

## A Study on Improvement of Wholesale Distribution for Imported Fruits since FTA

Yang, Dong Sun\* · Byun, Dong Heon\*\*

### < Abstract >

This study focuses on illuminating present distribution status of rapidly increased imported fruits after Korea-Chile FTA in 2003, for it can be streamlined by some policies as we suggest, that being said that it falls on somehow efficient trades among wholesalers via various distribution channels.

Confining those channels to their nature in business practices, we find they appear to be most commonly categorized to 2 paths for each 2 big individual transactions as follows : 1. the classic one between importers and wholesalers 2. the derivative one between wholesalers and big retailers.

The commission merchants, intermediary position in those channels, seem to satisfy roughly 70% of their demand directly from importers and the rest throughout wholesale auction markets. In the meantime, we find that 30% cut out of 49% supply, ratio to their entire distribution hands, is sold to conventional markets or retailers without formal business process. This sort of distribution practices, having analyzed by this study, turn out to work as economic distortion throughout markets for imported fruits.(Estimated tax omission of 4.0-5.8 million dollars annually)

Throughout broad and deep analysis, we suggest some improvement plans as follows, 1) rearrangement of importers by administrating their rights and qualifications for import, 2) reinforcement of distribution laws to police participants in that field 3) fair unloading rate such as charge per pallet, 4) building up and sharing market information system between government and wholesale market operators.

These suggestions could facilitate stake-holders in foreign fruits distribution industry in South Korea to be more committed to better and clearer transactions in business, and furthermore, will be likely to establish a desirable business practice for proper tax return, thereby legalizing the shadow economy.

Key word : imported fruits, distribution improvement, tax omission, shadow economy

\* First author, Professor, Korea Agro-Fisheries&Food Trade Corporation (yds1985@at.or.kr)

\*\* Corresponding author, Head of Marketing Research Institute, Korea Agro-Fisherie & Food Trade Corporation (willemdbh@gmail.com)

## FTA 이후 수입 농산물의 도매유통 실태에 관한 연구

### - 주요 수입 과일류의 유통을 중심으로 -

양 동 선\* · 변 동 헌\*\*

#### < 국문초록 >

본 연구는 자유무역협정(FTA) 이래 수입산 과일류가 국내의 다양한 유통채널을 통해 거래가 이뤄지고 있음에 따라, 유통채널 내에서 상대적으로 거래비중이 크고 유통의 효율화를 도모할 수 있는 도매시장을 거치는 수입과일에 대한 유통실태를 밝히고자 하는 연구이다.

수입과일에 대한 유통채널에서 수입업체-도매시장(대형유통업체)-소매업체로 이어지는 전형적인 구조를 띠고 있으며, 유통과정에서는 도매시장과 대형유통업체가 양대 축을 형성하고 있는 것으로 나타났다.

중도매인의 유통 형태를 보면, 수입업체로부터 70%를 직거래하고 30%는 도매시장 경매를 거쳐 유통하고 있는데, 중도매인이 유통채널 상에서 취급하는 전체 물량 중 30%가 재래시장과 소매점을 중심으로 비정상적인 형태로 유통되어 시장질서를 왜곡하는 것으로 분석되었다.

도매유통의 문제점으로 1)수입업체의 양극화에 따른 독과점 현상 및 과당 경쟁 발생, 2)하역비에 대한 차별적 부과, 3) 도매시장 운영자의 비정상적인 거래 관행에 따른 비효율적인 유통, 4) 중도매인 등에 의한 불투명한 거래와 그에따른 세금 누락으로 파악되었다.

수입과일의 도매유통의 개선점으로는 1)과일 수입업 영업요건의 재정비, 2)도매시장내 합리적인 하역비 부과 적용, 3) 도매시장에서 수입과일의 효율적인 유통이 확보될수 있는 거래방법의 다양화, 4) 유관기관간 유기적인 유통정보시스템 구축 등을 제시할 수 있다.

이를 통해서 수입과일의 거래 전과정에서 투명성이 확보되고, 나아가 지하경제의 양성화를 통한 세수 확보도 가능하다고 하겠다.

주제어 : 자유무역협정, 수입과일, 도매유통, 유통개선, 세수 확보

\* 주저자, 한국농수산식품유통공사 유통연구소 교수(yds1985@at.or.kr)

\*\* 교신저자, 한국농수산식품유통공사 유통연구소 소장(willemdhb@gmail.com)

## I . Introduction

The trend of fruits import has been increased consistently since Korea-Chile FTA in 2003, which recorded 4.3 percent of annual increase from 446 thousands tons in 2003 to 682 thousands tons in 2013, that is, 12.5 percent of annual increase from 286 million dollars to 929 million dollars. These expansion of import seriously affected new distribution system such as supply-demand relation of domestic agricultural production.

