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# Challenges for Brazil's Food Industry in the Context of Globalization and Mercosur Consolidation

**ABSTRACT:** This paper examines how the Brazilian food industry has been heavily affected by several recent institutional and economic changes. The food industry, including the processing and retail sectors, is part of a broader agribusiness system that conditions corporations' strategies, performance, and adoption of adequate governance structures. The Brazilian agroindustrialization process that preceded the formation of the sub-regional free-trade area (Mercosur) and economic liberalization influenced subsequent development of the agribusiness and food system in the Mercosur countries and their investment and trade links to countries outside Mercosur. The article emphasizes business strategies for coping with challenges and opportunities that have arisen from Mercosur integration, from economic stabilization programs and, more importantly, from a broad range of institutional changes such as trade liberalization, deregulation, and the friendlier treatment of foreign capital. These changes have together fostered the globalization process in the region and have stimulated different responses from large and small firms, all threatened by the new, competitive environment.

## INTRODUCTION

Mercosur (The Southern Common Market) was implemented on January 1, 1995, established by the Asuncion Treaty signed by Brazil, Argentina, Paraguay, and Uruguay in March 1991. Regional integration in the Mercosur block and general

economic reform in the member countries have quickly changed the competitive environment in Mercosur. Mercosur has faced many challenges to fully implement the common market. Regional integration has occurred gradually, as the Treaty established a timetable for tariff reductions and the harmonization of macroeconomic and sectoral policies as well as legislation; full results have not yet been reached. Increased intraregional trade flows and regional business strategies show integration has progressed.

The region's economy is also more integrated with the world economy because of globalization, and changes in the global food economy are mirrored in Mercosur's. Two factors drive globalization. The first are technological advances in transporting, preserving, and storing products as well as managing and exchanging information. The second is policy and institutional change—trade liberalization, financial market deregulation, growing acceptance of foreign direct investment and foreign firms, the growing protection of intellectual property, and the rise of competition and consumer protection laws.

The sudden exposure to liberalized markets and the accompanying deep institutional change constituted a powerful shock to the food and agricultural sectors in Mercosur countries, as those sectors had been subsidized, controlled, and protected as part of governments' import substitution strategy before the 1990s.

This article focuses on how the food industry in Mercosur responded to the market and institutional shock of globalization. The first section discusses the context of the development of Mercosur, and how globalization affected it. The rest of the paper then focuses on Brazil as a case study of the largest country in Mercosur, with majority or near-majority shares of Mercosur's GDP, population, and trade.<sup>1</sup> The second section describes structural changes in Brazil's food and agricultural sectors with the advent of globalization and liberalization in the 1990s (contrasting them with the prior situation). The third section focuses on business strategies in the Brazilian food industry in the face of these changes. The fourth section concludes by examining major risks and opportunities for new investments in Mercosur, and managerial implications.

## **THE CONTEXT: MERCOSUR AGRIFOOD TRADE DEVELOPMENT**

### **Growth in Trade**

The growth of intra-Mercosur trade flows has been rapid. Until 1990, the average share per country of exports to other Mercosur countries in total exports was 10%; by 1994, the average was 20%, and by 1998, 25% (Table 1). In volume, intrablock trade flows trebled in seven years. Overall exports from Mercosur countries grew 140% from 1990 to 1998, or 13% a year (Table 1)—that is, in the period after

