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RESTRUCTURING OF THE SLOVENIAN FOOD INDUSTRY IN THE PRE - AND POST EU-ACCESSION PERIOD

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ABSTRACT

The main objective of this article is to present an overview of the Slovenian food industry economic development in the period before the Slovenian EU accession and the first five years of the EU membership. The accession to the EU was certainly the most comprehensive change of economic environment since the state gained its independence. Nevertheless, already during the pre-accession period the changes intensified restructuring processes and increased pressures to the business performance of the sector. The agro-food industrial complex, however, is among the sectors of the acceding economies for which EU enlargement traditionally brings the most radical changes. Price level and cost differences, hardly comparable production structures, but mostly disparities in types and comprehension of the economic policies required large adjustments and caused notable economic pressures. Based on a framework of economic indicators the paper tries to answer some of the most recurrent questions related to the restructuring process of Slovenian food industry in the last decade. First we present past sectoral business performance using the appropriate mezzo-economic accountancy indicators, whereas in the central part of the paper four key restructuring determinants are analysed and commented. The determinants are formulated into the four relevant questions dealing with cost-price developments, relations in the Slovenian agro-food chain, developments of the international trade and trends in the budgetary transfers to support competitiveness. Results confirm that the economic restructuring which had been hindered in the Slovenian food industry during the last decade has been triggered radically after EU accession. This brought to the termination of favourable economic conditions in the highly protected domestic market and deteriorated radically the business performance, and only those food companies which will restructure proactively will sustain in the EU markets.

Key words: EU accession, restructuring; Slovenia; food processing industry

1. INTRODUCTION

Accession to the European Union has triggered substantial changes in the business environment of Slovenian food processing industry which intensified restructuring processes and increased pressures to the business performance of the sector. The agro-food industrial complex is among the sectors for which EU enlargements traditionally brought radical changes in the economic environment (Tangermann and Josling, 1994). Price level and cost differences, hardly comparable production structures, but mostly disparities in types and comprehension of the agriculture policies required large adjustments and caused notable economic pressures (El-Agraa, 1994).

The largest European Union (EU) enlargement in May 2004 involved ten countries, most of which just completed their transition to market economy, and another two countries with similar attributes – Bulgaria and Romania – joined the Union in 2007. The enlargement of 2004 differs from the previous ones in terms of the number of acceding countries and even more importantly in terms of the average level of economic development of the new Member States. The margin in economic prosperity is notably larger compared to any previous enlargement. These disparities bring both distinct challenges and opportunities for the new member states and for the incumbent countries of the Union (Artis et al, 2006).

However, neither the scale of the last EU enlargement nor the combination of the patterns and characteristics of agriculture, food processing, and rural economies are comparable with the past enlargements (Macours and Swinnen, 1997; Herok and Lotze, 2000). Therefore, the evaluation of EU enlargement and its implications for the agro-food sectors has drawn considerable research attention.

There are several studies evaluating in a rather detailed manner the EU accession effects for the sectors of Slovenian agriculture (Erjavec et al., 1997; Bojnec and Münch, 2001; Majcen

and Buehrer, 2001; Frohberg et al., 2002; Kavčič and Erjavec, 2003). Slovenian food industry has also been investigated; however focused studies are few (e.g. FAO, 1998; Erjavec and Kuhar, 2000, OECD, 2001; Kuhar 2003).

The main objective of this article is to prepare an overview of the Slovenian food industry development in the period before the Slovenian EU accession and the first years after the accession. Based on a framework of economic indicators paper tries to answer some of the most recurrent questions related to development of Slovenian food industry in the last decade. Four questions were put under the research scrutiny:

- Is food industry facing cost - price squeeze?
- Who is creaming in the food chain?
- Are the trends in international trade with food surprising?
- Has the budgetary support to the sector stimulated competitiveness?

The paper is structured accordingly to the elaborated four questions. Using data acquired from different sources (Statistical office, Ministry of finance, Agricultural institute of Slovenia) a series of economic indicators is calculated to elucidate the determinants of Slovenian food manufacturing sector development.

In the first part of the paper the situation in the sector is presented using indicators of business performance, efficiency and profitability whereas in the central part, the article tries to answer the elaborated questions and comment competitiveness determinants.

It is very much clear that the competitiveness is an important element of discussions and activities at different levels of the economic and policy environment, however it is also evident, that there is no consensus what exactly competitiveness is and what its most important determinants are (Martin, 2003). In the literature, different definitions of competitiveness exist. The definition of the OECD (1996) states it as the ability of companies, industries, regions, nations, and supranational regions to generate, while being and remaining exposed to international competition, relatively high factor income and factor employment levels on a sustainable basis. The definition used by the EU Commission (2003) states that it is the ability of an economy to provide its population with high and rising standards of living and a high level of employment for all those willing to work, on a sustainable basis.

There is no generally accepted theoretical framework economic literature, for sectoral competitiveness; similarly there is no consolidated terminological definition. The concept of competitiveness is clearly multidimensional and therefore it is difficult to deal with theoretically as well as empirically. In other words, competitiveness is a construct comprising different aspects of economic activity. Some of the leading authors (e.g. Martin et al, 1991; Trail and da Silva, 1996; Porter, 1998; Lall, 2001) therefore suggest a composite approach specifically designed according to the focus of analysis. Also the approaches to the analysis of competitiveness are broken down into two main groups (i) analyses of competitive performance and (ii) analyses of competitive potential. The first group measures profitability, growth, market share, trade, etc.; the second group is concerned with explaining why performance is good or bad. The techniques also differ with the level of the analysis; techniques appropriate for measuring the competitiveness of individual firms or of the national economy are not necessarily valid for measuring the competitiveness of a sector. In a strict sense, there is no specific research methodology applied in this paper, however economic indicators are computed according to the theoretical requirements.