The tariffs lowering by FTA was initially estimated to affect a welfare of consumer by price cutting of imported fruits, however, it is pointed out that the imported fruits have shrunk domestic market and become a main factor of price drops of domestic fruits(Lee ByungHun et al., 2013).

Why should the imported fruits soar? It is necessary to discuss about their importing patterns such as items, price and importing season etc, compared to the early domestic market opening. This is due to a reasonable estimate basis on competitive situation against domestic produce(Lee YongSeon et al., 2008).

In addition, some issues related to illicit transaction in imported fruits are raised, such as underdeclaration or undeclaration in customs procedure and violation of origin indication in distribution step. There are still the aspects to confuse decision making of producers, consumers and government, because of lack of study on import status and domestic distribution condition about imported fruits.

In this context, it is important to identify specifically on what kind of fruits are imported in what way and by what channels they are distributed. And such study needs to understand overall distribution system for imported agricultural produce, furthermore it would be helpful to figure out source of distribution problem, and to set up some measures for efficient distribution.

This study is limited in wholesale distribution system of imported fruits, however, retail field is touched on a few aspects by previous study and interview survey. The analysed items are imported fresh fruits, of which volume and amount are top eight such as orange, pineapple, grape, banana, kiwi, lemon, grape fruit, cherries.

A sampling survey was conducted for importers and wholesale market corporations such as GARAK, GANGSEO and GURI market in capital area, besides, auction dealers and commission merchants in wholesale market are also surveyed by interview. And import data of Korea Customs Service was used.

## II. Theoretical Background

Lee YongSeon et al. (2008) summarized up the characteristics and distribution of imported fruits and vegetables as follows. First, those prices become higher than the early market opening, and items with high unit costs mainly increased and get diversified. Second, most import firms are still small, however, some are very big sized, which become a cause to distribute inefficiently. Third, those distribution channels form the way of importers-wholesale markets(or big retailers)-retailers, the 30-40% of which are distributed through wholesale markets. Fourth, large retailers purchase one third of their volume from importers, and import directly the 20% of them.

Park JaeHong et al. (2012) asserted that since Korea-US FTA in 2012, domestic price of Cherry in addition imported price went down with sharp increased imports from US. The importers mainly supply to public wholesale markets and large retailers, and tend to prefer a listed auction in wholesale market in order to prompt paying settlement.

Lee ByungHun et al. (2013) asserted that the wholesale market corporations took a sale on consignment for importers, most of which were done by method of fixed price dealing or negotiated dealing. They pointed out that some institutional restrictions towards importers were to be introduced because most importers pursued a short term margin only instead of fair distribution to markets. Furthermore they assisted that public institution had to provide the accurate information about overseas trend etc. And they criticized that the wholesale corporations were mainly interested in paying settlement between importers and commission merchants, instead of neglecting their collecting role of produce.

Such studies show that ratio of imported fruits by importers and big retailers is estimated about 70% and 30% each, and direct imports by big retailers gradually increase.

And wholesale corporations mainly conduct sales on consignment through direct dealing with importers, that is, fixed price dealing and negotiated dealing, whereas, sometimes auction dealing by importers' request.

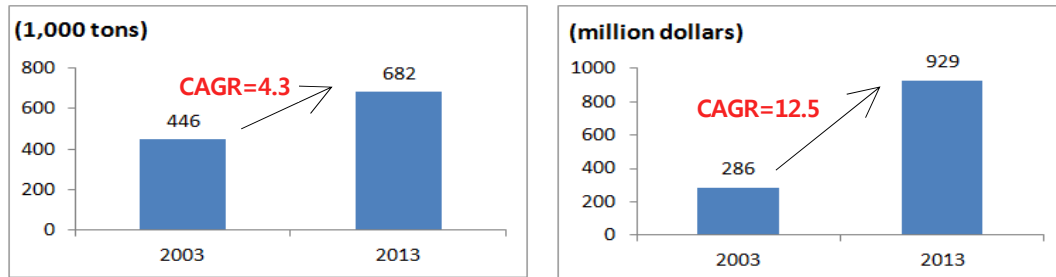
## III. General Status on Imported Fruits

### 1. General Status

The fruits import has been increased consistently since Korea-Chile FTA, which recorded 4.3 percent of annual increase from 446 thousands tons in 2003 to 682 thousands tons in

2013, that is, 12.5 percent of annual increase from 286 million dollars to 929 million dollars.

