EXECUTIVE SUMMARY

CHANGING AGRIFOOD DISTRIBUTION IN ASIA - KEY DRIVERS

The Asian agrifood marketplace is undergoing a transformation. Asia's traditional system of agrifood distribution is being rapidly left behind, being overtaken by a new network of modern food retail and foodservice outlets and giant shopping malls which are creating their own supply chains and distribution systems.

Among the key drivers of change in Asia's agrifood distribution systems are:

- Economic growth and per capita income growth
- Urbanisation
- Western cultural and commercial influences
- Asian economic crisis
- Western FDI in Asian Distribution Systems
- Continued growth in intra-Asian trade and Asia's trade with the world
- Globalisation of logistics and distribution services
- Asian agrifood distribution companies aiming to lift competitiveness

GLOBALISATION OF FOOD AND BEVERAGE RETAILING

Several key factors have set in train the beginning of a pattern of globalisation in food and beverage retailing since the 1970s. But the principal element has been increasing consolidation of food retailing in Western Europe and the USA, leading to the emergence of a number of major players with global ambitions. With the intensifying competition in food and beverage retailing, and maturation of their home markets, such consolidation is bound to continue, as the increasing minimum size required for profitable economies of scale point to mergers and acquisitions, and global expansion as the most logical way to survive.

However the "globalisation" of food and beverage retailing started much more recently and is at a far less advanced stage than agrifood processing, or many other industries. An examination of the global presence of the leading North American and European players reveals that only one third of them yet have any presence outside North America or Europe. All of the leading North American and European global food retailers still derive the greatest share of their turnover from operations in Europe and/or North America.

Most US food and beverage retailers remain heavily concentrated in their home US market (perhaps with some outlets in Canada), and are just beginning to advance into Latin America, Europe and Asia. Wal-Mart is the only US food retailer with substantial international operations (operations in Europe in Germany and UK, in China, ROK and Japan in Asia, and in Mexico and three other Latin American countries).

On the other hand, most of the leading European food & beverage retailers have established operations in several countries outside their home market. Some of the biggest have concentrated on expanding only into Western and Eastern Europe at this stage; but several have established a sizeable presence in the US market. Notably, it is the European players which have been the leaders in expanding into Latin America and Asia, especially Carrefour and Casino Guichard-Perrachon of France, Royal Ahold and SHV Holdings/ Makro of the Netherlands, Belgium's Delhaize Group and the UK's Tesco, and more recently Germany's Metro.

Accompanying the process of consolidation among major food retailers is increased segmentation of food retailing into several key formats, with each major retail chain making a strategic decision about which one or more formats to focus on. Of the three main food retailing segments (mass, low cost vs medium price vs premium), it appears that the biggest growth in food sales is taking place at the mass low-cost food retailers, in the format of hypermarkets and discount warehouses. There is also reasonable growth in the premium food retailing format (premium supermarkets, food sections at department stores). But medium-price formats like traditional supermarkets are suffering significant loss of market share.

KEY EFFECTS OF GLOBALISATION OF FOOD AND BEVERAGE RETAILING

The globalisation of food & beverage retailing is bringing about historic change in the agrifood supply chain. Among the most significant effects are:

- massive increase in purchasing power of the global retailers;
- marked reduction in the number of suppliers used by fewer, larger global chains;
- movement by retailers from less local sourcing towards more regional and global sourcing;
- increasing utilisation of house brands/ private labels by the retailers;
- a significant shift in the weight of agrifood industry power away from the agrifood processors towards the food & beverage retailers.

IMPACT OF GLOBALISATION OF FOOD AND BEVERAGE RETAILING ON ASIA

Asia has seen significant development of more modern food retailing in recent decades, particularly since the 1980s. Until recently however, this food retailing modernisation process has been primarily initiated and driven by Asian retail companies, led by the Japanese retailers. It was not until the late 1980s and early 1990s that the first Western food retailers sought to establish a presence in Asia, in response to the region's accelerating per capita income growth and expansion of Asia's middle class.