2. ECONOMIC PERFORMANCE

In Slovenia the Food, beverages and tobacco manufacturing sector represented 1,46% of value added in GDP in 2010 and 1,65 % in the total employment (SORS, 2012). According to the value added contribution in total manufacturing food industry is the third largest sector in Slovenia. However, in the last years the importance of food industry is declining in all

macroeconomic indicators, since in the year 1998 the food industry contributed about 2,8% of Slovenian GDP and almost 2,5% of total employment (Figure 1).

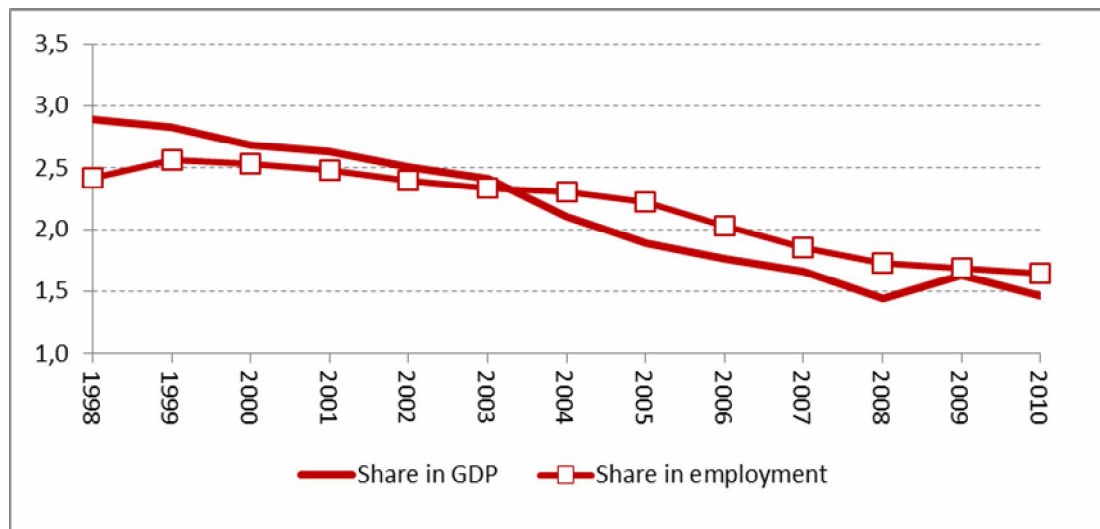


Figure 1. Slovenian food industry contribution to the national GDP and total employment in the period between 1995 – 2007. (SORS, 2012)

Industrial production of food manufacturing has mainly decreasing after the year 2000 (Figure 2). Until the year 2003 the production volume somehow stagnated, but in 2004 volume dropped for more than 10 % and than remained stable until 2007 when another shrinkage of the sector appeared and in the year 2011 the food manufacturing was at about 10% below the level of 2004 and beverage sector at about 15% lower. The index of production for total processing industry showed diverse trends, since in the period between 2000 and 2008 the volume increased by 35%, however in the year 2009 the volume dropped by almost 20%. The industrial production volume in the year 2011 was at about 5% higher than in 2004.

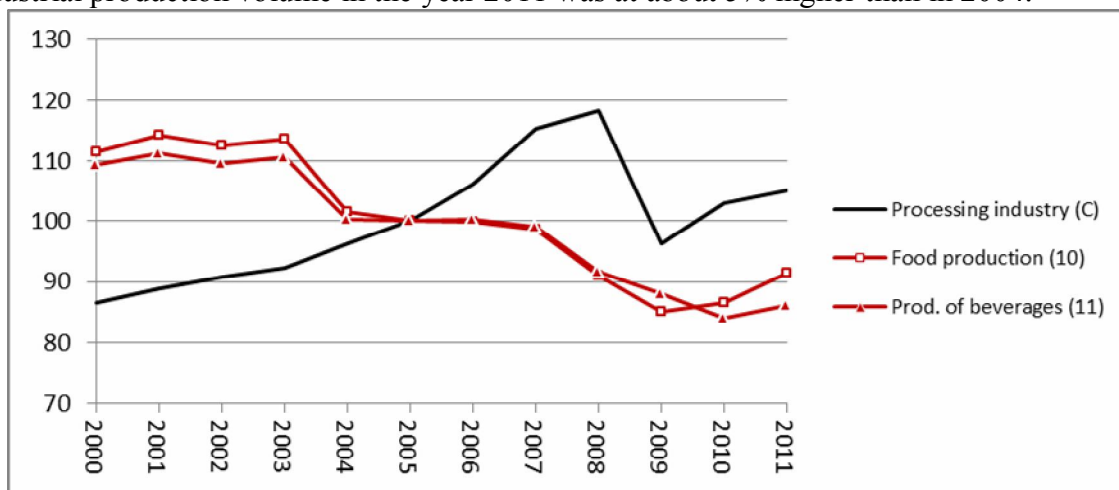


Figure 2. Industrial production volume indices in the period 2000 - 2011 (2004 = 100).

Unfavourable conditions in business performance of Slovenian food, beverages and tobacco manufacturing are discernable also from trends in productivity (measured as revenue from sales per employee) and value added per employee. Figure 3 shows values of the two indicators for food industry expressed as an index to the average of total manufacturing. In the year 2000 food industry attained about 25 % better productivity than average manufacturing and about one fifth higher value added per employee. However, the trends in the following years were constantly negative and in the year 2004 the value added per employee in food

industry fell below the average of manufacturing (index for 2005 = 92,2), whereas productivity was still slightly above the manufacturing average (2005 = 101,5). In the following years the indicators show some decent recovery. In the year 2009 value added per employee has risen on the levels similar to the year 2000, whereas labour productivity was almost ten per cent higher. In the following years the indicators fell again, where the productivity was still one tenth higher than on average of the processing sector, whereas the VA/employee was almost one tenth below the same average.