Table 1. Socioeconomic Indicators of Mercosur

	Argentina		Brazil		Paraguay		Uruguay		Mercosur		98/99 (percent)
	1990	1998	1990	1998	1990	1998	1990	1998	1990	1998	
Total population (1,000 hab.)	32,527	36,125	148,030	165,473	4,219	5,223	3,094	3,239	187,870	210,060	12%
Total GDP (1990 U.S.\$million)	153,215	242,764	435,457	529,988	6,271	7,538	8,355	11,348	603,299	791,640	31%
GDP per capita (U.S.\$ of 1990)	4,710	6,720	2,941	3,202	1,486	1,443	2,700	3,503	3,211	3,768	17%
Consumer price index (percent)	2339	0.9	2930	3.0	38.2	11.5	112.5	10.8	—	—	—
Total exports (U.S.\$1,000,000)	12,353	27,338	31,414	51,152	1,062	1,338	1,730	3,036	46,560	82,865	78%
Total imports (U.S.\$1,000,000)	4,078	32,521	24,927	63,313	1,348	3,403	1,317	4,817	-31,670	104,055	229%
Intra-block exports/total exports/total (percent)	14.8	34.2	4.2	17.4	35.7	53.8	34.4	53.1	8.9	24.8	—
Intra-block imports/total imports/total (percent)	21.5	24.9	10.8	16.4	39.6	55.9	40.9	39.6	14.6	21.4	—

\*Data of 1997. \*\*Data of 1997 for Argentina, Brazil, Uruguay, and of 1996 for Paraguay.  
Source: Central Bank and Secex.

trade liberalization. Thus, despite growth of trade within the block, trade with partners outside the block is still much more important—only 17% of Brazil's and 34% of Argentina's exports go to Mercosur. These figures suggest that rather than diverting trade, Mercosur's "open regionalism" has created trade.

But it can be hypothesized that the net effect on trade diversion or creation is theoretically ambiguous. The shifts of the members toward their comparative advantages after reform and integration has partially diverted trade from international markets towards the block, offset by the pursuit of economies of scale and scope by businesses in member countries to be competitive for increased trade on world markets (Chichilnisky, 1992). The net effect has not yet been examined empirically in Mercosur. Yet to date, the dominant perspective among the members is of a zero-sum game that leads to frequent conflicts and retrogressions that have marked the evolution of Mercosur. Reform and integration has not been a one-way street. Regional specialization provoked painful adjustments in members' economies—which occasionally provoked protectionist reactions. Those steps backward are dangerous because they threaten further intrablock integration and discourage agrifood businesses from "going regional."

Trade growth has combined with a second factor to cause deep restructuring of the members' agrifood economies: the countries have also undergone stabilization programs to curb long-term inflationary pressures and to correct overvaluation of currencies (Zylberstajn and Jank, 1996). The reforms and subsequent development processes of Brazil and Argentina have strongly affected the overall character of Mercosur, given their preponderant weight, and given that both had very closed economies before reform. Both followed strategies of import substitution before the reforms, including high levels of market protection, pervasive state participation in and control of the agrifood sector, and interest groups well organized to defend those policies. These policies resulted in a complex and very integrated agro-industrial system that was challenged by drastic trade liberalization, first in Argentina (as in the disintegration of milk clusters in Brazil, see Dirven, this volume) and more recently in Brazil, as discussed in the next section.

### **Constraints to Integration**

The most important challenges to Mercosur consolidation are as follows. First, the tax structure of the country-members is far from being consistent, resulting in biased competitive advantage. The heavy tax burden on the Brazilian agribusiness systems, including some windfall taxes, has hurt competitive advantage, not only in Mercosur but also in global markets. However, Argentina has increased taxes to meet public deficits, as was done in Brazil.

Second, exchange rate policies have a direct impact on trade patterns and continue to disequilibrate intraregional trade and create difficulties for the

implementation of common external tariffs. The recent devaluation of the Brazilian currency (the real) and the Mercosur crisis that followed is testimony to this unstable equilibrium.

Third, common external tariffs can determine the global trade volume and investments in Mercosur. The most important difficulty is related to the current average tariff level among country-members. This average tariff results mainly from the industrial policy of each country. Currently, Brazil's average tariff is 14%, while Argentina's is 10% and Paraguay's is zero, which explains why Paraguay has been an important door for Brazilian coffee and soybean and Argentine cigarette contraband.

Fourth, infrastructure integration is still very poor in Mercosur, because of a historically low level of trade among the country-members. Harbor duties and other harbor costs are much higher than the international standards as a consequence of regulatory practices and government monopolies. Only seven years ago, in Mercosur countries, all infrastructure services were provided by state companies. The privatization of public utilities is now changing the landscape and opening a vast opportunity for investments.

