

STRUCTURE AND FEATURES OF FOOD DISTRIBUTORS IN KOREA

DONG-HWAN KIM*

i. Introduction

In Korea, small scale shopkeepers dominate food distribution in urban areas. Korean people buy food products at small shops located near their residence. One can easily find "mon-and-pop" stores on almost every corner of streets. Butcher shops and fruits stores are also found in every neighborhood. Food wholesaling is also carried out by small merchants in an efficient way.

In general, food products are sold to consumers through multiple marketing stages. As a result, marketing margins of food products are generally greater than those of manufactured goods. In populous urban areas, wholesale markets play a major role in collecting and distributing food products.

Although the food marketing industries are criticized as being inefficient, it consists of a large number of small-scale stores which provide urban people with a great number of jobs. While the shares of GDP accounted for by agriculture sharply decreased from 15.6 percent in 1981 to 8.8 percent in 1991, the importance of food wholesaling and retailing industries in the national economy has been stable during the same period. The shares of gross domestic product (GDP) and total employment accounted for by food distribution industries have been 2.2 - 2.8 percent and 3.3 - 4.0 percent, respectively (Kim et al., 1994).

The purpose of this paper is to describe the structure and features of food distributing industries. Following introduction, food retailers and wholesalers are discussed in order. In both sections, structure is discussed and then some characteristics are examined.

* Research associate, Korea Rural Economic Institute, Seoul, Korea.

Focusing more on the distribution of commodities, this paper briefly examines the structure of processed food distribution. Lastly, recent developments and changes in the food distribution system are discussed in order to project the future of the industries. However, the structure of food service and processing industries is not examined in this paper, which focuses on retailing and wholesaling.

II. Retailers

1. General Structure

In Korea, food retailing has been dominated by traditional small-scale stores. Food and beverage products are sold through not only food stores, but also street stalls and peddlers. Food stores are generally small in scale and many of them are located at traditional market places. However, one can observe an increasing number of modernized food stores, such as supermarkets and convenience stores in recent years.

According to the National Statistical Office of Korea, there were 300 thousand food and beverage retail stores in 1991, providing employment to 514 thousand people¹. Food stores are distributed more densely in Korea than any other countries. There is one food store per 142 persons in Korea. While this figure is comparable to 199 persons in Japan, it is much less than 1,412 persons in the United States.

The numbers of establishments and employees in the food and beverage retailing industry have decreased since 1986. From 1986 to 1991, the number of establishments decreased by 2.1 percent and that of employees decreased by 2.6 percent. By contrast, total area of establishments has grown during the same period, indicating an expansion in the size of food shops.

About 49 percent of food shops in Korea were operated by one person and 50 percent by two to four persons. Stores with more than 50 employees represented merely 0.13 percent of total food store

¹ Statistics on retailing and wholesaling industries are available from National Statistical Office of Korea. However, statistics for street stalls and peddlers are not available.

establishments. Most food stores are family-owned businesses that share their space with the residence. Small family-owned food shops have been historically viable due to high population density, frequent trips to the stores, an emphasis on service, and the freshness and quality of the foods they carry.

The average size of food and beverage stores is quite small compared to those in Japan and the U.S. In 1991, sales and employees per establishment were 57 thousand dollars and 1.7 persons, respectively (Table 1). In terms of sales, the average size of Korean food stores is one eighth of Japanese food stores and one thirty-sixth of American food stores. Korean food stores, on the average, have a half size of employees compared to Japanese counterparts, and one ninth compared to American food stores. Food stores in Korea also have quite small selling space. Average selling area was only 29 m² in 1991. Being small-scale, labor productivity is also very low. Sales per employee in Korean food retail stores were 33 thousand dollars, much less than 113 thousand dollars in Japan and 128 thousand dollars in the U.S. (Kim et al., 1994).

TABLE 1 International Comparison of Food Retailers in Korea, Japan, and U.S.A.