<Figure 1> Trend of Imported Fruits



\*Source : Korea Customs Service

While the market share of main imported fruits like banana, orange, pineapple decreased by 10.8%p from 90.4% in 2003 to 79.6% in 2013, the others like grapes and cherry increased, which means the imported fruits were diversified (Table 1).

<Table 1> Volume of Imported Fruits

	2003		2013		Change of Ratio (%p)	CAGR (03~13)
	Import (1,000 tons)	ratio	Import (1,000 tons)	ratio		
Banana	221	49.6%	314	46.0%	-3.5%	3.6%
Orange	145	32.5%	153	22.4%	-10.1%	0.5%
Pineapple	37	8.3%	76	11.1%	2.8%	7.5%
Grapes	15	3.4%	63	9.2%	5.9%	15.4%
Kiwi	13	2.9%	20	2.9%	0.0%	4.4%
Others	15	3.4%	56	8.2%	4.8%	14.1%
Total	446	100.0%	682	100.0%	0.0%	4.3%

\*Source : Korea Customs Service

Although banana, the top imported item, recorded 10.8% of annual increase from 91 million dollars in 2003 to 253 million dollars in 2013, the market share decreased by 4.6%p from 31.8% to 27.2% during same period (Table 2).

The market share of big three items like banana, orange and grapes decreased 10.2%p from 78.7% in 2003 to 68.5% in 2013.

&lt;Table 2&gt; Amount of Imported Fruits

	2003		2013		Change of Ratio (%)	CAGR (03~13)
	Import (million dollars)	ratio	Import (million dollars)	ratio		
Banana	91	31.8%	253	27.2%	-4.6%	10.8%
Orange	113	39.5%	195	21.0%	-18.5%	5.6%
Grapes	21	7.3%	188	20.2%	12.9%	24.5%
Cherry	4	1.4%	90	9.7%	8.3%	36.5%
Pineapple	17	5.9%	61	6.6%	0.6%	13.6%
Others	40	14.0%	142	15.3%	1.3%	13.5%
Total	286	100.0%	929	100.0%	0.0%	12.5%

\*Source : Korea Customs Service

## 2. Trade from FTA Nations

The trade from FTA country with Korea has sharply increased since last 10 years, which increased by 3.4 times from 256 million dollars in 2003 to 862 million dollars in 2013. The market share of FTA country showed average 92~95% during 2003~2013 by volume base, meanwhile, from 84% in 2003 to 93% in 2013 by amount base. This means that fruits have mainly imported from FTA country.

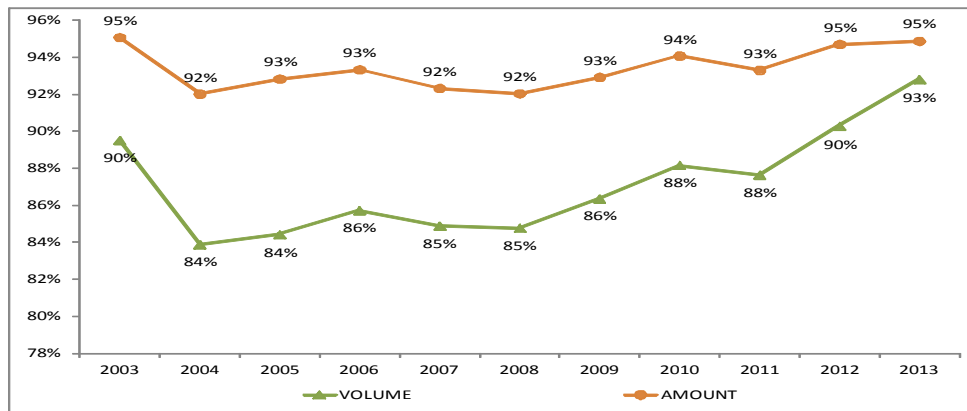
It has been expected that price of imported fruits would be down continuously because of tariff reduction by FTA, however, on the contrary, the import price has increased during lately 10 years. Actually the price increased by 2.3 times during 10 years from average 0.6 dollar per kilogram in 2003 to 1.4 dollars in 2013, because the exporting nations generate international demand by another FTA.