Fifth, so far, the member countries have not built a common regulatory apparatus, such as antitrust policies, consumer protection laws, standards of health and hygiene requirements for food products, and packing and trade regulations. Brazil has the longest experience of antitrust policy enforcement and is the only member with a merger and acquisition law. Also, the Brazilian Consumer Law is the tightest and Brazilian corporations have been adjusting to its requirements. Very recently, there has been movement, albeit small, towards the harmonization of regulations concerning competition and consumer rights. Also, the hygiene and sanitation requirements are still rather unbalanced. Grades and standards on packaging and additives are different and provide a source of protectionism. National certification is not accepted within the common market. Once again, Brazilian rules are the most severe, though the government's reputation for monitoring and guaranteeing standards is very poor. This is not the case of Uruguay's system of quality standards, which is internationally renowned.

## **STRUCTURAL CHANGES IN THE BRAZILIAN AGRICULTURAL SECTOR**

Brandão and Carvalho (1980) and Dias and Amaral (1999) note that in the 1970s, the Brazilian economy was highly protected as part of the import-substitution model of development. Brazilian agriculture grew quickly, supported by minimum prices and government procurement, and spurred by a rapid increase in the use of agricultural machinery and by subsidized credit. Agriculture received net transfers that amounted to 8% of the agricultural GDP. Subsidized rural credit and

declining relative prices (agricultural relative to industrial) benefited both the mechanical and chemical input industry and the food industry. The agricultural sector became an important market for industrial goods and, at the same time, provided cheap raw materials for downstream food and fiber industries. Those downstream industries were highly protected with high tariffs.

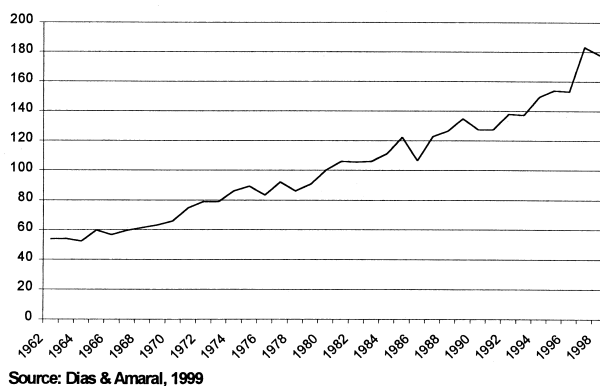
Policy created two groups of agricultural products: internal market products and export products. While the prices of the former were determined by domestic supply and demand, the prices of the latter were determined in world markets. Sectoral regulations and barriers to trade created and preserved that distinction. Through the 1980s, agricultural policy protected “domestic market products” at the expense of export products, to guarantee an adequate real wage for the industrial sector.

In the 1970s and 1980s, the rural credit system was not merely financial—it provided a coordination system that oriented food supply policy—including minimum prices, government procurement, and storage—to achieve the objective of low-priced food and constrain inflation. As inflation increased, interest rates became negative, thus increasing subsidies.

The government’s capacity to finance transfers and subsidies to agriculture declined with the second petroleum shock in 1979 and the Brazilian external debt crisis in 1982. Inflation grew from 40% in 1980 to 200% in 1984 and a negotiation with the World Bank and the IMF became unavoidable. The traditional recommendations of tight monetary policy and public deficit reduction at the macroeconomic level were accompanied by World Bank credit support to several sectors, conditional on deregulation, including price liberalization.

Economic policy reform was concentrated in 1987 through 1992. For more than 20 years the Brazilian government had been pervasively involved in the economy in production, infrastructure, public services, and regulation. Since 1988, trade liberalization, deregulation, and privatization threatened Brazilian companies’ established positions, requiring new strategies to foster competitiveness. Credit subsidies were cut, minimum prices and government procurement of food products were eliminated, tariffs were reduced, trade direct (quantity) controls and export and import licenses were eliminated, customs procedures were modernized. The remaining restrictions apply to health, food safety, and animal and agricultural diseases. Among agrifood items, the tariff reduction schedule set the lowest level of protection (0–10%) on chemical inputs. The greatest protection was kept for tractors and equipment (30%). Dairy and sugar received higher tariffs (20%), while cotton had no tariff other than an export prohibition to favor the textile industry. Consequently, Brazil became a net cotton importer after having exported for many years.