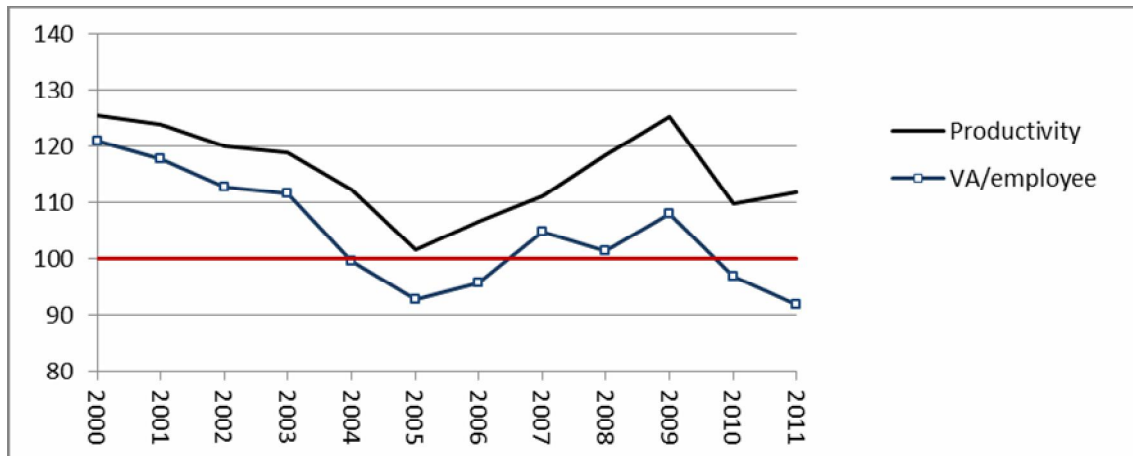


Figure 3. Productivity and Value added per employee in the Slovenian Food, beverages and tobacco manufacturing in the period 2000 – 2007; Total manufacturing = 100 (AJPES, 2012).

Consequently with worsening of productivity and value added creation, also profitability indicators have dropped, however with oscillating patterns in the last years. Trends of the profitability in the period between 2000 and 2007 measured as return to sales (ROS) is shown in the Figure 5. In the last years of the previous decade ROS was approaching 4% levels, but in year 200 and 2001 the value dropped considerably which was mainly due to the changed accountancy standards. In the pre-accession period the returns to sales was around 3,4%, but after the accession the indicator fell to negative value. Since then the results were constantly and steadily improving in order to reach 4,2% in 2007 which was higher than the average of the processing industry in Slovenia (ROA 2007=3,9%). However, after that, the indicator dropped again considerably, particularly due to the excessive loss in the beverage sector.

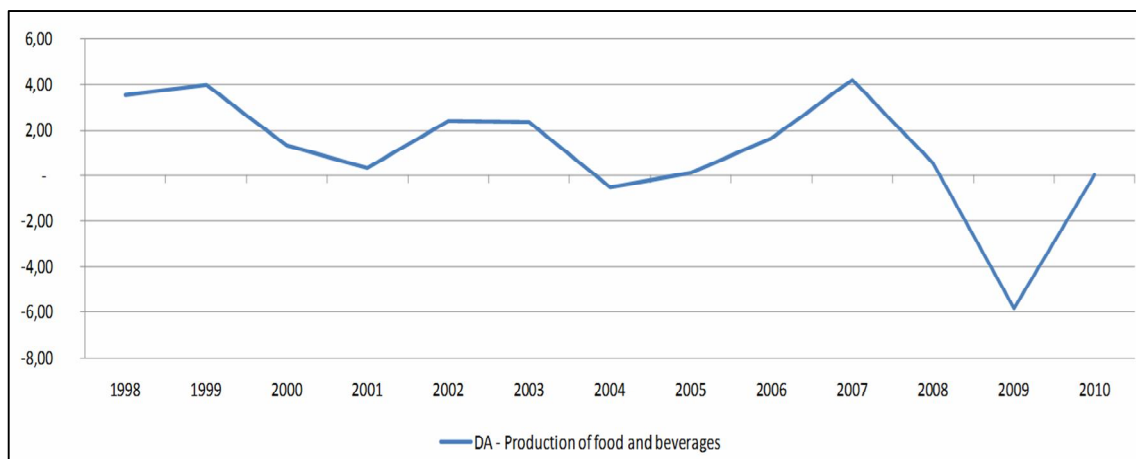


Figure 5. Return on sales (ROS) in the Slovenian Food, beverages and tobacco manufacturing. (AJPES, 2012)

The brief overview of some key indicators of business performance above shows rather apprehensive changes in Slovenian food, beverages and tobacco manufacturing sector. The sector has moved from one of the most prosperous industrial activities in Slovenia during the last decade to the average, but in the last two years some recovery is evident. What are the determinants behind these changes? In the following sections the article tries to answer this question with presenting trends in the economic environment of the food industry that might elucidate the developments.

2. EVALUATION OF SOME DETERMINANTS

2.1. Is food industry facing cost - price squeeze?

Price trend comparison at different levels of measurements reveals general information about the economic environment of an industrial sector. Figure 6 shows movements of price indices for agricultural inputs, producer prices of food, beverages and tobacco, the producer prices of the food processing industry aggregate and import prices of food in the period 2000-2012.

