015

Rabobank expects online grocery to account for between 20 percent and 25 percent of grocery sales by 2030 in Western Europe (see Figure 2).¹ With that in mind, the key question is: Will those consumers who (partially) switch their grocery purchases from offline to online also include bakery products in their virtual shopping baskets? Data from UK-based customer science company Dunnhumby confirms that in the established online grocery markets of France, the UK and South Korea combined, multichannel shoppers—people who buy their groceries both via offline and online channels (16.3 percent of the population)—already buy 11.9 percent of their morning goods like bagels and croissants online. In general, the percentage of morning goods bought within the online channel is higher than in the offline channel. By contrast, online sales of sliced or prepacked bread are similar to offline sales, while sales of fresh bread/in-store bakery items are roughly 50 percent less online compared to offline.

Figure 2: Grocery channel penetration forecast, top 7 Western European countries, 2009-2030f*



* Note: Top 7 includes Belgium, France, Germany, Italy, the Netherlands, Spain and the UK.

Source: Rabobank, IGD, 2015

¹ See Rabobank Industry Notes *Food Processors Challenged by Online Growth Dynamics* (May 2014) and *The Good Old Days Are Gone* (May 2015).

Apparently, consumers do buy bakery products online, but when it comes to fresher items, they still tend to prefer offline channels. That being said, Dunnhumby has noticed that online fresh bread sales are currently growing about a third faster than overall online sales—thus slowly bridging the gap.

Online has implications for the bakery sector

Whether producing branded or private label, fresh, frozen or long-life bakery products, sooner or later producers will have to learn the ropes of selling online. Those that lack newly required skills run the risk of missing potential online sales and possibly losing contracts. In essence, this means that bakery producers will have to rethink their assortments, marketing and supply chain strategies.² By gaining and sharing knowledge with retailers, bakery producers can also strengthen their relationships.

Get the online basics right for assortments, marketing and supply chain

When it comes to selling their products online, few companies ask consumers what they really want to buy online, which packaging varieties, price points, etc. The online offer is often quite similar to the store assortment.

Searchability and the right assortment are key

Bakery producers have a genuine chance to sell those products shoppers really want online. But to do so, it is also important that shoppers actually see (or can find) these 'wanted' products when they browse retailer websites via their PC, tablet or smartphone. When people shop for up to 60 grocery items, they often make split-second decisions. Therefore, producers should invest in product pictures and the right product descriptions, and they need to understand or influence retailer taxonomy. When products are ordered a first time, they become part of 'saved' or 'my usual' shopping lists, which guarantees a certain amount of repetitive sales.

An abundance of filter options is another element that can greatly impact sales. With the click of a button, large sections within categories can disappear from screens. And what shoppers don't see, they don't buy! Depending on retailer filter technology, bakery producers should have a tailor-made strategy in order to avoid being completely filtered out. Up-to-date knowledge of health and diet trends is key. Monitoring social media and asking shoppers' opinions to keep informed is also a good starting point. In terms of production, complexity is likely to increase, as recipes need to change more often in combination with shorter runs. On the positive side, if producers better understand what shoppers really want to buy, they should—at least in theory—receive better prices for their products.

Box 2: Filters can greatly influence sales volumes

Online grocery retailers offer an abundance of filter options. Depending on the technologies used, in combination with the variety of filters, they allow shoppers to make pre-selections of the products they want to buy. In most cases, products that do not match pre-selected criteria disappear entirely from screens, or in some cases, they end up at the very bottom of shoppers' views. More sophisticated retailers even 'help' their shoppers by using big data to show them the products that best match their past shopping behaviour and/or lifestyle. These often-used filters, in combination with shopper profiling, can cause online and offline product sales volumes to differ substantially.

Rabobank has divided filters in three core categories, namely Health/Ingredient, Lifestyle and Other. Health/Ingredient filters help shoppers to select products that are gluten-, dairy-, sugar- or nut-free; have low sodium; or are cholesterol-free, to name just a few. Lifestyle filters allow shoppers to select products that fit in any kind of diet or are classified as organic. The last classification of filters, Other, includes such options as artisanal, local and fair trade.

Bakery producers should be well aware of shoppers' quickly changing preferences in terms of health and lifestyle. Solely relying on information from retailers won't suffice, as it will allow competitors to always be one step ahead.

