Concentration in Hungarian Food Retailing and Supplier-Retailer Relationships[1]

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Abstract

The paper is a summary about the Hungarian retail sector based on the results of different research projects completed in the last five years. From all of these studies and of course the wide ranging domestic and international literature we had to conclude that the retailers have become more and more the exclusive owner of the information about the consumers and with this they become the new "captains" of the food chain. Thus we always started our research with gathering information about the situation of the Hungarian retail sector because we believed if we want to help those who try to adapt (the suppliers) then we have to know much more about those who dictate (the retailers).

Analysing the concentration in company and not branch level we can say that the cumulated concentration line of the CR-10 agricultural companies are very similar to that of the processing and the retail sector. But there is a very important difference in the absolute numbers. This is a further sign of the size and power difference in favour of retailing.

JEL classification: D3, L81

Keywords: food retailing, concentration, market structure, supplier-retailer relationships

1. Introduction and international comparison

In 2003 the net retail sales of consumer goods in the countries of the EU-15 with the population of around 380 million persons passed 1 000 billion USD, while in the 8 Eastern European new member states (73 million persons) it was only around 65 billion USD. The value of sales per person in the EU-15 grew with 25% between 1998 and 2003 and reached 2 751 USD, while in the 8 new member states with considerably (+67%) larger growth rate it still only reached 896 USD, 33% of the EU-15 average (Figure 1). In 5-10 years the value of retail sales per person in the two European country groups may come closer to each other, as the eastern European countries expect income growth and the Western European countries retail markets are coming close to maturity.

According to their concentration (CR-5) the Eastern European countries can be grouped into three categories. The countries are written in decreasing concentration order.

- Over 65%, the highest category: Lithuania, Slovenia, Estonia, Hungary
- Between 35-65%, middle category: Croatia, Latvia, Czech Republic
- Between 20-35%, low category: Slovakia, Romania, Poland, Bulgaria, Ukraine (Figure 2).

2. Trends in the Hungarian food retail sector

The political and economical transition at the beginning of the nineties and the privatisation had significant effect on Hungarian food trading. It was attractive for investors, especially for foreign investors. Several international supermarket chains started operating in Hungary, by reconstructing the old supermarkets or with green field investments. Some supermarket chains of Hungarian ownership were also created, some of them developed very quickly, expanding also abroad. In spite of this, most of the Hungarian trading businesses consisted of small- and medium-size enterprises, and was short of capital. Concerning the changes in the Hungarian food trade we have distinguished four periods:

- Spontaneous privatization 1989 - 1991
- Privatization 1992 - 1995
- Concentration begins 1996 - 2000
- Accelerated concentration 2001 -

The period of spontaneous privatisation happened in 1989-1990, when some mainly smaller shops were privatised, but when a significant number of private shops were established as well. Therefore the number of food retail shops started to grow.

During the period of privatisation (from 1991 to about 1995-96) the owners of the larger food retail chains have been changed (e.g. KÖZÉRT). Most of the shops in the favourable areas have become the properties of multinational chains. Some of the small private shops continued to develop, but some of them went bankrupt. The first part of the period is characterised by the launch of so-called "forced"[2] enterprises, lot of them only remaining in business for a short time. Therefore at the beginning of the nineties a big jump happened in the number of food shops. Within this, the number of shops operated by sole proprietors also grew. Their share in the total was the highest in the middle of the decade.

We call the last few years of the nineties the beginning of the concentration (1997-1999/2000). This period may be characterized with the appearance and growth of the mainly foreign owned multinational companies operating new, large surface store formats (hypermarkets) and the domestic owned chains (buyer groups) gathering mainly smaller store formats (small-shops, supermarkets). Still in this period, besides the ever strengthening modern retailing the small, independent shops represented a large and not decreasing number and share of the stores.

The new Millennium brought more changes, the concentration of retailing started to accelerate (from 2000), the winners of this period seem to be the multinational companies operating large surface stores and the domestic buyer groups with small-medium store formats. The real difference between this and the previous period is, that the number of stores and the especially the number of independent small shops started to decrease and we expect a more rapid disappearance of them in the next few years.