Price index of food, beverages and tobacco at the retail level generally fluctuate around the inflation rate if there is no radical structural change in the economic environment. It was to a large degree the case also in Slovenia; however after the year 2004 prices started to lag behind inflation and we can notice a drop by 5 % in real terms. This might almost entirely be explained by the EU accession and inclusion of Slovenia to the internal market. Further the retail prices were falling also in the subsequent period, when at the end of 2006 reached the lowest point. After that lowest point slight strengthening is present until the 2007, when the constant trend of food price increase started. In the last months of the 2011 the food prices were at about 30% higher than in 2005 and more than 50% higher than in 2000. (Figure 8)

Agricultural prices were growing in nominal terms, however when expressed in real terms they were constantly falling until 2005. This was however expected outcome of the agricultural policy reform initiated in year 2000 as a part of the EU accession process. Market-price support measures of the agricultural policy were gradually substituted by income support measures. In comparison with year 2000 prices of agricultural commodities were lower by 12 % in real terms in 2005. In the subsequent years the real price started to increase and then two price peaks of the decade were reached, one in end of 2007 and the second one in the first years of 2009. The prices were then around 40% higher than in 2005. Immediately after the peak the prices started to fall sharply and in the summer 2009 almost reached the average level of 2005. In the following years the prices of agricultural commodities were growing with fluctuating trend, however in the January 2012 the prices were again 30% above the 2005 average. Prior the year 2005 the food producer prices were growing faster than consumer prices and agricultural prices, since they compensate 30% in the first five analysed years. Latter we can observe a significant push-up in the period of agricultural inflation (Y2007), however the price increase was not as high. After that a considerable lagging of the producer prices behind the food consumer prices is evident, which is being explained by the growth of the food import prices. The latter increase by impressive 20 percentage points in the last two years of analysis.

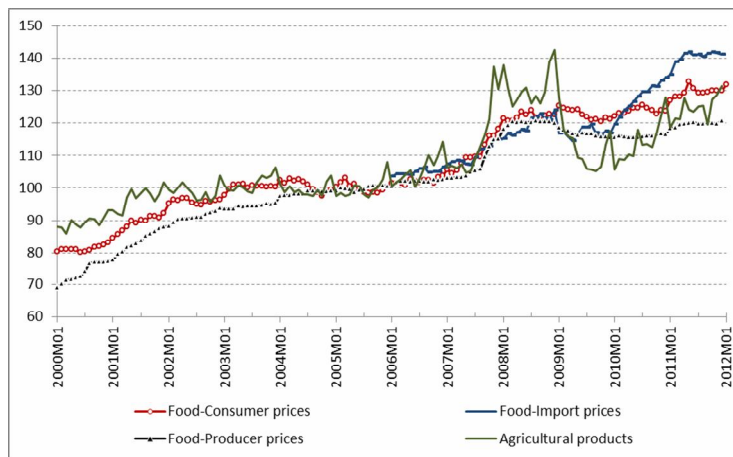


Figure 6. Indices for consumer prices of food, producer prices of food, import prices of food and agricultural products between 2000 and 2012; 2005=100 (SORS, 2012)

The price parities are shown in the Figure 7 where food manufacturing producer price index is compared with price movements of agricultural inputs, energy prices and labour prices. It might be anticipated that price parity for agricultural inputs is favourable for food manufacturers in the first period of analysis; indeed the index improved by 115 % between 2000 and 2005. Then, due to the abovementioned rise in agricultural producer prices in 2007, the price parity worsened (decrease by 10%), but improved again in 2009 in order to fall again in 2011 to about 5% below the average in 2005. Also the relation with the energy aggregate prices was favourable for food manufacturers in the first part of analysed period. However in the second part of the analysed period all price advantage has been annulled due to sharp price increase and the corresponding price parity has fallen to 87% in 2011. Furthermore, if trends in labour prices are compared to the producer prices of food, beverages and tobacco the former exceeds the latter and therefore the price parity getting less favourable for food producers. The parity value is decreasing constantly since 2000 with a turnaround in 2008, but than the parity was falling and has reached 95% in 2011. Here especially labour intensive sectors of food industry are negatively influenced.

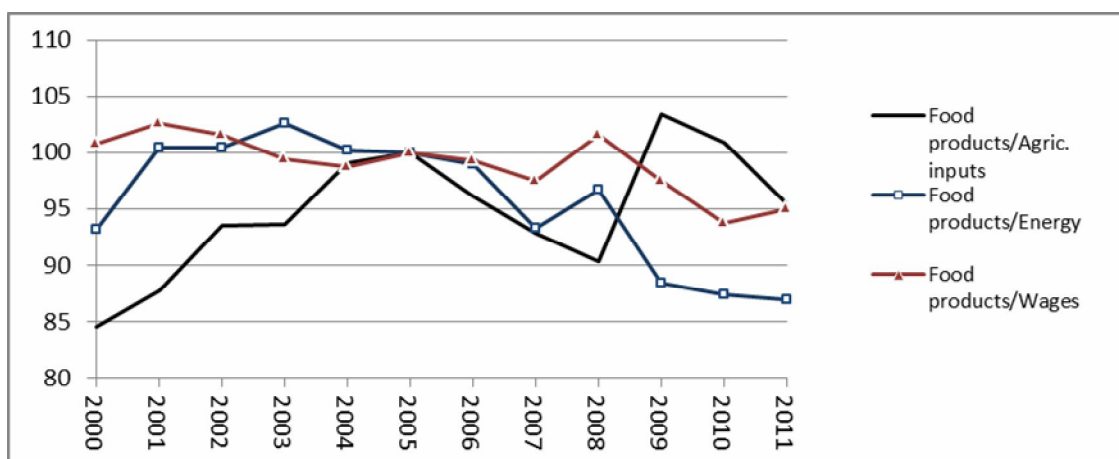


Figure 7. Selected price parities for Food, beverages and tobacco manufacturing (2005=100).