Surprisingly, during the transition to a freer economy, agricultural production has kept on growing (Figure 1), with increasing productivity, without the

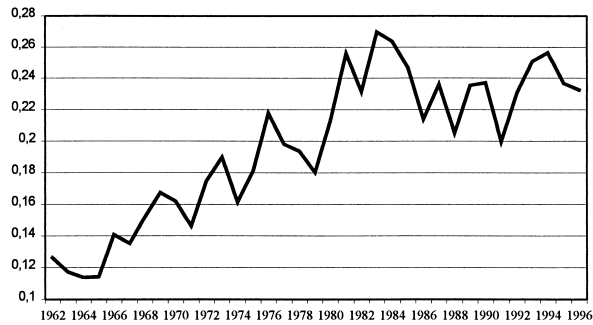


**Figure 1.** Agriculture and Livestock Production Index 1962–1998  
(1996 = 100)

adjustment crises seen elsewhere such as in Argentina. The reason for the continued growth of agricultural production can be found in agroindustrial growth. The inputs industry as well as agrifood commerce and the food and fiber processing industry began to finance the agricultural sector, assuming the role of system coordinator, a role previously performed by the State. Contrary to expectations, the private financial sector did not take on this role, causing the productive sectors to enter activities in which they had no expertise, generating one of the main threats to the new model: breach of contract. Only recently have new commercial instruments begun to emerge, mediated by the financial system.

At the same time, the terms of trade improved for farm products, due, among other factors, to trade liberalization, beginning in the farm input market. From 1987 to 1998, the increase in the purchasing power of agriculture and husbandry grew around 59%, combining improved terms of trade (31% on average) with productivity gains (22% on average).

Following economic reform, food sector trade deficits increased for several reasons. (1) Farm input imports increased as did imports of consumer goods spurred by higher incomes. (2) Exports did not grow as quickly as expected—and even stagnated. The ratio of exports/production, after 20 years of steady growth, reached a plateau of around 20 to 25% during the second half of the 1980s, and has declined slightly following the policy reforms—despite the modernization effort (Figure 2). (3) Productivity and prices of products for the domestic market have grown more quickly than those for exports. While land productivity grew quickly between 1987 and 1998 (1.85% per year for crops and 1.94% for livestock), the growth was fastest in staples (rice, corn, beans), and in livestock. While domestic product prices were pulled up by fast-growing consumer demand, export and import-substitution sectors were exposed to trade liberalization and thus downward pressure on prices. (4) Most Brazilian food companies are only

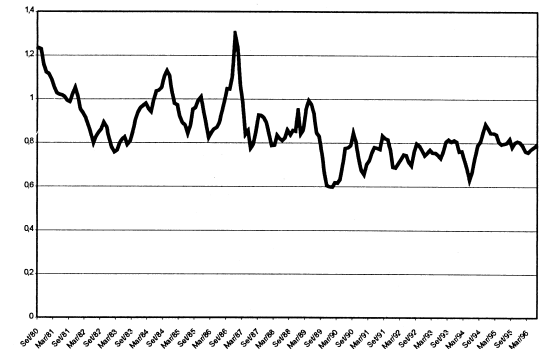


Source: DIAS & AMARAL, 1999

Figure 2. Export Coefficient Evolution 1962–1996 (%)