	Establishments	Sales	Employees
(Total)	(number)	(\$ mil.)	(numer)
Korea (1991)	304,971	17,261	514,430
Japan (1991)	622,751	293,160	2,541,778
U.S.A. (1992)	180,568	369,199	2,969,317
(Average)		(\$ thous.)	
Korea (1991)		57	1.7
Japan (1991)		467	4.1
U.S.A. (1992)		2,044	16.0

Sources: National Statistical office of Korea, *Report on 1991 Establishment Census Vol. 3: Wholesale and Retail Trade*, 1992.

Ministry of international Trade and Industry of Japan, *1991 Report on Business Statistics*.

U.S. Department of Commerce, Bureau of the Census, *1992 Census of Retail Trade: Geographic Area Series, United States*, RC92-A-52, 1994.

2. Store Formats

In Korea, major forms of food retailers are small-scale general food stores and specialty food stores carrying only a limited range of products. Small-scale mom-and-pop stores accounted for about a half of establishments and employees, but 34 percent of sales in 1991 (Table 2). Specialty shops, such as rice, meat, fish, fruits, vegetable, and tobacco stores, accounted for 46.5 percent of establishments, 44.3 percent of employees, and 45 percent of sales in 1991. By contrast, specialty shops accounted for only 6 percent of food store sales in the U.S. (U.S. Department of Agriculture, Economic Research Service, 1994).

Modernized grocery stores are not a dominant form of food retailers in Korea, although the number of supermarkets and chain stores are currently increasing. The number of supermarkets is only 0.8 percent of total establishments, but their sales are 13.0 percent of total food store sales.

TABLE 2 The Shares of Food Stores Accounted for by 'Kind of Business', 1991.

Kind of Business	Establishments (%)	Employees (%)	Sales (%)
General stores			
Mom-and-pop stores	49.0	45.8	33.8
Supermarkets	0.8	4.6	13.0
Chain stores	3.7	5.3	8.2
Specialty stores			
Rice and other cereal stores	8.6	8.8	10.9
Meat and poultry stores	10.6	10.8	11.7
Fresh fish stores	8.0	6.9	7.8
Vegetable stores	7.5	6.5	5.1
Fruits stores	5.3	4.7	3.9
Tobacco stores	2.6	2.0	1.7
Miscellaneous retail food and beverage stores	3.9	4.6	3.4

Sources: National Statistical office of Korea, *Report on 1991 Establishment Census Vol. 3: Wholesale and Retail Trade*, 1992.

² In Korea, grocery stores having size of 165m² and more are defined as supermarkets.

There were 2,248 supermarkets in 1991, up from 2,123 in 1986 (National Statistical office of Korea, 1992). A supermarket, on the average, employs 10 persons and its selling area is 391.4m². The size of supermarkets is much smaller than that of Western countries. Average selling area of supermarkets in the U.S. is about 2,000 m² (Marion, 1988).

Foods and beverages are the most important items in supermarket sales. Food products accounted for about 75 percent of total sales. Perishables and processed foods took 30 percent and 41 percent, respectively.

Korea has a unique system of affiliated retailers. Based on *the Wholesaling and Retailing Development Law*, the headquarters are designated and supported by the government if they satisfy the conditions set by the Law. The headquarters not only open their own stores, but also recruit independent stores as their affiliated retailers.

Affiliated stores have independent ownership, but use the same store names as their headquarter which are supposed to supply all the items retail stores want to carry. The objective of this arrangement is to enhance marketing efficiency by establishing distribution networks similar to chain stores in the Western countries.

In 1991, 13,395 food retailers were affiliated with the headquarters, nearly tripled since 1981 (Korean Super-chain Association, 1994). Although the number of affiliated retailers has grown rapidly, the role of the headquarters has not been significant. Due to the lack of capital and management skills, the headquarters do not function well as expected. In 1991, the headquarters supplied only 30.3% of products sold at their affiliated stores (Ministry of Trade and Industry, 1991). Tax problems also negatively affect the distribution function of headquarters. Affiliated retailers often purchase products at black markets to evade taxes. However, they can buy alcoholic beverages at cheaper prices through the headquarters than any other channels. That might be the only reason that grocery stores want to be affiliated with the headquarters.