&lt;Table 3&gt; Import from FTA Nations

		' 03(A)	' 08(B)	' 13(C)	C/A	CAGR(03~13)
Import (Million dollars)	Total	286	525	929	3.2	12.5%
	FTA nations	256	445	862	3.4	12.9%
Import (1,000 tons)	Total	446	527	682	1.5	4.3%
	FTA nations	424	485	647	1.5	4.3%

\*Source : Korea Customs Service

&lt;Figure 2&gt; Market Share of FTA Nations



\*Source : Korea Customs Service

## IV. Wholesale Distribution of Imported Fruits

### 1. General Status on Wholesale Distribution

#### 1.1. General Status

The transaction of imported fruits in wholesale markets increased by 10% annually in volume and 13.3% in amount during 2009-2012. As we can see in table 4, their share of wholesale market from total volume decreased from 45.3% in 2009 to 36.3% in 2012, however the role of wholesale market is regarded as still important, because its share in total distribution process occupies above one third and the key point to distribute to various market participants like big retailers and big consumers.

&lt;Table 4&gt; Distribution Status in Wholesale Markets(2009-2012)

	2009	2010	2011	2012
Amount (billion won)	404	462	450	588
Volume (ten tons)	206	256	246	274
Market Share (%, volume)	45.3	42.1	35.8	36.3

#### 1.2. Characteristics of Wholesale Distribution

The types of wholesale distribution of imported fruits show variously according to price, dealing method and distribution entity. It is well known that banana and orange are affected on price, grape on capital, and some fruits are affected on dealing method like auction or negotiated dealing method etc.

We conducted a survey on distribution channels, those characteristics and improvement alternatives etc, the samples of which were importers and wholesale corporations etc<sup>1)</sup>

The survey results are as follows. Major importers and big wholesale corporations dealt most of imported fruits, on the contrary, small importers dealt 3-5 items like popular fruits. The average inventory holding period showed that above 90% was below one month, which means that imported fruits are distributed promptly without inventory burden. The critical determinants at the stage of import were those import prices(28%), domestic consuming patterns(22%), domestic production decrease(22%) and domestic price rising(17%) etc.(Table 5, Figure 3)

## 2. Channel on Wholesale Distribution

Most of fruits are imported by specialized importers and a few of big retailers, and those distributing channels are generally divided by two paths. First, importers supply to wholesale market, commission merchants and big retailers, subsequently supplies passed through wholesale market are distributed to traditional retailers, big retailers and big consumers. But some patterns show that a few of fruits specialized wholesalers are also supplied directly from importers.

In details, the importers, 70% ratio of total imports, supply to wholesale merchants(35%), wholesale corporations(14%) and big retailers(21%). And the wholesale merchants, their entire ratio 49%, supply to traditional markets(15%), fruits retailers(15%), big consumers like catering&food service(15%) and big retailers(4%).

The important point here is that wholesale merchants' 30% cut out of 49% supply is supplied to conventional market retailers without formal business process. Meanwhile, the big retailers, 55% ratio of distribution hands, are supplied from direct imports(30%), other importers(21%) and commission merchants(4%). This case are known as clear transaction process from import to final supply.(Figure 4)

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1) We conducted interview survey for 4 importers, 3 wholesale corporations, 1 auction dealer and 4 wholesale market operators on June 2014.

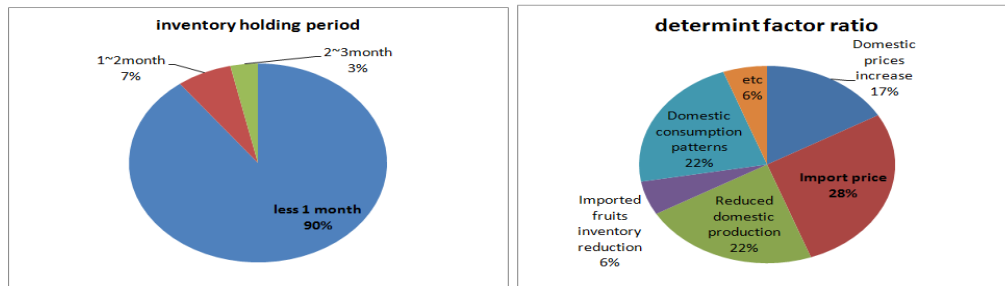


<Table 5> Distribution Characteristics by Item

Item	Characteristics
Banana	<ul style="list-style-type: none"> <li>-Monopolized by some multinational companies</li> <li>-transaction between importers and commission merchant</li> <li>-A weak role of wholesale corporation</li> <li>-Mostly negotiated dealing method, and partially auction method</li> </ul>
Orange	<ul style="list-style-type: none"> <li>-Major importers, and besides many small importers</li> <li>-A comparably strong role of wholesale corporation</li> <li>-Mostly negotiated dealing method, and partially auction method</li> </ul>
Grapes	<ul style="list-style-type: none"> <li>-A comparably strong role of wholesale corporation</li> <li>-Mostly negotiated dealing method, and partially auction method</li> </ul>