² From Dunnhumby, *The Multichannel Movement* (February 2015). In the established online markets, 16.3 percent of the population are multichannel shoppers. On balance, these shoppers spend 30 percent more on groceries—both online and offline—compared to offline- or online-only shoppers.

Online requires a more dynamic way of marketing bakery products

The right promotional spending is also important. In order to sell, products need to appear at the top of screens. Most products appear at the top because they either belong to a retailer's own label, are a leading (benchmark) or popular (volume-wise) product, or a 'my usual' product (personalised offering). Producers of brands might have to spend money on banner advertising, product promotions (offers can often be found at the top of screens) and sampling (helping to make a product temporarily appear on 'my usual' lists).

Bakery products—especially fresh and limited shelf-life items (i.e. a maximum of one or two weeks)—require the right ‘fresh guaranteed’ strategy. In the more developed UK online grocery market, several retailers highlight product shelf-life by adding a roundel (or a bullseye symbol) to product pictures. What sometimes happens is that a competing branded or retailer-own-label product has a longer shelf-life, possibly in combination with a lower price point. While the shelf-life of brands is usually chosen by suppliers, those of retailer-own products are chosen by the retailers. Typically, producers who sell brands have higher quality standards, which translate to a lower number of fresh-guarantee days. But this strategy can backfire, as shoppers might think differently. Choosing between a more expensive branded bread with three days’ guarantee and a cheaper retailer-own copy with four days’ guarantee might result in the purchase of the latter, as shoppers might think the more expensive product is less fresh.

As online grocery retailers gradually reach critical mass, they will increasingly invest in a more efficient supply chain. For consumers, this would result in fresher and better-quality products, but also in a broader product offering (a.k.a. long-tail). For the average bakery producer, this would imply an opportunity to increase the product offering at potentially better margins, as long-tail products are generally less price-sensitive. On the other hand, competitors would also be able to increase their online offering, thereby further increasing the fight for effective screen positions. Cross-sell promotions (e.g. combination buys) could provide an effective tool for bringing less popular products to shoppers’ attention and placing them onto ‘my usual’ lists.

Online requires a more flexible supply chain and damage-proof packaging

The evolution of online order fulfilment goes from store picking and dedicated fulfilment centres (also known as dark stores) towards semi-automated facilities. These dedicated fulfilment locations are either stocked by retailers’ central distribution centres or directly by suppliers. In the case of the latter, this likely implies extra delivery costs related to smaller-than-usual drops. As online grocery continues to grow over time, drop sizes should increase... and hence, costs decrease. Over time, Rabobank envisages that online grocers might also set up bake-off facilities or bakery lines in order to supply the freshest-possible bakery items.

Six out of every ten breads sold in Europe are prepacked, and most bakery products are fresh products (68 percent), with the balance being pre-packed long-life products. The issue of shipping-proof packaging also goes hand in hand with the growth of online bakery. Often, a combination of plastic and paper is used, as it is easier to print text (e.g. freshness period) on the paper part. Shipping a cake in a damage-proof way is also different, as it needs to be cooled. An increasing number of affordable packaging solutions is tackling this problem. These range from reusable bags to one-way (insulated) boxes. These products are being developed by specialists like Tempack, retailers, and/or postal & express services.

Neglecting online could impact overall sales volumes

Industrial bakeries should actively influence and cooperate with retail to improve their online sales volumes. By not doing so, they run the risk of their overall sales volumes (offline and online combined) coming under pressure, as online shoppers choose alternative products instead. A good example are beverages in the UK. CheckoutSmart tracks the online grocery orders of about 20,000 of its UK members. Between May 2014 and May 2015, they noticed remarkably strong increases of soft drinks, beer and white wine as a percentage of every GBP 100 spent (increases between 12 percent and 22.9 percent). The explanation lies in the lack of focus previously shown by these producers (i.e. they neglected online as an important channel), rather than in a surge in overall consumption.

A differentiated approach across products is key

With online grocery rapidly growing across Western Europe, bakery producers should develop a custom-made approach for the various markets. In France, for instance, where it is mainly pick-up points that drive online growth, several retailers are piloting additional pick-up windows for freshly baked baguettes and other bread products. In the Netherlands, consumers often put fresh breads in the freezer for later consumption. With this habit in mind, a leading Dutch online grocer is offering frozen freshly baked bread. This way, consumers get a better bread product after defrosting.

