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Main

SANCHOKU AT THE CROSSROADS

A Discussion on Recent Trends in Co-ops' Direct Buying Routes from Producers

Features

Review of Consumer Co-operative Studies June 2004

What is Sanchoku?

Sanchoku, translated as direct transaction or direct buying routes from producers to consumers, is a Co-op devised system to provide vegetables, fruits, meat, seafood, and other fresh food products directly, without the use of wholesalers, or other middlemen, from individual producers or agricultural organizations, such as agriculture and fishery co-ops, to Consumer Co-ops. The Co-op concept of direct transaction sets itself apart from other retailer's systems of direct buying by guaranteeing that all food labeled Sanchoku meets the strict safety standards set by Co-op. Sanchoku is seen as a way of guaranteeing the safety of products for members.

Basic Principles of Sanchoku

- (1) Trace ability: The origin of the product (production site) and the producer is identifiable
- (2) Standardization: The method of production is in accordance with Co-op specifications and fully disclosed and traceable. The farming, breeding and production methods must follow Co-op specifications with regard to the use of agricultural chemicals, fertilizers, feed, antibiotics and additives etc.
- (3) Communication: The system must provide the opportunity for direct exchange of information between producers and Co-op members.

Overview of Development

Sanchoku has been an integral part of the Co-op philosophy and way of doing business for more than 30 years. Consumers' anxiety over food safety and the credibility of agricultural products was the springboard on which Sanchoku was created. The Sanchoku system offers safe food at reasonable prices. The Sanchoku system has continued to grow over the years

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and has seen various growth spurts when consumer interest in the system increased following incidents of mislabeling and deception by the food industry.

Sanchoku was widely adopted by Co-ops in the 1970s following numerous incidents of mislabeling and food contamination in the 1960s due to a lack of standards and production systems that were heavily reliant on the use of chemicals and additives to produce "food with perfect appearance." Japanese consumers placed great emphasis on blemish free and uniform size and colored produce, which requires extensive labor and the use of chemical fertilizers and pesticides. Co-op was among the first groups to begin to consumers that an understanding of the process of production is as important at the appearance and taste when it comes knowing if a produce is safe to eat. In the 1970s, producers and regular wholesale channels were very suspicious of the new Sanchoku system that challenged the food industry's control of the food supply chain.

In the 1990s, Sanchoku was seen as a way to revive a slumping Co-op business following the economic recession after the bubble economy collapsed. It was seen as a vital part of Co-op's strategy to beat the competition by strengthening their perishable department. At this time, Co-op also took on a larger role as a consumer advocate group to establish stricter agricultural standards for food in accordance with revising the national Food Sanitation Law and the New Basic Law on Food Safety. Recognizing the importance of Sanchoku, in 1993, JCCU established the Committee for Sanchoku.

In 2002, false labeling, especially of meat, was a serious problem in Japan. This opened up a heated debate on the role and responsibilities Co-op and their producers and the safety of Sanchoku products. At this time, several producers were found to have labeled foreign meats as domestic products, concealing the country of origin. Some co-operatives were also found to have handled these meats and Co-ops came under sever criticism by consumers for this underhanded behavior.

In May of 2003, JCCU's decade long nationwide movement to revise the basic food laws in Japan came to fruition with the passing of official revisions to both basic food laws. This has meant that standards are now set across the board for producers, distributors and retailers alike. In a sense the bar has been raised for everyone. With many retailers now offering their own version of "Sanchoku" to consumers, competition has taken a toll on Sanchoku sales within Co-op. Sanchoku, the signature system of Co-op is now at the center of discussions within the co-operative community. In September 2003 CCIJ held a conference on Sanchoku and Food Safety and the JCCU's annual research conference in January of 2004 was devoted to discussing Sanchoku. The results of JCCU's 6th National Sanchoku Survey were published in February of this year.

Results of Survey show Sanchoku Losing Ground within Co-ops

Since 1988, JCCU has conducted a national survey to get a clearer picture of Sanchoku. The results of the 6th Survey on Sanchoku conducted in August 2003 were published by JCCU in the spring of this year. The survey consisted of three areas: the current status of Sanchoku in regional co-ops, an Internet survey of Co-op members views on Sanchoku and a survey of individual Sanchoku case studies.