If besides concentration we analyse also the structure of the market that is the size and differences in the first five retail companies (Dobson, 2002, Appendix 1, 2) we can say that

[2] After the change of political system unemployment increased drastically thus thousands of people started their own small businesses mostly employing only themselves or the members of the family.

the Hungarian retail sector is an asymmetric oligopoly. In the food processing sector the structure of the meat processing is also an asymmetric oligopoly, while the vegetable oil manufacturing is a monopoly. The other eight branches with 30 sub-branches can not be categorized as easily. But we could only find two sub-branches which had the least buyer power implicating structure namely not concentrated, one important the other fruit and vegetable processing and wine production. From the ten agricultural production branches eight belonged to this not concentrated category, an implication for the unfavourable position of raw material production.

Analysing concentration in company and not branch level we can say that the cumulated concentration line of the CR-10 agricultural companies are very similar to that of the processing and the retail sector (Figure 3). But there is a very important difference in the absolute numbers, while the CR-10 was 89% and the largest company had 1 211 million USD net sales in the retail sector, in the food processing industry the CR-10 was 22% and the largest company had 420 million USD (Figure 4), and in the agriculture the CR-10 was only 7% and the largest company only had 85 million USD (Figure 5). A further sign of the size and power difference in favour of retailing.

The ratio of the CR-10 retailers also shows the ever quickening pace of concentration. Between 1997 and 2003 the ratio of the largest ten food retailers from the total sales of the branch increased by 37%. In both 1997 and 2003 the Top-10 retailers share from the total sales (52% and 89%) had been realised in around 20% of the stores which means that the Top-10 retailers could capture larger market share without considerably increasing the number of stores. According to statistician experts a part of the rapidly growing concentration can be explained by the fact that the larger and more stable companies with consolidated market presence are more willing and precise in data provision.

We have two additional comments on the issues of the Top-10 lists and retail concentration. Companies operating C+C (cash and carry) stores like Metro and Interfruct are registered as wholesalers thus are not part of the retail statistics of Central Statistical Office and our previous figures, tables and analyses. Metro operates almost like a hypermarket and if we take it into account it would have been the second in the 1997 Top-10 list and the fourth in 2003. The retail stores are even more concentrated on the procurement side. From the Top-10 list Spar and the wholesaler Metro forms the buyer group METSPA with more than 1 800 million USD sales. Also from the Top-10 list the last two, Cora and Csemege (Match, Smatch, Profi, Alfa) founded PROVERA buyer group.

The domestic retail trade changes can not only be characterized by the increasing concentration and the decreasing number of stores but also with the appearance and success of new store formats and strategy types. Thus one of the reasons of the store number decrease is the ever increasing popularity of the large surface store formats.

Summarizing our knowledge of the Hungarian retail trade we can say that this sector is best characterized as “two poled” because beside the ever growing concentration and popularity of large surface stores the presence of the small shops is also very important. We found four main reasons for the still large number of small shops:

- With good adaptation strategy they can operate as convenient stores, specially formed to the needs of the local consumers.
- The presence of the so called “forced entrepreneurs” who started their business not to be unemployed and either invested too much energy and money to quit or still do not have alternative employment opportunities.
- The success of the almost franchise like domestic buyer associations who with their improved and centralized buying and other services offered considerably enhanced the assortment and price competition of these small shops.

- And last but not least the immobility of a large segment of the Hungarian, mostly rural population which makes the accessibility of the mostly out-of-town large stores difficult.

Few words about what we accept to be the main trends in the international food retailing:

- Globally further dynamic internationalisation.
- In the CEE countries and other not matured markets the selection of the domestic chains but the strengthening of the remaining ones.
- New international expansion of the discounters particularly the hard discounters (e.g. Lidl and Aldi) which is already happening in Hungary.

The food retail sector of Hungary is quite well developed almost a mature market especially compared to the other countries in the CEE region. Thus except in some particular segments – e.g. hard discounter Lidl – we do not expect many more green-field investors into our market, mergers and acquisitions are more likely to come.

3. Relationships of food producers and traders

„Modern retailers are…. a row of high-rise hotels between the manufacturers' villa and the consumers' beach."

(Cortjens és Cortjens, 1995)

With the appearance of retail chains the system of relationship of producers-traders considerably changed. In these relationships partners are usually not equal. The trader dictates and the producers have to adapt to the rules. It is true, however, that in spite of the unfavourable conditions, being the supplier of a chain makes it possible for food producers to sell large volume of products.