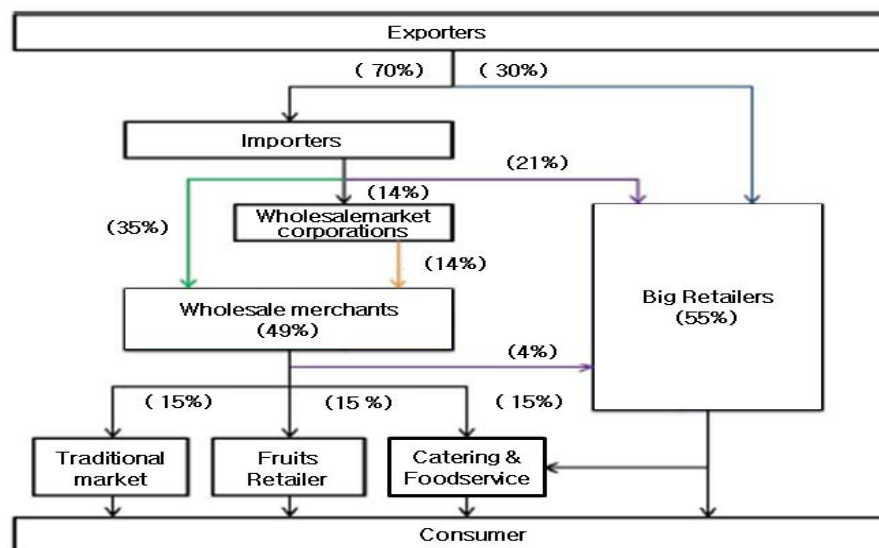
\*Source: Survey Results for Participants of Imported Fruits(2014.6)

<Figure 3> Determinants Considered for Fruits Import



\*Source : Survey Results for Participants of Imported Fruits(2014.6)

<Figure 4> Distribution Channel of Imported Fruits



\* ( ) is a portion in each step

### 3. Problems in Wholesale Distribution

#### 3.1. Monopoly and Excessive Competition by a Few of Importers

The fruits importers are classified into majors and small firms, which are different from their volume, stable supply and infrastructure. While a few of majors only can supply stably, most of small firms tend to pursue short term margin only, and then the market is fairly unstable. It is said that the business duration of importers was average two years, and 12.4% only continued the business above five years.(Table 6)

<Table 6> Comparison of Fruits Importers

	Majors	Small Firms
Scale	-Multinational firms *Dole, Del Monte etc *one or two in domestic firms -Annual sale 150 billion won or less	-Most importers -Generally small sale -Excessive competition
Stable supply	-Relatively high	-Relatively low
Infrastructure	-Private shipping & warehouse arounde harbor -Supply initiatives	-Supply from majors -Rental of logistic facilities
Key Features	- Quality safety and stable volume	-Short term margin

\*Source : Survey on distribution of imported fruits(2014.6)

#### 3.2. Inefficient Distribution by Abnormal Role of Wholesale Corporations and Commission Merchants

It is well known that the wholesale corporations pay no attention to collect produce, and instead focus on payment between importers and commission merchants, which results in lowering the competitiveness of wholesale market. It was a practice that the wholesale corporations, official consignees of wholesale market, should have distributed the imported produce to commission merchants by collecting function, however, they was able to earn easy profit by auction fee from commission merchants. And it is widely known that commission merchants also encourage tax omission by illegal offside dealings. As mentioned above, we expect that clear transaction of wholesale corporations and commission merchants will result in normal distribution process by importers and retailers.

#### 3.3. Some Unclear Transaction Process and Unfair Tax Return

It is said that some imported fruits can be abnormally distributed under overall transaction process. Some small importers and commission merchants sometimes omit the dealing documents, which would arouse doubt related to tax omission. Meanwhile domestic produce distribute clearly from farm to table, the prices of imported fruits are not clearly exposed under dealing process, which is pointed out resulting in distorting normal market mechanism.