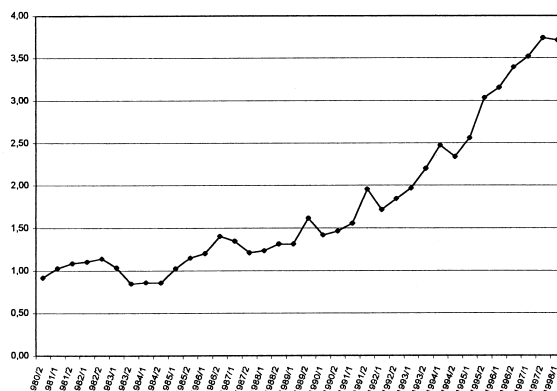
residual exporters, even in the case of leading firms. The latter even tended to shift toward attention to the growing domestic market after the 1994 macroeconomic stabilization program (Farina and Azevedo, 1999). Agricultural exports also suffered with the systematic exchange rate overvaluation, which also hurt processed food exports, mainly after the Stabilization Plan.

The trade deficit persisted even after the Brazilian exchange rate devaluation in 1999. This caused concern, which led to the creation of competitiveness fora, based on the concept of supply chains and headed by the Development and Trade Minister. Together with APEX (the Export Promotion Agency) the fora are expected to improve export performance—with the opening of international offices, promotion of the *Made in Brazil* label, the pursuit of global market opportunities and consistent export strategies, and the addressing of distributive conflicts within chains.



Source: DIAS & AMARAL, 1999

Figure 3. Evolution of Marketing Margins—Farm Gate Index/Food Retail Price Index 1980–1995

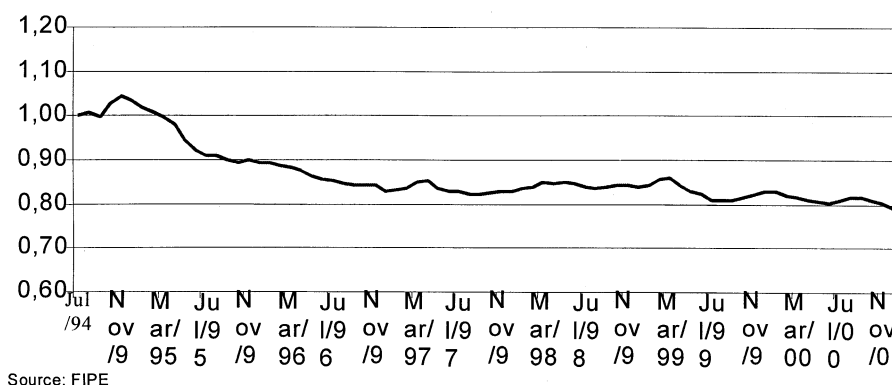


Source: DIAS & AMARAL, 1999

**Figure 4.** Urban Wages/Food Prices 1980–1997

Food industry profit margins have been squeezed by liberalization and monetary stabilization policies, with margins lower in 1990–1998 than in the second half of the 1980s. The prices of processed foods fell 30% between 1994 and 1997, driven by the intensification of competition among local food companies, by the growing market power of retailers (especially supermarket chains) and by processed food imports.

A crucial point is that domestic food demand has grown quickly over the past decade, driven by rising incomes. Figure 4 shows a systematic ascending ratio of urban wages to food prices. The stabilization program caused a modest improvement in income distribution (the Gini coefficient went from 0.601 in 1993 to 0.565 in 1995). Those who benefited most were the poorest 20% whose monthly income almost doubled. At the same time, the food real price declined, favoring the lower income classes.



Source: FIPE

**Figure 5.** Brazilian Food Real Price Index

**Table 2.** Brazil: Real Sales Volume Growth—1993/1997

	1997/93 (percent)	Growth rate/year (percent)
Processed Foods		
Dry pasta	24.82	5.5
Ham	111.59	20.5
Hamburger	154.95	26.3
Fruit juice concentrate	113.30	20.8
Biscuit	80.46	15.8
Tomato paste	48.24	10.2
Tomato sauce	87.20	16.9
Margarine	24.92	5.7
Olive oil/salad oil/cooking oil*	7.16	1.7
Beef**	13.23	3.1
Poultry**	35.18	7.8
Pork**	21.92	5.1
Dairy		
Ready-to-eat-dessert	124.95	22.5
Yogurts	212.60	32.9
Petit suisse cheese	167.93	27.9
Flavored milk	260.47	37.7
UHT fluid milk*	134.59	23.7
Condensed milk	66.98	13.7
Powder milk	35.95	7.8
Baby formula milk*	102.06	19.2

Source: Nielsen. \*1995 first column \*\* source Anualpec-FNP (1998).