With the advent of the Asian economic crisis, many Western food retailers, like the Western agrifood processors, quickly perceived that the drastic reduction of real estate and other asset prices provided a unique opportunity to buy into the region's retailing structure at low prices. Those already present like Carrefour, Royal Ahold, Wal-Mart, and Casino Guichard-Perrachon, as well as Dairy Farm International (part of UK's Jardine Matheson group), accelerated their planned investments in the region, often increasing their shares in existing joint ventures or buying out their Asian partners. Others not yet present, such as Delhaize, Auchan and Tesco, made their first investments during this period.

However, while the leading Western food retailers are gradually increasing their presence and, most importantly, market share, they are by no means yet dominant, though they are seeking to become so. Also, while there is growing success by some leading Western retailers, there have also been casualties among their ranks, with several having cut their links with one or more Asian market at some stage. So if one speaks of globalisation of food and beverage retailing in relation to Asia, one must say that the process is only just beginning, with the greatest changes yet to come.

Modernisation of food retailing has only recently started to take firm hold in many parts of Asia outside of Japan, Singapore, Hong Kong, and a few other cities. Moreover, consolidation of the Asian food retailing sector is also still only in the very early stages. While several Western retailers have acquired shares in some Asian food retailing operations, or even purchased them outright, there have not yet been any really large-scale mergers or acquisitions either among Asian food retailers (apart from some government-managed mergers in China), or between Western and Asian food retailers, to form a significantly larger global food retailer with a strong presence across Asia. Yet this is likely to become more of a possibility as competition among food retailers heats up further across the region.

At the same time, the arrival of the Western MNC food retailers has brought the start of irreversible change to the Asian food retailing sector. The Western MNC food retailers are steadily introducing their own global operating systems to the sector. From their expectations and requirements of suppliers, active supply chain management and establishment of modern transport and distribution systems, use of IT throughout corporate operations, through to pursuit of economies of scale and competitive standards of efficiency, strong customer focus and fiercely competitive pricing practices, they are establishing new performance benchmarks for food distribution and retailing across the region. These new benchmarks are being reinforced by the fast changing expectations of Asian consumers.

Moreover, as the MNC food retailers strengthen their presence in Asian markets, and link their Asian operations more closely into their global networks, they are also incorporating Asia more firmly into their global sourcing and purchasing network. Thus they are sourcing more from Asia, not just for their stores in Asia but for their entire chains.

ASIAN FOOD RETAILING SECTORS AND KEY ASIAN PLAYERS

In just the past five years, Asia has experienced the beginnings of a real revolution in its food retailing, a revolution which is likely to keep accelerating. This is occurring in the context of a transformation of Asian retailing in general, with a proliferation across the region of modern retail formats and giant shopping malls.

Japan and other advanced economies of Asia, principally Hong Kong and Singapore, have long had modern retailing formats, but major changes to food retailing only started around the 1960s and 1970s, with the advent of supermarkets and convenience store chains. The Japanese version of the European department store which includes a special section for food and beverages, had an early influential impact in most of Asia. Leading local conglomerates in most of Asia who were the dominant urban real estate holders (or SOEs in the case of China and Vietnam) followed suit by setting up their own department stores. The Japanese adaptation and improvement of the US convenience store format (demonstrated in particular in the form of the 7-Eleven chain purchased by Japan's Ito-Yokado in 1991) also started to be emulated. With the onset of significant economic growth in developing Asia in the 1980s and 1990s, and the first arrival of Western-style supermarkets and wholesale stores, the same local conglomerates started setting up their own chains of supermarkets and wholesale cash & carry stores, usually taking on a Western retailer as a technical adviser or minority partner. The regulatory environment in all of Asia maintained significant restrictions or prohibitions on foreign investment in distribution and retailing, and importantly also in land ownership, which allowed local players to control the pace of change and level of efficiency in the sector.

The Asian crisis changed the rules of the game irreversibly. The plunge in real estate and other asset values, and high levels of gearing pre-crisis, forced many Asian conglomerates involved in food retailing ventures, especially in the ROK, Thailand, Indonesia and the Philippines, to scale back and often sell down partly or completely their equity in their various joint ventures to their foreign partners. Most Asian governments came under pressure to further deregulate distribution and retailing from a combination of: pressure for reform and deregulation from the IMF and Western countries; from the importance for economic growth of reviving domestic consumption and of more efficient distribution and retailing; and from the benefits for consumer welfare of lower prices, especially for food and other basic necessities.