From the price trends and parities revealed above one can not firmly state radical cost-price squeeze for the food, beverage and tobacco manufacturers in Slovenia during the analysed period. Especially the sub-sectors with intensive agriculture input dependence (e.g. dairy, meat, bakery) could benefit from evident improvement of price parity, however this is not confirmed by business performance. A great part of potential positive price-cost development

is however absorbed within the supply chain. Anecdotic evidences point out intensive vertical pressures from retailing sector in Slovenia, which will be described in some more detail below. In case of producer – retailer business conduct in Slovenia (and other economies with highly dominant retailing sector) producer price is not the final element of the transaction that determine revenues of processors. Usually a series of retrograde discounts (e.g. for marketing, internationalisation, new products) is applied by the retailers quarterly, half-yearly or annually and is not captured within statistics of producer price. Retailers are imposing many other contractual and operational practices that negatively influence suppliers. Unjustified costs are carried onto producers (e.g. access to shelf-space, micro-distribution, ullage, collection of unsold goods etc.) which deteriorate their business performance and are of benefit to retailers. The next section describes development of the Slovenian retailing sector.

2.2. Who is creaming in the Slovenian food chain?

The role and position of food retailing in agro-food chain has changed considerably in the last few decades. Food retailers are not only passive intermediates between producers and buyers but a dominant determinant that is shaping considerably the economic environment of producers and actively present in evolution of food purchasing behaviour and food use.

Due to its basic economic characteristics the food retailing is the most flexible part of the agro-food chain that is able swiftly to respond to demand changes. Modern food retailing is therefore reactive and proactive – it is capable to perceive changes in all levels; but above-all it is capable of effective stimulation and directing. Domination of retail trade in food chain is a global phenomenon (Dobson et. al, 2003). In majority of developed economies the sector of grocery retailing has become increasingly concentrated both at national, but also globally. The sector is now dominated by a limited number of large multiple-store retailers that attract the majority of consumer spending on food. Slovenia here is no exemption and it ranges among the European economies with the highest level of concentration in food retailing sector (Juhasz and Stauder, 2005). High degree of concentration is an important lever of profitability in retail sector, as in this activity the positive effects of the economies of scale are substantial. Because of the structure of costs and basic economic characteristics an increase of the scope of business is translated in an immediate growth of profits. Table 1 illustrates the effects of changed scope of business on the profitability of a retail company (taken from Fearné et al. 2001). If net margin of a retailing company is 1 % for the value of sales of 100 units, it jumps to 26 % if the volume of sales increases by 2 %!

Table 1. Effects of sales value changes on net profit margin in food retailing (a hypothetical case)

	Case A	Case B
Sales value	100	102
Purchasing value of goods sold	80	81,6
Gross profit margin	20	20,4
Fixed costs	13,3	13,3
Variable costs	5,7	5,8
Net profit	1,0	1,29
Net profit margin (<i>profit /sales</i>)	1,0 %	1,26 %

Source: Fearné et all, 2001

Although this case is simplified (based on a cost structure of a French retail company), it is real enough to illustrate the mechanisms of growing market power of retailers in the process of concentration. Because of a high share of fixed costs and the characteristics of variable costs, which are as a rule disproportionately variable with the volume of revenues, the companies engaged in retailing are extremely responsive to changes of revenues from sales.

Any rise in the latter leads to disproportionate change in the profitability, and the same goes for a drop in the revenues from sales. Preparation of a profound study about retailing sector in Slovenia is beyond the scope of this article, however already a basic analysis of sectoral data reveals significant trends (Figure 9). Two fundamental indicators of the market structure are presented for Slovenian retail food sector and selected European countries. The first indicator is Herfindahl-Hirschman Index (HHI) that is a commonly accepted measure of market concentration. It is calculated by squaring the market share of each firm competing in a market, and then summing the resulting numbers (US Federal Trade Commission). Markets in which the HHI is between 1.000 and 1.800 points are considered to be moderately concentrated, and those in which the HHI is in excess of 1.800 points are considered to be concentrated and usually raise antitrust concerns of the governments.

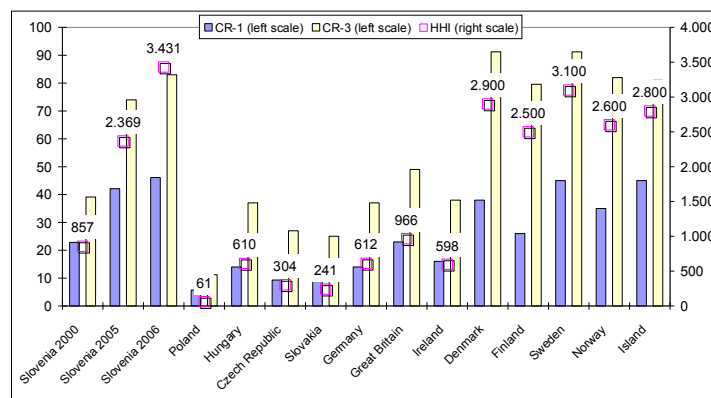


Figure 9. Distribution of revenues from sales in Slovenian retail trade sector. (IMAD, 2009)

The data for Slovenian retailing sector show enormous growth of the HHI value in the period between 2000 and 2006 since the index quadruplicated. In the last year the HHI reached the value of 3.431, a considerably higher value than estimated for Sweden and Denmark which have the among the highest HHI in Europe. Also according to the other indicator of the market structure – namely the Concentration ratio (CR); Slovenian retailing sector is highly saturated. The measure of Concentration ratios provide estimates of the extent to which the largest firms contribute to activity in an industry. We have estimated the Single firm concentration ratio (CR1) and Three firms concentration ratio (CR3) for Slovenian food retail for comparisons with the selected countries. In 2006 the largest Slovenian retailer contributed 46% of the total sectoral revenue, whereas the first three retailers contributed as much as 83%. Both figures are among the highest in Europe.

In 2000 the concentration was considerably lower (CR3=39 %) and sector was predominantly consisted of small regional retailing groups and traditional independent retailers. Driven mainly by processes of mergers and acquisitions by a leading retailing group and organic growth of other major players the sector has become highly consolidated. The small independent retailers have been marginalised and are now; if survived - restricted to act as convenience stores for top-up shopping. Simultaneously with the sectoral concentration growth also business performance was rapidly improving for the few leading enterprises.