A brief summary of the results follows. Overall, 88% of the regional Co-ops responded to the survey. The results clearly indicate that the percentage of perishable food now supplied to Co-ops through the Sanchoku system has significantly decreased in the past four years, which had also decreased from the previous four years. In

comparing the results of 2004 to 1998 and 1994 the downturn is clearly visible. The latest survey indicates that the 14% of perishable foods is supplied through Sanchoku. This is down significantly from 21% in 1998 and 26% in 1994. It also follows that all categories of perishable foods supplied through Sanchoku have significantly decreased since 1998. While agricultural produce has decreased from 39% to 28%, fish and seafood has decreased from 19% to 8% and meat has slipped from 37% to 28%.

The results of the survey further shows that 86% of Co-ops that completed the survey have some form of Sanchoku standards set in place. Furthermore, 90% of the Co-ops with standards, base their standards on the three basic principles outlined above.

Why Are Sanchoku Products Decreasing?

One of the main reasons for the decline is, with the passing of the new food laws, many products no longer meet the new rigorous and verifiable standards. Also, recent incidents of product mislabeling and undisclosed use of unauthorized pesticides breached members' confidence in the safety standards of Co-op products. Co-op is now struggling to restore consumers' confidence in Co-op and Sanchoku products after these incidents.

In particular, three main reasons for this precipitous decline have been identified as follows. First, the standards for perishable food have become more rigorous and many products that were previously classified as Sanchoku are no longer eligible under the new stricter standards in accordance with the revised Food Sanitation Law and New Basic Law on Food Safety. Second, new Co-op joint-business associations formed to improve management while unifying supply channels has allowed Sanchoku products to be mixed with non-Sanchoku produce from regular channels, therefore disqualifying the Sanchoku products to be classified as Sanchoku. Third, there is a big gap between Co-ops that are being proactive and doing risk analysis and those Co-ops, which are not. The survey shows that while large-scale regional Co-ops are more progressive, the mediums to small scale Co-ops show a poor performance in terms of risk analysis.

The Issues

There is a general agreement among scholars that there has been inertia and declining creativity in the Sanchoku system since 1992. Those who have followed Sanchoku since its inception say that when Sanchoku was first proposed, it was a very fresh approach to reestablish Co-op as the leader in food safety. The concept was innovative, but unfortunately the concept was not fully established around a firm business model. In the 1990s, Co-op began to put more emphasis on the business aspect of Sanchoku, but a full plan was never firmly established. There is a cloud of ambiguity hanging over Sanchoku with regard to developing fundamental policies on standardization, agriculture, internationalization and distribution which needs to be addressed in order to make the system work and make it marketable to consumers. . The following is an outline of these issues:

1) Standardization of Products

Ooki, Shigeru, in his article, *Issues with Standardizing Co-ops Direct Buying Routes from Producers* discusses the important issue of standardization. Among the three basic Sanchoku principles of trace ability, standardization and communication, he states that standardization is the most difficult principle to define and follow-up on, since standardization must include the important element of taste.

Standardization, he argues, involves the following four traits for each product: clarification, scientific proof, verifiable results and marketable products. Above all, in

the case of Co-op, Co-op must have a totally transparent system and remain honest with their members while continuing to creatively develop the Sanchoku system. While size shape and color of products are important in terms of appealing to people, it is the taste that is the defining element. In terms of produce, even if the standard of size, shape and color is determined in advance, the final product may not turn out as planned since in agriculture there is always outside factors that influences the final harvest. In order to follow through with standards, a process of quality control is necessary.

He also points out that without standards you cannot have a label, so the issue of producing something under the Sanchoku label is really an issue of standardization. Furthermore, he would argue that although there are basic standards set by the government, it is the standards set by private organizations that become the 'de facto standards' and although it is not the legal standard, it in effect becomes the criteria by which consumers choose products and thus becomes the official standard.

When standards are set, however, variety is necessarily eliminated. Any product that does not meet the standard exactly is not permitted on the market. This standard determines an organization's brand. Once you determine your brand you have the choice to ask other producers to follow the standards set by your brand, or an organization can make it obligatory that all suppliers for the organization produce to your standard.

It is important to remember that three things determine the quality of food: appearance, taste, and health or ethics of the product. Quality in the narrowest sense means size, shape and taste. Health means safety. And ethics deals with human rights as well as environmental preservation. Basic quality is largely determined by health and safety, which is determined by the producer. Beyond this however, the consumer decides what is quality by the appearance and taste of the food.