Apart from the expansion of retail chains of foreign ownership in Hungary, retail chains of Hungarian ownership were established as well, either by changing the existing structures or by establishing new enterprises. These Hungarian chains tried to keep up with the foreign chains in their outside appearance, solutions of logistics, information technology and in their way of handling suppliers learning quickly from the efficient foreigners.

In the past few years more and more buying associations were established with the collaboration of food chains, further increasing the already strong bargaining position of the traders and further increasing the concentration of trade.

Special problems and strategies of the SME suppliers: findings of an interview based research

Small entrepreneurs who wish to become suppliers constitute a special segment in the relationship of producers and traders. Based on the interviews conducted with the managers of the food trading companies we summarised our results.

Traders do not expect large advertising contribution from small-size enterprises, however, they try to compensate it somehow; for example, by paying lower purchasing prices. There is also the problem, which is due to the small size of the companies; that is, they are not able to supply in sufficient quantities even to a small chain. They do not always realise what it means to be a supplier of a food chain. This means that the product supplied has to be found in each store of the chain and it cannot be out of stock. Regarding the distribution and logistics small-size enterprises cannot provide direct transport and this is a disadvantage - this might sometimes also prevent them from becoming a supplier. This obstacle can be overcome by marketing co-operation established by the producers (co-operation might be useful also in the cases of regional specialities).

Another significant disadvantage of the small-size enterprises is the lacking capital, that is, the power of market. Small-size entrepreneurs are much more exposed on the market than the large ones; in general they are not able to invest capital in order to defend themselves. A further requirement or the secret of the success is that these products have to satisfy niche markets. No small-size enterprise can be successful with universal production.

We also collected information on the possible ways of helping small-scale suppliers to integrate into this global retail world. According to Narayanan and Gulati (2002) there are two possible ways of helping small-scale suppliers on the central governmental level. The first group of measures are connected to enabling factors which may include help in developing vertical coordination (e.g. sample contracts), in decreasing transaction costs (infrastructure development), or with education and special financial/credit programs. The other cluster of measures are the coping factors including the support of risk reducing and insurance programs, the development of rural but non-agricultural employment potentials and the special product innovation programs suitable for small-scale production/processing.

Apart from the central governmental measures the suppliers in a buyer power driven chain my also have initiatives of their own. We find the strengthening of vertical and horizontal cooperation outstandingly important in this situation.

4. Conclusion

The new Millennium brought more changes, the concentration of retailing started to accelerate (from 2000), the winners of this period seem to be the multinational companies operating large surface stores and the domestic buyer groups with small-medium store formats. This is the main reason for the Hungarian retail trade becoming “two poled” with ever growing concentration and popularity of large surface stores but also the significant presence of the small shops.

In the food retail sector Hungary is a quite well developed almost mature market especially compared to the other countries in the CEE region. Thus except in some particular segments – e.g. hard discounter (Lidl) – we do not expect many more new green-field investors into our market, mergers and acquisitions are more likely to come.

If besides concentration we analyse also the structure of the market that is the size and differences in the first five retail companies we can say that the Hungarian retail sector is an asymmetric oligopoly.

The ratio of the CR-10 retailers also shows the ever quickening pace of concentration. Between 1997 and 2003 the ratio of the largest ten food retailers from the total sales of the branch increased by 37%. In both 1997 and 2003 the Top-10 retailers share from the total sales (52% and 89%) had been realised in around 20% of the stores which means that the Top-10 retailers could capture larger market share without considerably increasing the number of stores. According to statistician experts a part of the rapidly growing concentration can be explained by the fact that the larger and more stable companies with consolidated market presence are more willing and precise in data provision.

With the appearance of retail chains the relationship of producers-traders considerably changed the partners are usually not equal. Our findings in the supplier (especially SME) buyer relationship are grouped into problem and possibilities factors.

We also collected information on the possible ways of helping small-scale suppliers to integrate into this global retail world. On the central governmental level the first group of measures are the enabling factors and the other cluster of measures are the coping factors. The suppliers in a buyer power driven chain may also have initiatives of their own. We found the strengthening of vertical and horizontal cooperation outstandingly important in this situation.