In sum, food items are sold mainly through small "mom-and-pop" type stores at the retail level in Korea. Most food stores are independent and western style supermarket chains are not yet developed.

III. Wholesalers

1. General Structure

In 1991, there were 27 thousand food wholesalers in Korea, providing jobs to about 140 thousand people. The total size of the industry has grown steadily. The number of establishments and employees doubled during 1981 - 1991.

Food wholesaling is mostly run as a small family business. Food wholesalers having employees of four or less than four accounted for 58% of total establishments. And about 90% of total establishments were operated as a family business.

The average size of food wholesalers in Korea is very small; each establishment employs only 5.1 persons and is operated in the area of 88.5 m² (Table 3). Such size of operation is too small to compare with those in other countries. Japanese food wholesalers are

TABLE 3 International Comparison of Food Wholesalers in Korea, Japan, and U. S. A*.

	Establishments	Sales	Employees
(Total)	(number)	(\$ mil.)	(number)
Korea (1991)	27,326	20,116	140,158
Japan (1991)	99,987	763,437	977,053
U.S.A. (1992)	54,425	641,436	920,612
(Average)		(\$ thous.)	
Korea (1991)		736	5.1
Japan (1991)		7,635	9.8
U.S.A. (1992)		11,786	16.9

* Wholesalers of raw agricultural products are included in the category of food wholesalers.

Sources: National Statistical Office of Korea, *Report on 1991 Establishment Census Vol. 3: Wholesale and Retail Trade*, 1992.

Ministry of international Trade and industry of Japan, *1991 Report on Business Statistics*.

U.S. Department of Commerce, Bureau of the Census, *1992 Census of Wholesale Trade: Geographic Area Series*, United States, WC92-A-52, 1994.

about twice greater in employment size and about ten times greater in sales than Korean counterparts. Food wholesalers in the U.S. are much greater than those in Japan and Korea. The average size of American food wholesalers is about 3.3 times greater in employees and 16 times greater in sales volume than Korean wholesalers.

2. Characteristics of Food Wholesalers

In addition to small-scale, food wholesalers in Korea have characteristics different from those in the Western countries. Some characteristics of food wholesaling industries in Korean are as follows.

First, general-line distributors are not yet developed. Most food wholesalers in Korea are specialty wholesalers which buy and sell a group of products having similar physical characteristics. In other words, each of most wholesalers specializes in carrying one or two of such items as grains, fruits, vegetables, meat, fish, etc. In terms of establishments and sales, wholesalers carrying produce, fish, and beverages have a lion's share among various types of business (Table 4).

TABLE 4 The Shares of Food Wholesalers Accounted for by 'Kind of Business', 1991.

Kind of Business	Establishments	Employees	Sales
	(%)	(%)	(%)
Rice and other cereals	4.3	3.5	4.2
Meat and poultry products	6.0	3.8	2.4
Fish and marine products	11.2	7.3	7.9
Fruits and vegetables	21.9	11.3	10.0
Breads and confectionery	5.6	7.2	6.2
Non-alcoholic beverages	19.8	28.5	16.6
Alcoholic beverages	6.2	11.9	20.6
Processed foods	13.8	17.3	16.1
Miscellaneous food and beverage	11.1	9.2	15.8

Sources: National Statistical Office of Korea, *Report on 1991 Establishment Census Vol. 3: Wholesale and Retail Trade*, 1992.

Small-scale food stores and restaurants procure produce and livestock products mainly from public wholesale markets in large cities. Only a small share of such products is purchased directly from producers or local shippers. Therefore, wholesale markets located in urban areas play an important role in the marketing of unprocessed agricultural products. There are about 180 produce wholesale markets, eleven livestock product wholesale markets, and a grain wholesale market. Among them, the government owns and operates ten produce wholesale markets and a grain market. Agricultural and livestock cooperatives and their federations³ also operate their own marketing centers which function as wholesale markets (72 produce marketing centers and three livestock product marketing centers).