The immediate effect was twofold: (1) a general increase in food demand, and (2) a recomposition of demand towards protein and value-added products, especially dairy and meat, which have elastic demand. For an average 30% increase in real incomes, frozen food, yogurt, dairy desserts, and *petit suisse* cheese demand grew more than 80%; processed meat, juices, and vegetables grew more than 30%. (However, the value of gross sales of processed food increased only 18%, because of a decrease in food prices.) As a consumer trend in Brazil and in Mercosur in general, there is also a small but fast-growing demand for services-added food, associated with greater quality, nutrition, health, and environmental sustainability. The increase in demand for processed as well as prepared food is partly driven by an increase in the opportunity cost of women's time, as they enter the away-from-home workforce. In 1971, 23% of Brazilian workforce were women, while by 1997–1998 that figure had climbed to 40%. In 1971, the average time of meal preparation was 2 hr, decreasing to 15 min in 1997–1998.

Since 1996, the Brazilian economy grew more slowly than expected. Even so, the average growth rate of food consumption in 1993–1997 was extremely high, especially when compared to developed countries (Table 2). Despite this improvement in Brazilian food consumption, the Argentine and Uruguayan *per capita* consumption is still much higher, especially for protein foods.

While protein intake is 99.3 gr. *per capita* in Argentina, Brazil's is 65.9. Consequently, Brazil still has great potential for increasing and diversifying food demand, compared to EEC countries and the U.S.

The Brazilian food market is huge and has the potential to grow further, quickly, as discussed below. Part of this increase has been met by imports; whereas only 10% of Brazilian exports to Mercosur are in food products, 31% of Brazilian imports from Mercosur are food products. Indeed, growth potential of the Mercosur food market is concentrated in Brazil. The Brazilian *per capita* GDP is lower than that of Argentina and Uruguay and the income distribution is the worst in the sub-region. This implies potential for a growing food demand, as is corroborated by the food demand increase in the 1990s, shown in Table 2.

The food industry and food retailing strategies are geared to and reflect the investment opportunities arising from the market development discussed above. Most Argentine and Uruguayan investments were stimulated by access to the Brazilian food market, not only in the dairy sector but also processed food.

## FOOD INDUSTRY RESTRUCTURING AND AGRIBUSINESS STRATEGIES

### Investment Strategies

There has been substantial foreign direct investment in Mercosur food industries. There has been substantial investment from outside Mercosur in Mercosur. The growth potential of the food market has attracted new investments from multinational companies. Acquisitions have been the most common strategy to grow and enter new markets.

Moreover, despite Mercosur's stop-and-go integration process, more than U.S.\$ 3 billion over 1994 through 1998 were invested by 458 Brazilian companies in Argentina and by 322 Argentine companies in Brazil. Food, chemical, and automotive industries are among the most integrated. Brazil has become the main market for exports of key branches of the Argentine food industry, such as dairy and wheat products. The growth of Argentine exports to Brazil has stimulated investment, organizational change, joint ventures, and strategic partnerships to improve the information and knowledge of the Brazilian food market structure. An analogous process has occurred for Brazilian companies with respect to the Argentine market.

Strategic alliances and joint ventures have changed the competitive environment in Mercosur. Argentine companies have invested heavily in Brazil, acquiring Brazilian firms or building their own plants and distribution systems. Many Brazilian companies are investing and looking for partnerships in Argentina and Uruguay, resulting in real business integration. Also, the fast-food companies'

supply strategy has already adopted a Mercosur dimension. The cheddar cheese produced in Brazil for McDonald's and a recent frozen potato plant in Argentina will supply all the McDonald's restaurants in Mercosur.