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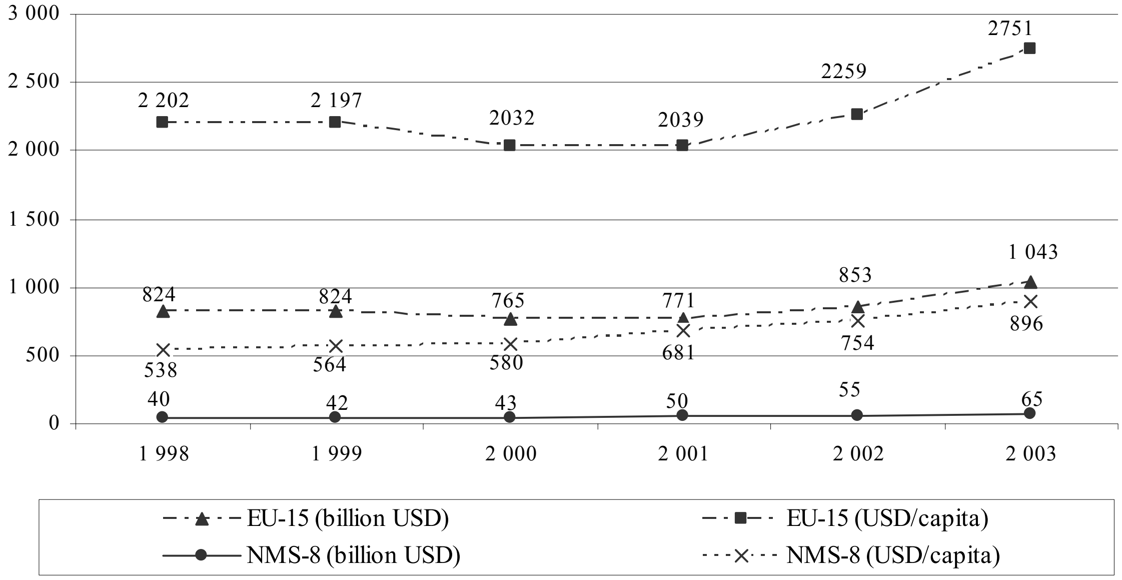
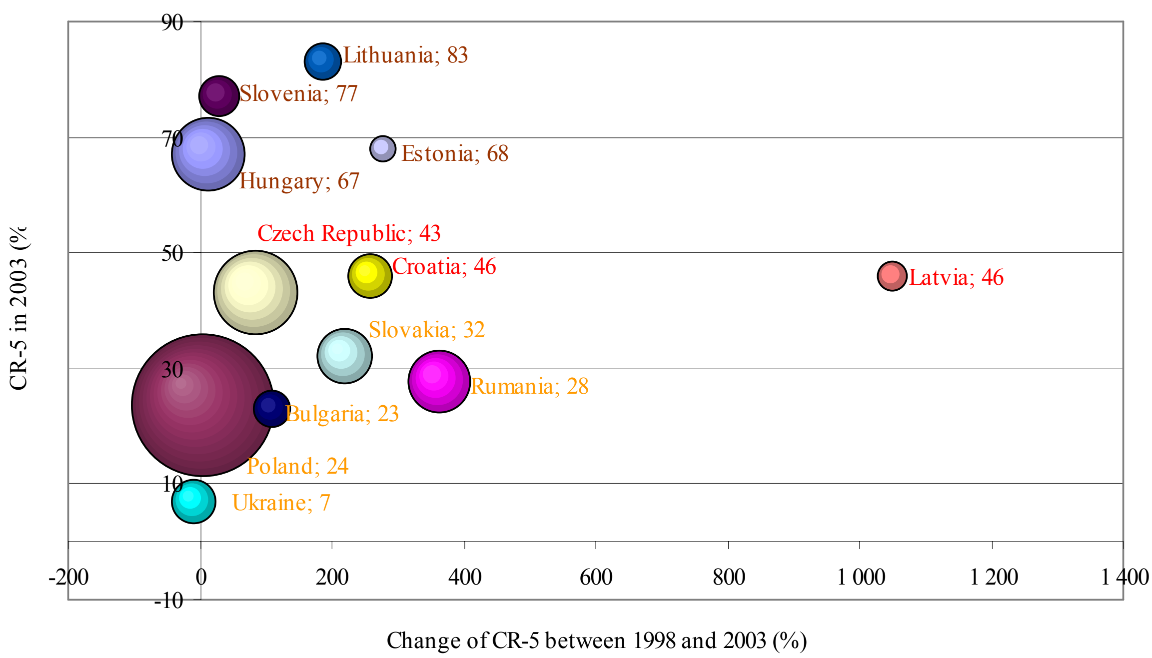
Figure 1: The consumer goods retail sales of the European countries