The distribution of packaged food products and beverages is totally different from that of perishables. The marketing of these products is vertically tied to manufacturers⁴. Many manufacturers have developed their own distribution channels, establishing exclusive dealers and manufacturers' own sales outlets⁵. Under this arrangement, a dealer should carry products of a certain manufacturer exclusively. In addition to the exclusive dealership, retail price maintenance has been a common feature of the trading relationship between manufacturers and distributors. Other business practices in Korean food marketing include the use of rebates by manufacturers to maintain the loyalty of wholesalers and retailers, the staffing of retail outlets by employees of the manufacturers, *ex post facto* pricing, and small lot high frequency deliveries.

These vertical ties between food manufacturers and distributors are, however, now being changed as new forms of retailers emerge. In recent years, discount stores and membership wholesale clubs (MWC) have been opened in large cities. They purchase, by cash, products from manufacturers at lower prices than the prices to their

³ In Korea, agricultural cooperatives are organized separately from livestock cooperatives at the local level. These cooperatives are then organized to form respective national federations. As a result, the cooperatives are highly centralized and the national federations play a significant role in the marketing of agricultural and livestock products.

⁴ It is difficult to statistically describe marketing systems of processed foods and beverages. The description is based on casual observations.

⁵ This type of vertical structure makes it difficult for new entrants to penetrate the market.

designated dealers, and sell at lower prices than the prices recommended by manufacturers. Although these types of independent distributors are in the early stage of development, it is expected that they will grow rapidly.

IV. Recent Developments in Food Marketing

1. Foreign Investment in Food Distributing Industries

The Korean government has gradually liberalized foreign direct investment in distribution industries. Foreign investment in wholesaling and retailing industries has been allowed for certain types of business unless it violates governmental restrictions on the number and size of stores. However, these restrictions have been eased in recent years.

Foreign direct investment in distribution industries began in 1981 by allowing the investment in a single store less than 300m². The restriction on the selling area of stores has been eased step by step. Currently, foreign investment is allowed up to 20 stores and selling area of 3000m². From 1996, the restrictions on the number of stores and selling area have been lifted.

In food retailing and wholesaling industries, the government allows foreign investment in all types of business except cereal wholesaling and meat wholesaling. Until last year, foreign investment has not been allowed for cereal retailing and meat retailing, but the investment on these retailing industries has also been liberalized from 1996. Furthermore, the investment in chain store operation will also be liberalized from 1996.

As foreign investment and licensing is liberalized, several foreign food marketing firms opened or plan to open their stores in Korea. European and Japanese firms already invested in food retailing and wholesaling (Table 5). Carrefour and Makro, big European distributors, are constructing a hypermarket and a warehouse store in 1996, respectively. They also bought lots for other stores.

In addition to direct investment, foreign firms have license agreements with Korean counterparts. Licensing is a common practice in convenience stores. Having license agreements, Korean convenience stores use the store names of American chains, such as

Seven Eleven, Lawsons, Circle-K, AM.PM, and Japanese chains, such as Family Mart and Mini Stop. The licensor also allow the licensees to use their know-hows related to chain store operation.

Two supermarket chains (Hanyang and Haitai) also had licensing agreements with Japanese counterparts to learn the know-hows related to chain store operation, but they did not renew the licensing agreements. Having a licensing agreement with Price Costco of the U.S., the Sinsegye department store opened a membership wholesale club (MWC) store under the name of Price Club.

TABLE 5 Foreign Food Distributing Companies in Korea.