Environment and health concerns are now a very big concern. How to secure standards with regards to these two very basic elements is of utmost importance to Co-op. The process of production and distribution must be transparent from the producer to the consumers' table and quality control must be established, but the ethical issues such as use of child labor are very hard to control when it comes to standards.

In order to have standards for Sanchoku, Ooki suggests that there must be a system of certification that includes:

- 1) Standardization of the standards
- 2) Management system that judges the final product to make sure the product meets the standards
- 3) Train specialists to evaluate the quality of the produce
- 4) Design and follow through of a plan that includes a "do, check, act" cycle
- 5) A system of evaluation must be set in place, which includes both voluntary and outside evaluation.

Co-op has played an important role in establishing standards for perishables, but it is questionable whether each Co-op rigorously follows these standards. Co-op is now reexamining the relationship between Sanchoku and Co-op. The 6th Survey of Sanchoku shows that compared with four years ago, the number of incidents of BSE, food poisoning, mislabeling, use of non-registered pesticides on food and such incidents have increased, while still approximately only one half of Co-ops have really seriously examined their policies with regard to safety, regardless of the size of the Co-op. Even amongst the large-scale Co-ops, over 3 billion yen in total turnover, only 40% have examined their policies with regard to Sanchoku. In smaller scale Co-ops even less than 40% have examined their Sanchoku policy. The results of the survey further indicate that Co-ops have different interpretations of Sanchoku. Even when a Co-op

sets standards, they find it difficult to follow through with the standards, because each Co-op has made a firm decision on what course to take. In fact most have not decided on a definitive plan for Sanchoku.

2) The Agricultural Question: Regional Development vs. A Product Centered System

Co-op is also now facing the dilemma of the agricultural question with regard to Sanchoku. At present, there is a wide array of ways in which Co-ops acquire their products with most Co-ops using a combination of contracts with regional organizations such as agricultural co-ops, as well as, individual contracts, but with most Co-ops having no set policy in place. Discussions are now focused on what stance to take, as they have never clearly stated their position. The issues involve: (1) should Co-op represent purely the consumer's interest (2) should Co-op represent the interests of all residents in a region i.e. regional development or (3) should Co-op work to protect domestic agriculture? Co-op is now facing this decision and they are now considering their members' viewpoints as they see that consumers' views have changed on this issue over the past 20 years.

Co-op has two options: to develop a comprehensive regional agricultural Sanchoku policy or to develop a system that focuses on a product-by-product policy. Concentrating on developing a regional Sanchoku policy has the advantage of ensuring continuity with producers in one region and overtime reducing overall costs. A regional policy also promotes mutual benefits for other organizations such as agricultural and fishery co-ops, as well as other businesses in the area. The weakness with this system is that it lacks Co-op internal momentum from the quality control point of view for each item.

Developing product-by-product Sanchoku, on the other hand, puts the focus on the agricultural commodity. This type of policy focuses on establishing standards for each item, since each item is individually contracted. This system has the advantage of improving the quality of each specific product. It does not, however, take the position of becoming involved in regional agricultural development and regional business development, which is mutually beneficial to a region, especially if it is the region within which the Co-op operates. It should be noted that product-by-product contracts presuppose that the Co-op has the ability to manage the assortment of products and coordinate picking-up all the products.

Thus, Co-op has to make the decision whether they are going to focus on dealing with regions or individual producers or a combination of both. The reality of a regional system is that Co-op loses the ability to have a full choice of products, because most regions do not have the capability to produce either enough of a particular commodity, or sufficient variety of products to fulfill Co-op orders. Thus Co-op must combine both types. Co-op is dealing with a double-edged sword in terms of finding a balance. They must be careful not to sacrifice consumer interests over protection of domestic agriculture and regional development.

3) Internationalization and International Sanchoku

The second issue that Co-op is now addressing is internationalization. There are several issues here. The first question is what ratio to set regarding domestic vs. imported products and thus how much importance to place on supporting Japanese domestic food policies. Some Co-ops have tried to establish international Sanchoku, but they have come under criticism for ignoring local agriculture. The debate on this has been stopped short without any conclusion. Co-op does not have a clear policy about imports. While some Co-ops only import when domestic products are not in adequate supply, other Co-ops have introduced safety standards on imports. Imports are increasing nonetheless and foreign products are sometimes treated equally with-

out any explanation. Co-op is facing the dilemma of the fact that in many incidents overseas products can be imported with more consistency and at a cheaper price than domestically produced products.