Source: Own calculation from Planet Retail database

NMS= New Member States-8 without Cyprus and Malta

Figure 2: The concentration of the Eastern European countries retail trade between 1998 and 2003[3]



Source: Own calculation from Planet Retail database

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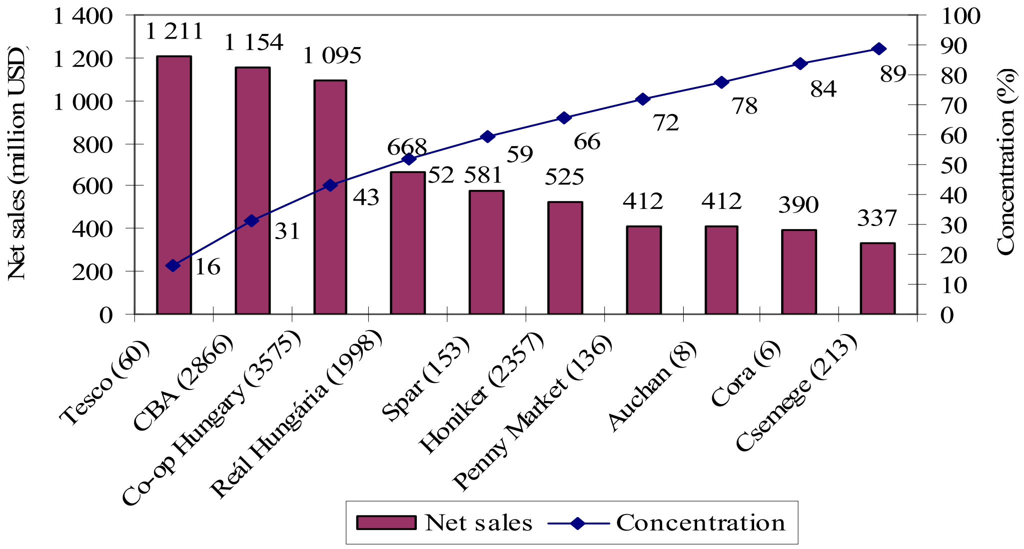
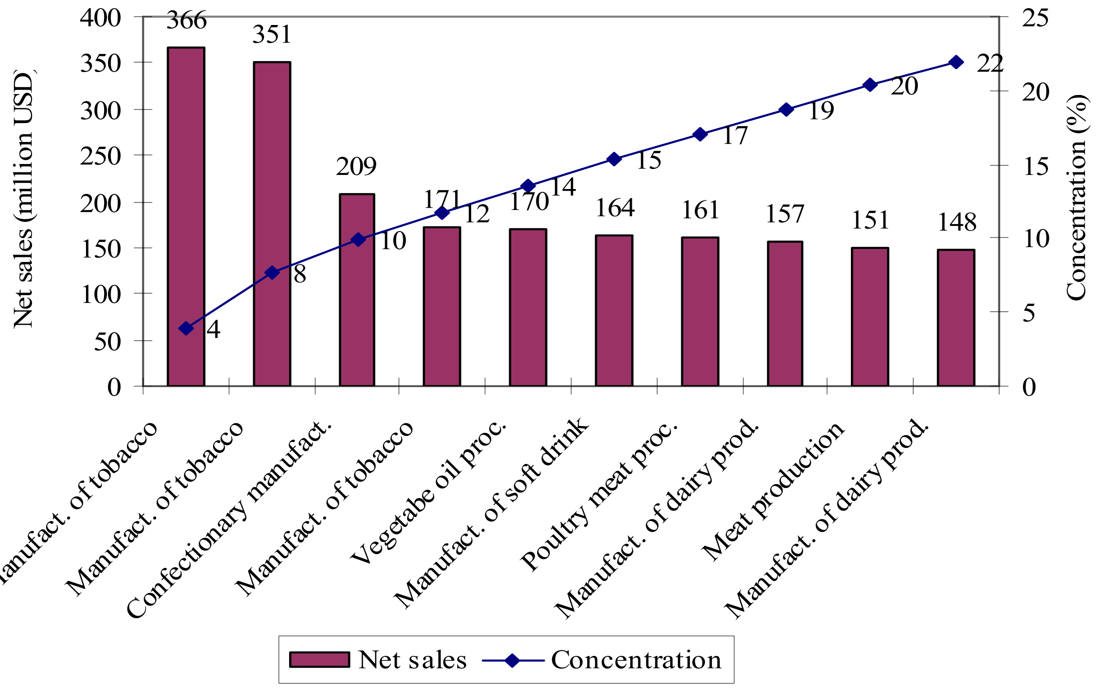
[3] The size of the circle shows the retail market size of the country in 2003: Hungary =8,6 million USD; Poland =32,6 million USD