Thus a battle for survival and shakeout of industry players, local and foreign, is well underway across the region. Traditional mom & pop stores in almost all markets have a falling share of total food sales, making a shrinkage of their numbers inevitable, though this change is much slower in South Asia, Burma, and parts of Indo-China, and with some surviving by transforming themselves into convenience stores, usually under a chain banner. In the region's higher income economies like Hong Kong and Singapore, wet markets are falling by the wayside as they are increasingly being replicated in modernised form as fresh produce sections inside supermarkets and hypermarkets. In general, hypermarket and convenience store chains are proliferating faster and doing better than supermarket chains, though with some exceptions.

Japan is starting to see some rationalisation and consolidation of its numerous convenience store chains, while it is still a fast growing format in most of East Asia, including importantly as an attachment to petrol/gas stations ("gas marts"). A substantial shakeout is underway among Japan's supermarket chains, with a number of chains either going under or being obliged to radically restructure, and some or all of their stores being absorbed by other players (such as Daiei, Mycal and Kotobukiya). At the same time, others have maintained profitability and are continuing to expand, such as Ito-Yokado and the Aeon/Jusco group. In Japan, there are still at least five major food retail chains each with annual food and beverage sales of over US$5 billion, and at least another dozen with food and beverage sales of over US$1 billion per annum. Japan's Ito-Yokado, with an annual turnover of over US$28 billion, owns the world's largest conveience store chain (7-Eleven), with 23,000 stores worldwide.

In the rest of Asia, a similar shakeout is underway. Challenged by the Western retailers, some Asian players have given some ground, especially during the Asian crisis. But many are stepping up their modernisation efforts and working to achieve the new benchmarks set by the Western chains, in order to hold their own. In most Asian markets, there are still several significant local players in each, such as ParkNShop in Hong Kong, LG Mart in Korea, President Chain Store in Taiwan, NTUC Fairprice in Singapore, and the Hero and Matahari supermarket chains in Indonesia. Since the onset of Asia's economic slowdown, and of heightened price consciousness in Asia's middle class consumers, Asian retailers have been more closely observing and learning from the Western chains, in a determined effort to improve their competitiveness and enhance their chances of survival.

GLOBALISATION OF FOODSERVICE – FAST FOOD

In the world's developed markets, the long standing trend towards more eating-away-from-home and home delivery of prepared meals continues to grow, driven by a wide range of factors, and along with it, the growth of large companies meeting these consumer requirements on an increasingly organised and consolidated basis. The growing pattern of organised foodservice is characterised by: chains of outlets using a uniform brand identity; centralised procurement of supplies; focus on quality, standardisation and safety from suppliers; uniformity in product menus across outlets; uniform taste; existence of strong controls; and the use of technology. But with the growing maturation of developed country foodservice markets, the major players have looked increasingly to developing markets for their future expansion. Some fast food chains have focused particularly on Asia in their global expansion strategies. For example, McDonald's, KFC and Pizza Hut all have more outlets in Asia than in Europe.

The USA, with the world's largest economy and its own particular cultural trends, has been the leader in the concept of large-scale organised fast food (or QSR segment – quick service restaurants) and produced the leading global fast food chains, most notably McDonald's, KFC, Pizza Hut, Burger King, Wendy's, Domino's, and so on. While the US chains have been the leaders in international expansion in foodservice, the US market (with retail sales of around US$110 billion in 2000), yet remains core to their operations and earnings. However, the maturation of Western fast food markets, particularly evident in pioneer fast food formats like hamburger chains, is giving greater importance to strengthening sales for such chains in markets outside the USA.

Also, changes in Western fast food markets, such as more consumer interest in healthy fast foods, are giving rise to newer fast food chains such as the USA's Subway (submarine sandwiches). This has been accompanied by the increasing spread of "café society" culture, stimulating growth of numerous café chains, from the US pioneers like Starbuck's, to European chains such as Italy's Lavazza. As a result, most major fast food companies are moving beyond a single fast food chain type and developing a stable of brands to appeal to a wider range of fast food tastes and trends, and introducing these across all major markets, not least in Asia.