4) Distribution

Another area of indecision is the tie-up between wholesalers and distributors. There is a need to establish a distribution theory with regard to Sanchoku. There is also a need for a large-scale discussion among all member Co-ops of JCCU to determine a standard Co-op theory and practice with regard to distribution. It is important to remember that the original intent of Sanchoku was to cut through all the middle people, make the distribution process more transparent, and reduce costs for consumers. Now, with Japanese consumers more aware of the lack of transparency in the food industry and distribution process, and the control that distributors wield within the food industry, Sanchoku, more than ever must live up to its original intent. . Co-op must remember that Sanchoku was created to address these concerns and to establish a more effective and responsive distribution system. To streamline distribution, some Co-ops have joined together in Regional Co-operative Associations and in theory everyone supports these organization, but in reality they are not serving the Co-operative community well.

It can be argued that Co-op has not taken a comprehensive view on the use of and place of wholesale markets and distributors in the Sanchoku system and have tended to use these sources when necessary. Co-op is now debating how to balance the use of large distributors and wholesale markets in terms of managing supply and demand and settling accounts. The reality of the situation is that most Co-ops cannot rely on Sanchoku alone and must continue to somewhat rely on wholesale markets for a variety of reasons including finance and supply. The perishable distribution system in Japan is now changing in response to fierce competition so it is very important for Co-op to make new policy decisions accordingly.

Co-op Facing the Turning Point with Sanchoku

Sanchoku is now facing a turning point and Co-op needs to decide on its direction and what action it will take in the future. In the views of Ooki, there are three important things that Co-op needs to face.

1) Increase member involvement through improved communication

In his view, in the past Co-op has taken too passive a view on the importance of developing member involvement. This is evident by decreasing member involvement. Furthermore, the process for member involvement should be consistent and the method of how to market members' activities needs to be reviewed. Members have been taken for granted. The concept that members on the whole are wise consumers has not been fully considered in the equation. In terms of Sanchoku, there is a need for more interaction by members in the process, and their input needs to be valued in the food chain.

It is not always easy to communicate the 3 principles of Sanchoku to members. Many Co-ops, in their explanation of Sanchoku are too long-winded and lose consumer's interest when the concept is too convoluted and difficult to grasp. If consumers have a hard time understanding the concept, the purpose of Sanchoku is defeated. Co-ops also now need to recognize that the principles have unique traits specific to any one region. Distinct regional differences need to be incorporated into the principles so that members feel that the system is grass root in nature.

2) Developing a System: Merchandise Development and Pricing

The current nature of Sanchoku is based on rather ad hoc ordering and the quantities vary. In fact, according to the survey, 70% of Co-ops don't have definite overall plans that they follow regarding Sanchoku and only 40% of store have definite contracts for firm amounts, while 60% of non-store operations have set contracts.

Furthermore, the risk factor on the producers and the burden to farmers needs to be taken into consideration when developing merchandise policies and setting prices. The risk factors in farming due to weather for example must be considered. There can be shortages as well as surpluses and farmers are forced to either try or get produce from other farmers to meet contracts, or sell excess produce when Co-op's market is saturated.

There is a problem with the ad hoc nature of the contracts and inconsistencies, which tends to be harmful on both the buyers' and producers' sides. The only way to avoid inconsistencies in orders and avoid safety issues is to contract all produce from farmers and not use wholesalers and other distributors. Basically, Co-op is reluctant to assume the farmers' risks, and does not rely on Sanchoku alone, instead preferring to fill orders through local wholesalers. Many Co-ops also simply leave the orders up to the agricultural co-operatives, which while nullifying many of the attributes of direct buying, reduces the risk to the Co-op. Co-op Sanchoku has a history of relying on outside agencies such as agricultural co-ops and wholesalers and thus has left the system wide open to discrepancies in product and product quality and safety.

So in effect, Sanchoku is not direct because it relies on outside middlemen and organizations to fill in gaps in distribution and it is therefore not a direct system of buying for the consumer. In general only two thirds of Co-ops have some direct contracts with producers. So it is debatable if Sanchoku has not become a misnomer at Co-op. The question remains if this misnomer can be redeemed in the eyes of Co-op members.