<Table 7> Estimated Unclear Transaction

	Annual Total Import (A)	Commission Merchant & Intermediary Handling		Unclear Transaction	
		Total (B)	Share of Conventional Market/Retailer (C)	Amount (D)	Margin (E)
Ratio	100%	49% of A	30% of A	50~70% of C	15% of D
Amount (\$ million)	929	455	278	139~194	21~29

\*D and E is based on interview survey for wholesale market participants(2014. 6)

As we see in Table 2 and Figure 6, considering commission merchant and intermediary handle 49%(455 million dollars) of total imported amount(929 million dollars), and the 30%(278 million dollars) is distributed under conventional markets or retailers, it is estimated that unclear transaction will be about total of 139~194 million dollars and margin of 21~29 million dollars and corporate tax omission of 4.0~5.8 million dollars. These results are summarized in table 7.

#### 3.4. Discriminative and Unreasonable Imposition of Unloading Charge inside Wholesale market

An unloading charge system, which is different from domestic dealers, is applied to importers inside wholesale market. The importers tend to pay around double each unit, because importers are highly imposed by box unit instead of pallet, even in case of unloading of pallet unit. This may result in increasing logistics cost of imported fruits, consequently distorting those price mechanism.

#### 3.5. Economic loss caused by Standardized Quarantine

All imported fruits are compulsory to quarantine in stage of customs clearance. Because a large amount of produce are to be put into quarantine uniformly, quality deterioration and economic loss are inevitably incurred. Especially some items like grapes may be discarded due to quality decline.

## V. Improvement Plans in Wholesale Distribution

We could suggest some plans to improve wholesale distribution of imported fruits and strengthen the competitiveness of agricultural industry.

First, it needs to rearrange the importers through strengthening of their business requisites. This could prevent them from excessive competition in aspect of import and domestic distribution, and could improve overall industrial environment related to imported fruits. The importers, who are exposed due to tax omission and unfair dealing, have to be kicked out from the business.

Second, it needs to reinforce a wholesale market mechanism for imported fruits to be normally distributed under all transaction process. Both fixed price dealing system and negotiated dealing system are to be adapted to all imported fruits, and furthermore a market wholesaler system also has to be considered to all wholesale markets. These could result in fair tax return report and consequently clear dealing business in the industry.

Third, it needs to improve the unloading charge system inside wholesale markets, which has to be adapted equally to all produce by pallet basis. As a result, this could improve logistics system of wholesale markets, and furthermore straighten the price decision mechanism.

Fourth, it needs to make the imported fruits transact clearly in all distribution process. In order to accomplish this goal, it has to build up comprehensive market information system from customs service office and national tax service office to wholesale market operators. Consequently, this could induce a clear dealing of imported fruits from ports to consumers, and furthermore result in proper tax return through legalization of shadow economy.

Fifth, it needs to introduce a differential quarantine system by each item, which could improve those quality and minimize economic loss.

## VI. Conclusion

The trend of imported fruits has been consistently increased since Korea-Chile FTA in 2003, which recorded 4.3 percent of annual increase as 68 ten thousands tons in 2013, and recorded 12.5 percent of annual increase as 929 million dollars.

This fact has brought international trust through the faithful execution of FTA, and widened an opportunity of consumers' choice. However, it has been often pointed out that the imported fruits shrunk domestic market.

We analysed on the general status about distribution channel of imported fruits and improvement plans for those efficient wholesale distribution.

The main problems on wholesale distribution of imported fruits showed 1) monopoly and excessive competition caused by a few of importers, 2) inefficient distribution due to abnormal role of wholesale corporations and commission merchants, 3) unclear dealing process by wholesale market participants like commission merchants and doubt of their tax omission, 4) discriminative and unreasonable imposition in unloading charges inside wholesale markets,

We could suggest some improvement plans as follows ; 1) rearrangement of importers by administrating their rights and qualifications for import, 2) reinforcement of wholesale markets mechanism and laws for imported fruits to be efficiently distributed, 3) improvement of unloading charge system such as imposition by pallet unit, 4) building up and sharing of comprehensive market information system from customs service office and national tax service office to wholesale market operators.

These suggestions can facilitate stake-holders in imported fruits industry in South Korea to be more committed to better and clearer transactions in business, and furthermore, will be likely to establish a desirable business practice for proper tax return, thereby legalizing the shadow economy in that field.

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