The food retailing sector in Slovenia has clearly foregone drastic structural changes in the last period. Surely, modern business strategies and practices were introduced, however with rather negative consecutive implications for suppliers. With the substantial consolidation of retail market the nature of the supply chain has changed considerably.

The scale of operations of the major retailers and their control of purchases means that they are able effectively to dictate terms and conditions to producers. Through aggressive bargaining strategies, including the use of de-listing tactics, and the increasing use of auctions

for awarding contracts, retailers have been able to drive down the prices and margins that producers receive. Allied to these moves has been the increasing use of vertical restraints placed on producers. These buyer-induced restraints generally take one of two forms: either aimed at further rent extraction or limiting producers' freedom or incentives to supply elsewhere. The first form includes listing charges, shelf-space fees ("slotting allowances"), promotion support payments and retroactive discounts on goods already sold. The second form includes exclusive supply obligations and other "non-compete" contract clauses as well as most-favoured-buyer type contracts.

Also heavy investment has allowed retailers to reap economies of scale through the operation of large store formats and large chains of stores. This has been supported by the implementation of sophisticated logistics and distribution systems married with significant investment in new technology (such as e-POS). The result has been significantly improved efficiency with greater sales per outlet and per employee. However, beside a very successful modernisation, introduction of contemporary management practices and conduct, established growth of profit might be ascribed to the market structure too. Oligopoly – oligopsony market structure enables economic domination of retailers in the Slovenian food chain. High level of vertical power makes retailers possible to introduce business practices that adversely affect the competitiveness of their suppliers and distort competition.

Beside the evident negative effects on food suppliers' business performance the result in Slovenia might be also that suppliers are likely to invest less and spend less on new product development and innovation, leading to lower quality and less consumer choice. The high level of concentration in Slovenian retailing has negative implications also on smaller entities in the sector itself. Certain of the practices give the major buyers substantial advantages over other smaller retailers, whose competitiveness is likely to suffer as a result, again leading to a reduction in consumer choice.

Negative occurrences in the vertical relations is not unique in Slovenia, however several structural deficits of the food sector make the condition for suppliers even more unfavourable. One of these negative features is a low level of integration of Slovenian food processors into the international markets.

2.3. Are the trends in international trade with food surprising?

Slovenia has traditionally been and will very likely remain a net food importer; however the importance of agro-food trade in total international trade is limited. The aggregate of agro-food commodities accounted less than 3 % of total exports and about 6,5 % of total imports of Slovenia (SORS, 2012). If we focus on processed food alone total trade has been growing steadily in the analysed period (Figure 10). The value of export reached 1,365 billion EUR in 2011 which is around four times more than in 2000. The import was increasing constantly after the independence, however after the EU accession the growth rate has noticeably intensified due to a significant reduction in border protection (see below).

Export of processed food was oscillating somewhere around 350 millions EUR in the pre-accession period. Until the year 2004 the value was increasing with constant trend, however in the year of accession exports decreased. Exports improved again after 2005 and in the last year the figure reached 0.6 billion of EUR.

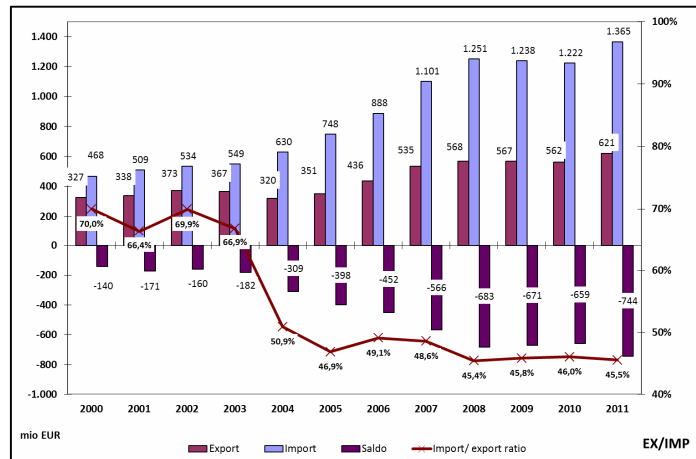


Figure 10. Slovenian international trade with food, beverages and tobacco products. (SORS; 2012)

One of the important features of the Slovenian international trade with food until the accession was a rather equalised development of both sides of the balance and therefore the export-import ratio has not oscillating considerably. Due to the import increase and export decrease after year 2004 net trade deficit has almost doubled. Consequently the export-import ratio has fallen to 45 % from the levels above two thirds in the pre-accession period.

Before the EU accession Slovenia has signed various bilateral and multilateral trade agreements which progressively opened its borders to a widening range of food commodities. At the same time these agreements were increasing the potentials for better access to foreign markets for Slovenian food products. However, it might be concluded that the pre-accession trade policy has not stimulated international competitiveness of the Slovenian food industry and trade pressures are among the main determinants of decreasing sectoral performance. Unfavourable developments on both sides of the Slovenian food trade balance could be anticipated if the basic features were to be considered.

The figure 11 shows effective tariff rate for food, beverage and tobacco aggregate and selected food products sub-groups in the period between 1998 and 2004.