Company Name	Nationality	Types of investment	Amount of inv. (\$ 1000)	Store formats
Carrefour	Netherlands	Single	60,000	Hypermarkets
Netherlands, B.H.	lands	Venture		
S.H.V. Holdings, NV	Netherlands	Joint Venture	24,833	Warehouse stores
Miyamoto Kumi	Japan	J.V.	421	Supermarkets
JRJ Co.	Japan	Single	751	Health foods wholesaling
CCNR Co.	Switzerland	Single	5,200	Non-alcoholic beverage wholesaling
Daiken Co.	Japen	Single	61	Food marketing

Source: Ministry of Finance, 1993.

The existence of foreign distributing firms is not yet significant since there are still the restrictions on foreign investment and other entry barriers, such as consumers' behavior and trading customs which are different from those of the Western countries. However, more foreign firms are expected to invest in Korea after 1996 when the restrictions on foreign investment are lifted. Currently, U.S. and Japanese firms plan to open their stores in the near future. While U.S. firms intend to invest in wholesaling and discount stores, European and Japanese firms have plans to open supermarkets and hypermarkets.

2. Advent of New Store Formats

As foreign direct investment in distribution industries is liberalized, new forms of retail stores have been introduced in recent years. Convenience stores have been introduced through license agreements. The number of convenience stores sharply increased from seven in 1989 to 1,404 in 1993 (Korea Super-chain Association, 1994). The number of convenience stores has increased rapidly in Korea since they open 24 hours and have clean selling spaces. It is also expected that the number of convenience stores will increase further in the future.

Most convenience stores are organized by chains. In 1993, there were eight convenience store chains (Korean Super-chain Association, 1994). Unlike supermarkets, the headquarters supply most of products sold in the chain stores and affiliated stores. Although the average size of convenience stores is smaller than that of supermarkets, nearly all of convenience stores are equipped with the Point of Sale (POS) computer system.

In addition to convenience stores, several kinds of discount stores are quite successful in the large cities. There are four discount stores (E-mart, New Mart, Grand Mart, and Samchonri Mart) which imitate store formats of Wal Mart and K-mart⁶. It is expected that, as consumers become more sensitive to prices, the number of discount stores will increase further in the future.

Recently, two membership wholesale club stores (Price club and Kim's club) were also opened in populous areas⁷. The membership wholesale club is very popular in the U.S. and prices are lower than any other retail store formats. Selling area of the wholesale clubs is greater than that of supermarkets and other grocery stores. National Agricultural Cooperatives Federation also operates five wholesale clubs which specialize in agricultural products.

⁶ Unlike in the United States, discount stores in Korea sell perishable foods and processed foods in addition to general merchandise. In aggregate, food items take 40-50% of total sales.

⁷ Wholesale club is a hybrid wholesale-retail establishment selling food, appliances, hardware, office supplies, and similar products to its individual and small-business members at prices slightly above wholesale prices (U.S. Department of Agriculture, Economic Research Service, 1992-1993 *Food Marketing Review*).

Having warehouse-like selling area and low services, the discount stores and membership wholesale clubs sell food items in prices 20-30% lower than supermarkets and other retail stores. These lower prices are eagerly welcomed by consumers. However, these stores do not purchase agricultural products directly from farmers or local dealers. In most cases, they purchase agricultural products at the wholesale markets in urban areas, and resell to consumers.

3. Government's Plans for Improving Agricultural Marketing

In order to improve the marketing of agricultural products, the Korean government has established a plan for investing large sums of money in constructing marketing facilities. According to the plan, about 10 trillion won (12.8 billion dollars, 1995 constant dollar) will be invested in constructing shipping and packing facilities in producing areas and distribution facilities in urban areas.

When constructing marketing facilities, the central government is supposed to subsidize 50 percent of total construction costs. Major construction plans are as follows: In producing areas, it is planned to construct 4,000 produce shipping points and 160 produce packing houses. It is also planned to construct more public wholesale markets and distribution centers in urban areas. By 1998, the number of public wholesale markets will be 34, covering most of urban areas in Korea. The government also plans to construct a number of marketing facilities for livestock and fishery products.