Major fast food MNCs are moving towards centralised purchasing of their major raw materials and inputs on either a global or regional basis, in order to maximise their purchasing power. For example, in the mid-1990s, Yum! Brands Inc (KFC, Pizza Hut) consolidated most of its worldwide food and other input procurement activities under a single unit called the Supply Chain Management unit, which sources, negotiates supply contracts, and makes purchases from hundreds of suppliers in a number of countries. The unit also monitors market trends and seeks to identify and capitalise on purchasing opportunities to enhance the company's competitiveness.

GLOBALISATION OF INSTITUTIONAL CATERING SERVICES

The growth of the important agrifood sector of institutional catering and contract foodservice has been driven by the catering requirements of a range of large-scale organisations such as military forces, healthcare and educational institutions, and companies. With the post-WWII growth in scale of such organisations, so has the scale grown of the catering involved. With increasing numbers of organisations finding in-house catering inefficient, costly or of unsatisfactory reliability and quality, the trend towards outsourcing of corporate catering has flourished. With the ever growing scale and increasingly multinational presence of individual companies, the scale and reach of the professional contract foodservice companies capable of meeting their catering requirements has similarly had to grow.

The world's leading institutional foodservice MNC, Compass Group (which specialises in contract and concession catering), has estimated the global institutional foodservice market to be worth almost US$300 billion by 2001, with outsourcing of foodservice growing at around 3-4 per cent pa. It also assesses that still only about 30 per cent of the market is covered by major players, with as yet only two clearly large-scale MNC players: Compass Group and Sodexho Alliance; but it sees consolidation taking place at an increasing pace.

IMPACT OF FOODSERVICE GLOBALISATION ON ASIA

Asia has long had a strong tradition of eating away from home. But only in Japan has the local out-of-home cuisine been transformed into an organised industry, and in Japan there are still a large number of small and medium-sized foodservice companies. In the rest of Asia, single restaurants, small individual food vendors and hawkers have predominated as the purveyors of local cuisine.

But the advent of the US fast food chains from the 1970s and 1980s brought a turnaround in Asian corporate attitudes towards the foodservice sector. Most US and European MNC fast food chains prefer to operate in developing countries through a single master franchisee for a whole country or even several countries in a region, somewhat like the development of "anchor bottlers" by The Coca Cola Company and PepsiCo Inc, though the master franchisee may in turn allocate sub-franchises to a number of smaller operators. Consequently some of the master franchisees can become significant business enterprises in themselves, especially when they gain franchises for more than one well known fast food chain.

Some Asian companies focus just on being franchisees of Western fast food chains, and seek to gain franchises for a stable of well know fast food brands, usually with one in each fast food segment (ie hamburger, pizza, chicken, coffee, etc). But increasing numbers of Asian companies are also seeing the potential for developing their own successful fast food chain concept, either Western or Asian cuisine, and growing it through franchising. This is likely to play a role in driving consolidation in the Asian foodservice market.

In Japan, this has long been the case. .Amidst the fierce competition in the Japanese restaurant sector in the 1990s, it became increasingly clear that an enterprise had to attain a certain minimum scale in order to survive, and by the end of the 1990s, a common goal for the leading chains had become c¥100 billion/ cUS$800m in sales from about 1,000 restaurant outlets. Thus consolidation is taking place in Japan's restaurant industry at an accelerating rate, with the leading chains generally increasing their proportion of total sector sales, while smaller enterprises are losing share.

Global foodservice market leader Compass Group concludes that over 80 per cent of the major Asia-Pacific institutional and contract foodservice market with annual sales of around US$90 billion remains self-operated, and thus offers major opportunities for professional large-scale foodservice companies. Compass and others also expect that while multinational companies are currently the principal customers in Asia for professional foodservices, in future more Asian companies will start to outsource their catering requirements to professional operators. This will be partly driven by employees' demand for better quality and more hygenic food. Another factor will be the price competitiveness against the small-scale food vendors on the part of the leading foodservice MNCs that use global sourcing and bulk purchasing to lower their unit costs. All three of the leading global institutional caterers, Compass, Sodexho and Aramark, have been developing a growing presence in Asian markets, and since the mid-1990s all three have formed joint ventures or made acquisitions in Japan.

CONCLUSION

An historic change is taking place in Asian agrifood distribution systems, change which is likely to accelerate in the coming decade and transform the Asian agrifood marketplace for all players. It will be essential for Australian agrifood suppliers to understand the new Asian marketplace and hone their market entry strategies accordingly.