Figure 3: CR-10 food retail companies share from FMCG retail sales[4] 2003



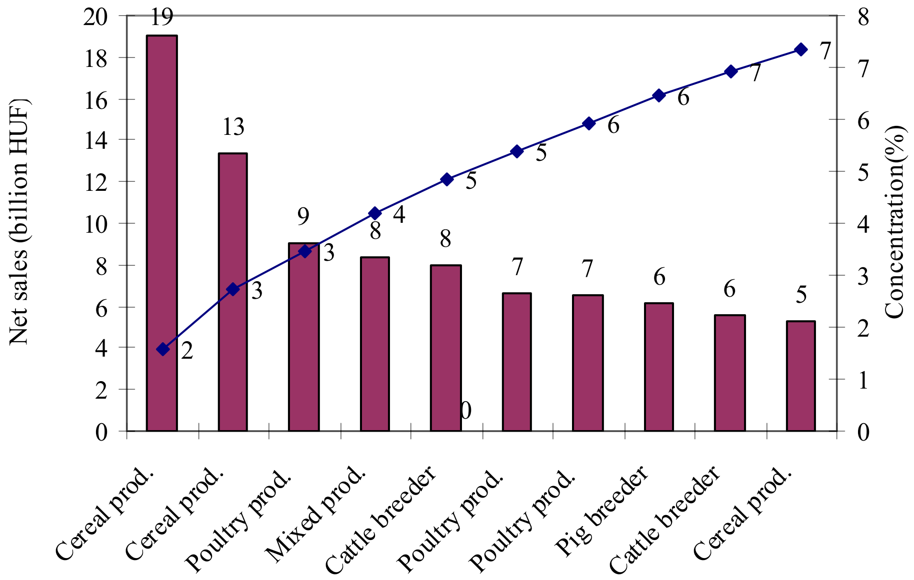
Source: Own calculation from database of the CSO (1998-2004) and the issues of Mai Piac (1998-2003)

Figure 4: Concentration (CR-10) of the Hungarian food processing sector (2002)



[4] C+C companies like Metro are registered as wholesalers thus are not part of the retail statistics of CSO; The numbers in the parenthesis are the number of stores operated by the company

Figure 5: Concentration (CR-10) of the Hungarian agricultural sector (2002)



Appendix 1: Retail market structure of the CEE countries between 1998 and 2003

		CR-5	MS1	MS2	MS3	MS4	MS5	Type of market structure
Hungary	1 998	59	20	17	13	5	5	Asymmetric oligopoly
	2 003	67	18	18	12	11	8	Asymmetric oligopoly
Poland	1 998	23	11	6	3	2	1	Not concentrated
	2 003	24	10	4	4	3	3	Not concentrated
Czech Republ.	1 998	23	5	5	5	4	4	Not concentrated
	2 003	43	11	10	9	7	6	Symmetric oligopoly
Slovakia	1 998	10	3	2	2	2	1	Not concentrated
	2 003	32	12	7	5	4	4	Not concentrated
Slovenia	1 998	60	51	8	1	0	0	Dominant company
	2 003	77	59	12	2	2	2	Dominant company
Latvia	1 998	4	3	0	0	0	0	Not concentrated
	2 003	54	20	12	8	5	0	Asymmetric oligopoly
Lithuania	1 998	29	22	6	1	0	0	Dominant company
	2 003	83	46	16	12	8	1	Dominant company
Estonia	1 998	18	13	3	2	0	0	Dominant company
	2 003	68	33	23	6	4	1	Duopoly
Bulgaria	1 998	11	10	1	0	0	0	Not concentrated
	2 003	23	17	4	1	1	0	Not concentrated/ Dominant company
Romania	1 998	6	6	0	0	0	0	Not concentrated
	2 003	28	17	7	2	1	1	Not concentrated/ Dominant company
Croatia	1 998	13	6	3	3	1	0	Not concentrated/ Dominant company
	2 003	46	8	5	5	4	0	Symmetric oligopoly
Ukraine	1 998	6	4	1	1	0	0	Not concentrated
	2 003	18	6	5	4	2	2	Not concentrated
NMS-8 average	1 998	28	16	6	3	2	1	Not concentrated
	2 003	56	26	13	7	6	3	Dominant company
CEE-4 average	1 998	9	7	1	1	0	0	Not concentrated
	2 003	29	12	5	3	2	1	Not concentrated/ Dominant company
CEE average	1 998	22	13	4	3	1	1	Not concentrated/ Dominant company
	2 003	54	25	12	7	5	3	Dominant company