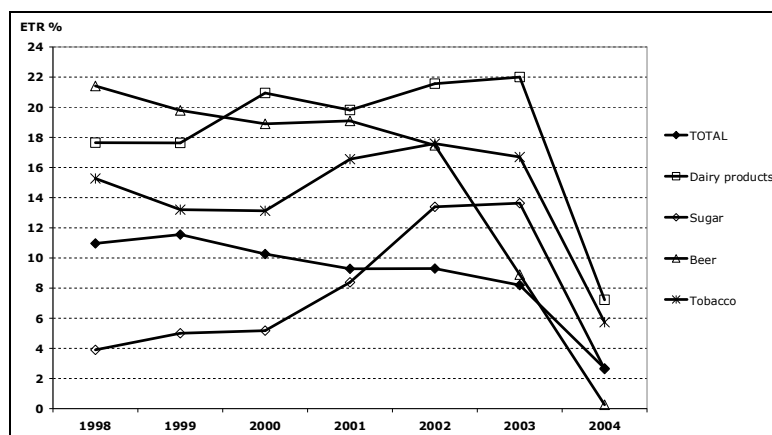


Figure 11. Effective tariff rate for food, beverages and tobacco products aggregate and selected product groups in Slovenia. (Ministry of finance, 2005)

For the majority of other food groups the effective tariff rate in the pre-accession period has been fluctuating around 10 %, whereas lower effective protection was found edible oils, processed fruits and vegetables and in the last period also for wine.

From the evaluated import protection one could anticipate the effect of the inclusion to the internal market of the European Union on Slovenian food trade. The Slovenian food market

has been highly protected until the EU accession and therefore access of foreign competitors has been impeded. After the accession the trade barriers for products from the European Union has been abolished and the effect of “trade creation” appeared, which is described as a basic effect of trade union (El Agra, 1994). Effect of the import growth after the accession was also accelerated due to the regional structure of imports. In the pre-accession period more than a half of the total food imports value was originating from old member states of the European Union.

Also on the export side of the Slovenian trade balance the EU accession effects might be expected from the regional structure of trade which is presented in the figure 12. Until the year of accession not less than 60 % of the Slovenian food exports was realised on the markets of Former Yugoslavia. With these countries Slovenia signed different trade agreements which made food products price competitive in comparisons with other imported products. However, after the takeover of the Common custom tariff of the European Union these trade agreements were abolished and Slovenian food products were charged with tariff and consequently the import prices increased. This has immediately resulted in export decrease to the former Yugoslav markets by 15 % in 2004 and further similar fall in 2005. In the last year the share was slightly above 35%. The share of food exports to the European Union markets was indeed increasing during the entire period. In the year 2011 the share reached almost two thirds of the total exports, out of which about 10% was realised on the markets of “new member states including Bulgaria and Romania. Regarding the growth of exports it should be noticed, that its considerable part is due to intensified export of standardised milk in bulk to the neighbouring states – particularly to Italy.



Figure 12. Regional structure of Slovenian exports of food, beverages and tobacco products. (SURS;2012)

The changes in trade policy after the accession might not be the single determinant of the constant decrease of Slovenian exports to the traditional markets. Beside these, also other factor changed among the most influential are: revitalisation of domestic food production in these markets; partially the Slovenian food export is being replaced with investments in production capacities in former Yugoslav countries; and not least also the policy measures to promote Slovenian agro-food export has changed. Next chapter describes the budgetary policy for food industry in Slovenia during the pre-accession period.

2.4. Has the budgetary support to the sector stimulated competitiveness?

Agricultural policy remains a rather important determinant of the economic environment of food industry in majority of modern economies. Under the influence are especially those sub-sectors that are closely related to the volatile agricultural markets. Budgetary transfers to food

industry have been decreasing during the analysed period (Figure 13), however with important changes in the structure of intervention. In the period during the years 2000 and 2004 the Slovenian food industry annually received between 30 and 45 million EUR of budgetary transfers. However, after the EU accession the figures have drastically decreased. In the year 2005 the total transfers to food industry dropped to 15 million EUR, reached 22 millions in 2006, and decreased to mere eleven millions EUR in 2007. In the years 2008 and 2009 the levels remained comparable to that.

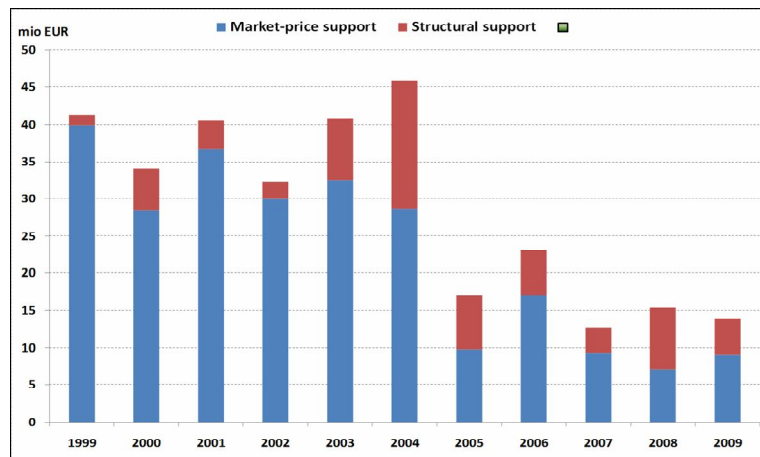


Figure 13. Budgetary outflows for Food, beverages and tobacco manufacturing in Slovenia. (AIS, 2012)

In the figure the total budgetary transfers are divided into two parts; namely market interventions and structural policy measures. The first part includes mainly transfers to exporting food enterprises (export subsidy) with intention to stabilise domestic agricultural commodity markets. Proportion of this type of support in total transfers to food industry was around 90 % until 2003, when the share of structural measures increased, but also the value of export subsidies decreased considerably. About two thirds of the export promotion transfers were earmarked for stabilisation of the dairy markets, whereas the majority of the rest was distributed to meat and vine processors. The export promotion measure in combination with bilateral trade agreements had clear distortive implications on competitiveness of Slovenian food sector and importantly influenced the structure of exports. After the EU accession the policy of export promotion has changed (eligible types of products, export destination, amount of support) and become administratively more demanding. Authority over the measure has been transferred to the EU Commission. All these changes have influenced the radical drop (for two thirds) of transfers under this measure in the post-accession period.