The construction of marketing facilities will affect food distributing industries. First of all, as discussed before, the importance of public wholesale markets in agricultural marketing is expected to increase. Agricultural and livestock cooperatives will be more active in food marketing than ever since they plan to play a major role in constructing marketing facilities. The emphasis on agricultural cooperatives in food marketing may impede the growth of private marketing firms, such as general-line wholesalers and shippers. The government's plan may also impede the direct marketing of agricultural products between local shippers and wholesalers or supermarket chains since the government over-emphasizes the role of the public wholesale markets.

V. Conclusions

The Korean food distribution system has been dominated by large numbers of small shops. General-line distributors are not yet developed and the share of retail food sales accounted for by grocery stores is very low. Due to these factors, physical efficiency in food distribution is generally low and the high prices are forced on consumers. The development of modern and large scale distribution firms has been impeded due partly to poor grading and standardization, traditional trading customs, and tax problems.

Since farming units and food retailers are so small, a large number of merchants are engaged in collecting and distributing agricultural products. In addition to middlemen specializing in collecting and distributing, wholesale markets in urban areas play a major role in food marketing. On the contrary, direct marketing between shippers and retailers does not play as an important coordination mechanism. In the marketing of agricultural products, processors are not important since the degree of processing is very low. Food products are mainly marketed through merchants who sometimes carry out simple processing on food items they buy. In the case of more sophisticated processing, processors are more likely to rely their raw materials on imports.

The distribution channels of processed foods are totally different from those of perishables. It is a general situation that manufacturers have their own distribution systems, awarding exclusive dealership to designated agents. To increase the loyalty of retailers, manufacturers sometimes give rebates to retailers, support promotions, and provide sales personnel to retailers.

It is, however, expected that the food distribution system will change to a more efficient one as western style supermarkets and various types of discount stores emerge in recent years. Large scale foreign marketing firms also have plans to open their stores in Korea. These stores sell food products at lower prices than conventional retail outlets. Although supermarkets and discount stores currently purchase most of perishables at the wholesale markets, they are expected to purchase agricultural products directly from producers and local shippers as their stores become organized as chains. Moreover, they will also turn their eyes to imports when imported

products have lower prices than domestic products since they are very sensitive to prices.

REFERENCES

- Kim, Donghwan and Changgon Chun. 1994. *A Study on the Liberalization of Foreign Investment in Service industries Related to Agricultural Marketing*, Korea Rural Economic institute Research Report R307 (in Korean).
- Korea Chamber of Commerce. 1993. *Statistics on Distributors* (in Korean)
- Korea Super-chain Association. 1994. *1994 Almanac of Distributors* (in Korean).
- Marion, Bruce. 1988. "Food Retailing and Wholesaling in the United States: Organization, Trends and Competition" University of Wisconsin Department of Agricultural Economics Food System Research Group Working Paper WP-1.
- Ministry of Finance. 1993. *A List of Firms Invested by Foreigners*.
- Ministry of International Trade and Industry of Japan, *1991 Report on Business Statistics* (in Japanese).
- Ministry of Trade and Industry. 1991. "Survey Results of Headquarters and Affiliated Stores."
- National Statistical office of Korea. 1992. *Report on 1991 Establishment Census Vol. 3, Wholesale and Retail Trade* (in Korean).
- Riethmuller, Paul. 1994. "Recent Developments in the Japanese Food Distribution System" *Food Policy* 19(6): 517-32.
- Sung, Bai-Yung. 1993. "Korean Agricultural Marketing System: Its Efficiency and Performance" *Journal of Rural Development* 16: 15-40.
- U.S. Department of Agriculture, Economic Research Service. 1994. *Food Marketing Review 1992-1993*.
- U.S. Department of Commerce, Bureau of the Census. 1994. *1992 Census of Wholesale Trade: Geographic Area Series, United States*, WC92-A-52.
- U.S. Department of Commerce, Bureau of the Census. 1994. *1992 Census of Retail Trade: Geographic Area Series, United States*, RC92-A-52.