Investments in new capacity have also increased, with most of those in the Mercosur oriented to the Brazilian market. The acquisitions and mergers have been followed by the adoption of modernization and quality assurance processes in the acquired firms, improving competitiveness and expanding capacity.

The immediate consequence of these new investments and entries in the food market has been an increase in competitive pressure, resulting in lower prices (Figure 5), a larger number of products, increasing market segmentation, and differentiation. This also had the effect of increasing the concentration ratio and the degree of "internationalization" (foreign ownership) (see Jank et al., this volume).

The capital movements in Mercosur are as important as the trade flows in understanding the integration progress. Capital movements are less sensitive to short-term movements of exchange and interest rates and more responsive to long-term institutional changes. The Asuncion Treaty and subsequent agreements are important to the establishment of the new rules of the game, though they are still incomplete and far from representing agreement on important aspects.

The flaws in the institutional framework have stimulated protectionist strategies inside the block, creating nontariff barriers to trade flows. For example, there has been a "potato war" between Brazil and Argentina, based on Brazilian legislation that regulates the use of agrochemicals. Brazilian producers have succeeded in creating a health barrier to Argentine exports, thus protecting national suppliers. Also, beer circulation has been restricted by Brazilian legislation, which regulates the additives in food and beverages. The protectionist behavior will only fade as the institutional rules consolidate and the nontariff barriers can no longer be used as an anticompetitive device.

### **Concentration in Retail: The Rise in the Power of Supermarket and Fast-food Chains**

Food prices (relative to nonfood prices) have declined almost 40% from 1994 to 1997 in Brazil and have not increased since then, despite the 1999 Brazilian exchange rate devaluation. These price decreases have been driven by economic stagnation and retailers' market power, which prevented increases in the prices of imported inputs from being transmitted to consumers.

Brazilian food retailing has become more concentrated than the processing segment. As in the food industry, mergers and acquisitions were the main path for concentration and denationalization. By 1999, of the 10 largest supermarkets, four were multinationals and one had formed a partnership with an international

company; in 1994, there was only one multinational firm among the top 10. Moreover, the role of supermarkets in food distribution has increased and now covers 72% of food consumption expenditures in Brazil. The consequence of those changes is that supermarkets have attained higher market power to negotiate prices with food processors and wholesalers, and to impose their own standards. But international retailers have also spurred the modernization of Brazilian retailers. Heavier competition has reduced supermarkets' operational margins and fostered new patterns of competition.

The fresh fruits and vegetables (FFV) department has become a factor of differentiation and profit recovery for supermarkets. However, its management is particularly complex because of the absence of standards and uncertainty in supply. The larger supermarkets have made formal or informal agreements with wholesalers, which sometimes include supply management and waste control. Waste has been enormous in FFV market channels and for that reason waste control can provide an important source of gain. Wholesaler firms are responsible for both the produce within the stores and supply chain management. Agreements with wholesalers enable the supermarket to reduce risk and increase product quality and the wholesaler to add service and margin to his traditional business. Frequently, market risk is transferred entirely to the wholesaler, who is paid only for the quantity actually sold, and the price negotiation is strongly based on the spot market. Consequently, most wholesalers prefer to supply small and medium supermarkets and open-air merchants, opening an opportunity for those firms to survive, despite the market power of leading retailers.

### Market Segmentation Strategies

Market segmentation strategies have been based on the quality dimension, and new consumer trends associated with health, nutrition, and convenience. Pre-prepared and frozen food sales have grown 20% annually, while sales of *diet* and *light* products have grown 26% per year since 1990. The share of vacuum-packed milk in total consumption of fluid milk increased from 4% to almost 70% over the 1990s.

To put in place a segmentation strategy based on quality and cost control, the food industry and food services have changed upstream relationships. Formal or informal contracts have been adopted between the food industry and suppliers. Those contracts establish different prices according to scale, quality requirements, and crop, harvest, and postharvest practices. The process has already been important in poultry and pork breeding and is now extending to the milk, orange, coffee, and horticulture subsectors. Food service companies, mainly in fast food, have stimulated important changes in production and management practices in both the processing and the raw material segments, to meet standards (Farina and Machado, 1999).