Across all offline channels, we can distinguish the following three bakery product categories: i) Fresh (shelf-life of a day); ii) Limited shelf-life (up to a week); and iii) Long shelf-life (up to several months). Fresh products include fresh bread, rolls and croissants. Limited shelf-life products include pre-packed bread and chilled products. Long shelf-life products include (gas-packed) breads and bake-off varieties.

Fresh bakery products are a true means for differentiating online

In terms of online consumer uptake, we would expect some initial hesitance coming from consumers, especially those in countries like France, with a sizeable, albeit shrinking, artisanal channel. Fans of artisanal bakeries probably don't buy much of their fresh bread in supermarkets anyway.

In the UK, online grocery is predominantly home delivery, whereas in France, it is mainly click & collect. In order to increase consumer uptake of fresh bakery products, several French retailers are conducting tests with separate bakery pick-up windows at their pick-up locations. This way, shoppers can add impulse bakery buys to their online orders.

Moving forward to further improve the selection, quality and image of fresh bakery products for the online grocery channel, industry and retailers will have to work closely. Think of solutions like on-site baking-off facilities and a time-stamping for freshness guarantee. But equally important is being able to offer unique products that can really help differentiate retailers in a market which, by definition, will become more (price) transparent.

Limited shelf-life product sales can benefit from freshness guarantees

When compared with fresh, the short shelf-life category faces different challenges and opportunities. It's important that retailers are able to convince the consumer about product freshness, quality and how long the product can be stored before consumption. The latter is very important, since online grocery purchases usually replace two to three regular shopping trips and thus include purchases not intended for immediate consumption. In the UK, it is common practice on retailer websites to provide guaranteed freshness days for every single item. In France, this is less the case—in part due to a less sophisticated order picking structure, often including store picking, remaining in place. In the case of the latter, it is impossible for French retailers to publish freshness days on their (local) sites.

Long shelf-life products face fewer obstacles

Long shelf-life products face substantially fewer challenges than their fresh and limited shelf-life peers. Compared to offline assortments, online products do not require materially different packaging or extensive freshness guarantees. Production batches can remain relatively high, with costs low, as products can be stored before being replenished. This flexibility, among other things, provides excellent marketing opportunities. Think of promotions or combo deals with other categories.

Box 3: Alternative distribution models—small, but growing fast

Bakery producers should also review their strategy when it comes to online-inspired new distribution models. These include online bakery specialists, ecosystems of the likes of Amazon and Alibaba, direct-to-consumer trading platforms, meal kit/box home delivery services and online food service/QSR services involving bakery products.

Online ordering of birthday and personalised cakes is becoming popular in several countries. Providers even offer the possibility to upload a picture, which is then printed on the cake. This type of service is offered by online grocery retailers, mixed variety retailers and an increasing number of specialists with names like Cakes Next Day (UK), votreGateau.fr (F), deineTorte.de (D) and gefeliciTAART.nl (NL), but also by other online bakery specialists like Sponge (UK), which offers next-day delivery of sponge cakes, in addition to birthday and personalised cakes.

A group like Amazon is continuously testing new delivery and service concepts. One of these tests includes one-hour meal deliveries from local restaurants, but fruit & vegetable deliveries from local growers (farmers' markets) are also currently being piloted. We think

extending these tests by delivering fresh or limited shelf-life bakery products would be a possibility.

There are also opportunities for branded bakery products if and when FMCG producers create new trade platforms to circumvent the traditional retail trade. For such platforms to become successful, a one-stop shopping experience would be preferred, thereby offering a full palate of bakery products.

Meal kit solutions are becoming very popular in many Western European countries, but also in the US and Australia. Meal kits as offered by groups like Blue Apron and HelloFresh now include fruit & vegetables, meat and fish. On a small scale, there have already been pilots with breakfast meal kits, which also include bakery items. In a developing economy like India, online specialists like Zomato offer breakfast boxes and bags, which also include bakery products. Fulfilment of these boxes is taken care of by partnering local restaurants.

In China, the online breakfast market is growing rapidly. For a small amount, customers can pre-order a coffee and bakery product for pick-up the next morning from local food service outlets.

Conclusion

Online grocery will continue its robust growth in the foreseeable future, and this will have implications for bakery producers. Now is the time for action. Bakery producers should rethink their assortments, marketing and supply chain. A sit-and-wait approach may eventually result in loss of market share and a hard-to-bridge gap with groups that embrace the new channel. Thus far, we have seen strong online sales trends for long-life and morning goods like bagels and Danish. In the meantime, fresh products have had a slow start online, but have begun to catch up.

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