Source: According to Dobson et al (2003) method using the Planet Retail database
CR-5=concentration ratio of the top-5 companies, according to their net sales;
MSi = market share of i company;
Dominant company = MS1>25% and MS1>2*MS2;
Duopoly = MS2>15% and MS2>2*MS3 and not dominant;
Asymmetric oligopoly = MS1>15%, MS>5% and MS1>1,5*MS4 and not the previous two category;
Symmetric oligopoly = none of the previous ones and MS>5% and at least 67% of the next one;
Not concentrated = MS<10% and CR5<33%, The averages are not weighted

Appendix 2: The market structure of the Hungarian food processing industry (2002)

	Net sales	CR-5	MS1	MS2	MS3	MS4	MS5	Type of market structure
Meat processing								
Meat processing	279	44	14	9	7	7	6	Asymmetric oligopoly
Poultry meat processing	227	62	18	16	11	10	7	Asymmetric oligopoly
Poultry and meat products	97	74	26	14	14	11	10	Asymmetric oligopoly
Fish processing	2	93	33	28	13	12	7	Duopoly
Vegetable and fruit processing								
Potato processing	20	99	51	24	20	2	1	Dominant company
Vegetable and fruit juice	43	84	29	26	14	9	5	Duopoly
Other vegetable and fruit	144	33	8	8	7	5	4	Not concentrated
Vegetable and animal oil processing								
Crude oil processing	2	68	38	8	8	8	5	Dominant company
Refined oil processing	44	100	99	0	0	0	0	Dominant company
Margarine production	3	100	98	2	0	0	0	Dominant company
Dairy industry								
Dairy product production	228	57	18	17	9	8	6	Duopoly
Ice-cream production	2	97	60	21	6	6	3	Dominant company
Milling industry								
Milling product manufact.	97	42	12	10	7	7	7	Symmetric oligopoly
Starch production	31	100	94	5	1	0	0	Dominant company
Animal feed production								
Productive livestock feed	143	48	16	13	9	6	4	Asymmetric oligopoly
Hobby animal feeds	25	96	78	11	3	2	2	Dominant company
Other food industries								
Bread, fresh pastry prod.	100	14	4	3	3	2	2	Not concentrated
Preserved bread, pastries	30	78	42	12	12	6	6	Dominant company
Sugar production	76	100	31	24	23	11	10	Asymmetric oligopoly
Confectionary	120	80	45	16	10	6	3	Dominant company
Food pastes	20	83	60	15	4	3	1	Dominant company
Tea, coffee manufacturing	15	87	64	13	6	3	0	Dominant company
Spice and seasoning man.	8	92	52	28	5	3	3	Duopoly
Other food production	3	98	37	30	28	2	2	Asymmetric oligopoly (3)
Drink production								
Alcoholic drinks	39	52	15	12	10	9	6	Asymmetric oligopoly
Ethyl-alcohol production	67	74	41	12	9	9	4	Dominant company
Fruit wine production	5	100	87	12	0	0	0	Dominant company
Wine production	55	24	6	5	5	4	4	Not concentrated
Other not fermented drink	0,2	80	37	16	15	7	5	Dominant company
Beer production	128	96	30	28	25	8	5	Asymmetric oligopoly (3)
Malt production	0,1	100	57	43	0	0	0	Duopoly
Soft-drink production	103	82	41	25	6	5	5	Duopoly
Tobacco manufacturing								
Tobacco product manuf.	249	100	38	36	18	6	2	Asymmetric oligopoly

Source: According to Dobson et al (2003) method using AKI-APEH database