The second part of budgetary transfers to the food industry presented in the Figure 13 classifies to the structural support measures, which aim at the industry competitiveness improvement. Under different programmes (National program, Special Accession Programme for Agriculture and Rural Development, Rural Development Programme) the eligible food processors receive investment support for construction or renovation of production premises and /or purchase of machinery and equipment. The amount of transfers has considerably increased in the years 2003 and 2004 due to the launching of the EU co-funded SAPARD programme and the national programme. Whereas in year 2005 almost half of the transfers originate from the RDP a structural measure, which has been for the first time entirely prepared by the EU structural policy programming procedures. The same holds for the year 2006 and 2007, when the new financial period was initiated. The Rural development plan 2007-2013 will have the first results only in the subsequent years, however the instruments focused to the food industry have largely remained unchanged.

Despite the considerable amount of budgetary transfers to Slovenian food sector, majority of them has not been intended for long term competitiveness improvement, but rather to stabilise domestic agricultural markets and to correct price distortions. Only in the last period the share of structural measures increased, however processes to build sustainable economic competitiveness are demanding and long lasting.

3. CONCLUSIONS

The accession of Slovenia to the European Union was certainly the most comprehensive change of economic environment since the state gained its independence. The article attempts to reveal the economic trends in food industry during the pre-accession period and the first year of the membership. With the presentation of selected economic indicators it tries to answer four most striking question facing by Slovenian food manufacturing sector, which experiences constant deterioration of business performance. The questions are rather fundamental; however they have not been tackled systematically yet.

The price trends at all levels (input costs, producer prices, retail prices) in the sector are revealed not to be radically negative. Especially the prices of agricultural inputs have dropped considerably before accession, whereas the producer prices of manufactured food in the analysed period surpassed the overall price growth. However, prices of food at the retail level (e.g. price of composite supply) reduced in real terms. This might be explained by reduction of import prices due to the abolition of tariffs, but the price competitiveness of Slovenian suppliers has therefore deteriorated. Analysed price parities are mainly favourable for the food manufacturers – producer prices are growing at decreasing or stagnant input costs; however producer price does not represent the whole revenue side. Especially not in the economies with highly concentrated retailing sector. The analysis confirmed evident trends in Slovenian food chain. Food retailing in Slovenia has reached very high level of market concentration and the leading four players now control over eighty percent of sales in the sector. During the analysed period the concentration in retail trade has been increasing which has been most obviously reflected in the pressures on suppliers, shifting of an increasing share of transaction and distribution costs, and in other requirement and conditions for cooperation.

Therefore the first question regarding cost-price squeeze in the food manufacturing sector might be answered partially affirmatory, whereas the answer to the second question is much more straightforward. In a phenomenon of vertical competition the Slovenian retail sector undoubtedly dominate the chain, whereas at the same time its first vertical partner – the domestic food manufacturing industry is stagnating also due to market power abuse. The retailing domination is a global appearance; however Slovenian food manufacturers are in specific circumstances due to other structural deficits. One of important ones is a specific international trade structure and distorted competitiveness on traditional markets. It has been revealed that among the main determinants of low competitiveness is pre-accession trade policy which consists of high tariff barriers and free trade agreements with ex-Yugoslavian countries. After the EU accession “ad-hoc” liberalisation triggered substantial import pressures and reduction of sales on domestic markets. Changed trade agreements were detrimental to the competitiveness on the traditional export markets, and there are only moderate trade creation effects with penetrating the EU markets. Poor integration into the EU single market thus remains one of the major structural deficits of this industry, which became obvious very soon after joining the EU. The foreseen changes of the conditions in traditional export markets, which were a consequence of acceding to the common customs tariff, radically reduced advantages of Slovenian companies there, which ended in a slump in exports. The attempts of food-processing companies to compensate for this drop by establishing themselves in the EU single market have been rare so far. Moreover, in these markets, companies face problems of a competitive and vertically integrated economic

environment. Penetration into the market channels in an enlarged business environment marked by high concentration of supply will be extremely difficult for Slovenian companies. In close relation to the revealed deficiencies in international trade is also government intervention in the sector through the budgetary transfers. The majority of transfer to food industry was under the measure that has in great extent comparable implications as classical export subsidies, only a small part of the budgeted until 2003 was intended for restructuring and competitiveness. The considerable growth of structural funds in the last years is beneficial; however the moment has been lost for the needed pre-accession restructuring of the industry. Food industry is therefore now facing a substantial stimulus for sectoral restructuring at about one and a half decade later than the rest of the processing industry in Slovenia.

The agro-food sector is among the parts of economy that has undergone the most radical changes, and therefore long term accession implications are expected to be the most evident.

The economic restructuring that had been hindered in the Slovenian food industry during the last decade has been triggered radically after EU accession which brought to the termination of favourable economic conditions in the highly protected domestic market. Competition from the internal market, but more significantly the reduction of export competitiveness due to the abolition of free trade agreements has caused an important long term deterioration of economic performance in almost all sub-sectors of the Slovenian food industry.

The government failed to implement a gradual foreign trade liberalisation in the market of processed-food products, which would allow control over the dynamics of exposure of domestic suppliers to foreign competition. Instead, food-processing industry was in some key segments protected up to the accession, when the "ad hoc" liberalisation took place. It can thus be expected that the consequences of accession will be more negative than they would have been should a gradual liberalisation took place. Establishing sales opportunities and business partnerships is an extremely demanding and long lasting process, especially on the saturated and extremely competitive food markets of the European Union. As a rule, capital intensity of production is the main generator of value added per employee, which, however, depends on the use of new technologies. Innovation, development of new products and distribution methods are crucial for successful food-processing companies, with the emphasis on consumer friendly use, positive nutritive effects eco-products and environmentally friendly production. Although lately Slovenian companies have paid some more attention to these issues, the quality of supply and generated value added remain low. Only those Slovenian food-processing companies which will modernize their management and marketing strategies and actively seek for new business opportunities will in the long term be successful in the European Union markets.

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