Determination of price for Sanchoku products is another one of the major difficulties cited by Co-ops. Prices are negotiated between the producers, and the Co-ops. In most cases the prices paid are based on the wholesale market prices at the time of delivery, with allowances made for quality variation. Some would argue that Sanchoku is a movement, not just a part of the Co-ops' commercial operations and as such, price negotiations with producers are not based entirely on commercial considerations, but form a part of some Co-ops aim to support Japanese agriculture. If Co-op chooses to support domestic agriculture, price policies for Sanchoku need to reflect this stance while still remaining competitive in the market. This is the dilemma.

Co-op Sanchoku at the Crossroads

Discussions are now ongoing about the crossroad that Co-op faces with regard to what direction Sanchoku will take in the future. The problems presented here pose future challenges for Co-op. One of the major challenges is how to distinguish Co-op Sanchoku from their competitor's produce which if offered under a system similar to Sanchoku. . Although Co-op originally conceived the Sanchoku concept, many major food retailers now offer their own version of "store brand Sanchoku" thus Co-op no longer enjoys the advantageous position it once had. Going up against the competition's strong marketing and advertising campaigns is now a top priority. In view of the new situation, Co-op is now faced with the dilemma of developing a Co-op Sanchoku Label and a system. Co-op has identified Sanchoku as one of the keys to their continued growth and ability to compete against the other supermarket companies. The question is now how to further develop this key component of Co-op.

Conference on CSR and Co-operative Response

CCIJ's annual research conference on September 18th attracted more than 130 participants. This year's theme focused on Co-operative Response to Corporate Social Responsibility (CSR). In view of the wide spread concerns on corporate malpractices, discussions on CSR have been in the limelight and a number of standards and codes of conducts have been proposed by both international and national organizations, and corporate bodies. Co-operatives has been active in promoting environment-friendly and ethical trading in many fields, but needs to develop effective assessment and reporting systems. Prof. Taniguchi made the keynote address to outline the latest development in CSR. Prof. Mizuguchi of Gunma Economic College presented a critical view on the "CSR boom." Mr. Ueyama of Aeon Corporation outlined the best practices of the biggest retail groups in Japan, while Ms. Wada of the Housewives Association assessed the food industries from the consumers' viewpoint. The second part of the conference was dedicated to co-operative practices and the four best examples with Co-op were presented. The Comprehensive Co-operative Assessment award was given to Co-op Kobe, the Management Quality Award to Fukui Co-op, Product Assessment went to the Metropolitan Co-op Federation and the Compliance-based Management award was given to Saitama Co-op. Prof. Tsuda of St. Andrew University chaired this session.

Study Team Visits Canada to Learn About Family Support Systems

CCIJ organized a study group on how to support young families, and how to involve fathers in child rearing. This group, headed by Ms. Sumi Fukukawa, a professor of Komazawa Women's College, conducted a study tour to Canada this September. Seven members visited various organizations and facilities such as a Family Resource Center, Ontario First Duties, East York, East Toronto, Grey County Early Years, and the Ottawa Health Center, among others. They had the opportunity to listen to a lecture about social entrepreneur and women's work by Tom Gigi, a well-known consultant on community development and community recourses. Although Canada's social structure is much different from Japan's, they learned a great deal about basic cultural mindset about children and child rearing. The group will publish a report in May.

Study Team Visits European Social Enterprises

CCIJ, in early September, sent a study team to learn about the institutional framework of social enterprises in some European countries. CCIJ is studying the legal/institutional framework of co-operatives and the support structure for co-operatives' social enterprises. The group, which has been collecting information through websites, books and interviews, decided to directly collect information from organizations that supports the social enterprises in Europe. The study team is composed of Prof. Hideaki Seki, Aoyama Gakuin University, Prof. Iwakazu Takahashi, Meiji University and Mr. Akira Kurimoto, Director & Chief Researcher of CCIJ. They visited Social Enterprise London and Greenwich CDA in the UK, CGM and Sol. Co. Brescia in Italy. It also had a chance to take part in the International Co-operative Forum held in Münster, Germany.

Another study team visited the UK to make an in-depth study on the partnership between government in each level and social enterprises. This visit was part of a five-year research project, organized by the Management Research Centre of Meiji University. This project is subsidized by the research funds of The Ministry of Education and Technology. The study team is composed of approximately 13 academics and practitioners including the leaders of nonprofit organizations, and the public and co-operative sectors, which are headed by Prof. Ichiro Tsukamoto, professor of Meiji University. It visited a few intermediary bodies within the voluntary sector and local governments tackling social exclusion and regenerating communities.

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