### Collective Action

Market segmentation has become an important alternative for small and medium firms, which cannot compete against the largest firms on the basis of price. However, these individual strategies required a strong effort of collective action to support them. For example, organic products have become an important, though challenging alternative, mainly based on small producers' consortia. Geographical denominations such as *Café do Cerrado*, and high quality pre-prepared food have represented important niches for survival.

Substantial cooperative action has been necessary to implement those strategies and to lobby for the needed legislation. Organic products and origin denomination still lack adequate legislation and enforcement. The Association of Café do Cerrado (CACCCER) has been important in obtaining those changes and also in developing the culture and expertise among coffee growers to supply high quality and special coffees (Farina, 1994a). By the same token, ABIC—the coffee roasters association—has developed collective strategies to regain consumer confidence in Brazilian coffee and also to foster the consumption of specialty coffees (Farina and Saes, 1998).

Although collective action has been important in coping with new competition, Brazilian farmer and processing cooperatives have faced a loss of reputation among rural and industrial producers as well. Most new collective strategies are based on associations and consortia. Successful strategies based on market segmentation and product differentiation depend on new governance structures that guarantee quality, regularity, and competitive prices. In the Mercosur context, the identification of suppliers is not constrained by national frontiers and there has been real competition among the production systems of the four countries.

Collective action has also been used in the marketing segments. On the one hand, the most dynamic wholesalers have implemented new strategies to keep their best clients, such as the creation of associations to supply small and medium supermarkets. Without formal contracts, the retailer is guaranteed a regular supply at competitive prices and the wholesaler keeps its market-share. This strategy reduces waste and benefits both retailer and wholesaler (Farina and Machado, 1999).

On the other hand, small and medium supermarkets have acted cooperatively through their union (SINCOVAGA) to make viable the adoption of electronic supply chain management such as EDI and ECR (a project technically supported by the University of Sao Paulo). They also have tried to adopt a “neighborhood store strategy,” avoiding direct competition with the largest supermarket chains. To cope with the market power of larger retailing chains, the food industry has given some support to small and medium retailers' strategies, in collaboration with the SINCOVAGA project.

## IMPLICATIONS: NEW COMPETITION PATTERNS AND MERCOSUR PERSPECTIVES

The increasing competitive pressure in the Brazilian economy has led the food and agribusiness system to adopt quality management procedures to reduce costs of logistics, production, and distribution. A second target is consumer recognition and willingness to pay premium prices. As the Brazilian government has lost reputation in these areas, the private sector has adopted mechanisms such as private quality certification and traceability.

Despite the difficulties discussed above for the integration of Mercosur, many investment opportunities have been appearing for agribusiness, especially related to such products for which there are complementary characteristics. The capital goods and food industries have been investing in plants across the country-members or forming joint ventures. These cross-operations allow for scale and scope economies, and for tracking consumer preferences and supplier trustworthiness. However, the investment risks are still high because of recurrent crises within the block caused mainly by macroeconomic instability. Joint ventures, strategic alliances, and direct investments across member-countries create a favorable environment for institutional and economic harmonization because of the main players' interests.

The new competition patterns that came with growing regional integration and globalization have required adaptation by the Brazilian firms. Most of the leading Brazilian companies were sold. The remaining companies not only have to adjust costs but also must adopt quality and cost, not only for their own products but also for their suppliers' products and management practices. Small and medium firms have found successful strategies in niches and specific market segments. Many of these strategies have been supported by collective action by associations, consortia, and to a lesser extent by traditional cooperatives.

## NOTES

1. Brazil's population is 78% of Mercosur's population, its GDP is 62% of the region's GDP although it has only half the per capital GDP of Argentina and the worst income distribution (Table 1); Brazil's exports are 62% and its imports 60% of the Mercosur totals, and 43% of intrablock exports and 46% of intrablock imports are Brazilian.

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