STRUCTURAL CHANGE IN THE FOOD INDUSTRY: A SURVEY ON THE TRENDS TOWARDS CONCENTRATION*

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ABSTRACT

This article aims to discuss the changes undergone by the world food industry with emphasis on the recent development, taking place in the European Union. The structural change in the food industry has been deeply affected by the whole process of globalization, mainly in terms of integration trade areas and institutional changes which have created a more favorable environment to increasing trade and investment transactions. The analysis contains a survey of the recent literature actual path of transformation affecting food industry in the light of new competing conditions and market access. As it is argued, structural change in food industry worldwide towards concentration is associated to the overall trends of trade and FDI, and also to market integration, the emerging of own label products in the retailing segment and finally the strategies of advertising and innovation adopted by firms.

Key words: Food Industry, Structural Change, European Food market

1. Introduction

This article aims to discuss the changes undergone by the world food industry with emphasis on the recent development, taking place in the European Union. In the context of globalization, structural change in any industry is hinged to two main aspects of the new international

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economy. On the one hand, there has been a deeper integration in the markets, both regionally, in free trade areas, and globally. On the other hand, institutional changes within countries and at international level have created a more favorable environment for increasing trade and investment transactions.

As a result, competition between firms is no longer confined within national borders, as it has lately included foreign competitors both from trade and foreign direct investment (FDI), hitherto unknown to the economic agents. In short, as protectionistic rules appear to be less effective in many countries, the world price becomes more transparent. Therefore, based on this trend, firms that are potentially able to compete in foreign markets are stimulated to step up plans to invest in other countries attracted by local comparative advantages. Simultaneously, national firms become more exposed to new and strong investors, more especially multinational enterprises (MNEs), given their ability to exploit those advantages in a coordinated fashion. Despite the pervasive emphasis put on trade expansion and on the dissemination of new opportunities for investors in a global scale, one of the central features of globalization has been a visible centralization of capital. In reality, one can translate this as a mere materialization of what is more essential in capitalism, usually unleashed when market conditions are more favorable. This paper contains a survey of the recent literature addressing the questions related to the actual path of transformation affecting food industry in the light of new competing conditions and market access. As it is further argued in this analysis, concentration has been a striking feature of the structural change in the food industry worldwide. In order to discuss this process, attention will firstly be paid to the overall trends of trade and FDI. Secondly, some evidences of the process of structural change in that industry will be shown, followed by an assessment of the main aspects underpinning it, namely market integration, greater importance of own label products in the retailing segment, and finally advertising and innovation related costs.

2. International Trade and FDI in Food Industry

World trade relations were intensified in the 1990s, after many economies were immersed in inflationary problems, largely prompting governments to keep their industries, at various degrees, under protection. Despite being just comparable to the late nineteenth century, world trade volume grew in 1994-97 at 8.7% a year, which is much higher than the growth of output. It is, however, relevant the fact that this expansion of trade drifts away from the hitherto prevailing inter-industrial pattern, according to which North-South relations accounted for most of the barter between raw material and processed and diversified products. Indeed, over the last years, not only has trade increasingly expressed competitive advantages, generated in the context of industrial development led by technological innovation, but also it has resulted from the internationalization of industrial production. Consequently, trade has become more of an intra-industry nature, reflecting the transactions between industrial plants disseminated worldwide, mainly in those sectors where technological development has been more intensive.

Within the agrofood system, although bulky commodities account for a large share of the trade, processed products have become more significant in recent years. Between 1972 and 1993 the value of trade in manufactured products grew 574% against 355% of homogenous commodities. Moreover, in 1993, processed food products accounted for 67% of world trade in the food sector (Henderson et al, 1998). This is a clear cut indication of how international food trade has become much more complex and, as such, supported by aspects other than resource endowments and factor costs. Basically, the fact that trade is becoming intra-industry revolves around a dynamics in the production structures where economies of scale and scope, product differentiation and process innovation coupled with new marketing strategies, become key factors. Therefore, attention should be focused mainly on created competitiveness by investment in production capacity coupled with innovation and also with the expansion of market outlet, rather than on specialization only.

Another characteristic of international food trade in recent years, is the level of concentration among both firms and countries. Of the fifty largest food-processing firms, ten were responsible for 44% of processed food trade. Among countries, only twenty-four were responsible for 68% of manufactured food trade in 1962, going up to 80% in 1990. France, Netherlands, the United States, Germany and the United Kingdom accounted for 38.2% of the world manufactured food exports whereas Japan, Germany, the USA, France and the UK imported 52.7% of the total of it (Henderson et al, 1998). Thus, in recent years, international trade has revealed a very unbalanced distribution between blocks of nations as most transactions have occurred within the triad. So, this is the geographical area where the flows of investment in the food industry have taken place. As for less developed countries a smaller amount of trade transactions in the agroindustrial sector has taken place, mostly consisting of natural or semi-processed commodities, with low level of differentiation. In reality, this reflects the overall trends, according to which trade within Western Europe accounted for 35% of global trade flows in 1992 (Hoekman and Kostecki, 1996), justifying the attraction exerted by Europe to foreign investors.

In recent years, another widely discussed central aspect of globalization and market expansion is the increase of foreign direct investment. The growing importance of inter-industry trade has largely been reinforced by the fact that multinational firms have directed their investment decisions towards different countries, attracted by local advantages, as we will show further in this paper. As correctly pointed out (Traill and Gomes, 1997), FDI is to be seen as complementary to rather than a substitute for trade, according to the requirements imposed by the internationally distributed production. Expansion of FDI can thus produce more trade as a result of the presence of MNEs in different countries reinforcing their role as the driving force of a more integrated economy. On the other hand, new investment has made competition in host countries tighter mainly where market oriented industrial policy has been enforced. Also, a more flexible approach in home countries helps the underpinning of the flow of capital towards new markets. Regardless of the forms of investment, its expansion has strongly determined the emerging of a global pattern of production and consumption, expressing an accelerated internationalization of production by means of an increased mobility of capital and of knowledge and technology (Strange, 1997).

As previously pointed out, expansion of FDI largely depends on the attractiveness of host countries in terms of new opportunities, assuring institutional arrangements and market conditions. Following an exclusively free market orientation, national economic policies are expected to attract MNEs by expanding domestic market, reducing external costs affecting production, deregulating institutions and privatizing state companies. These aspects however fall short to deal with the impacts of FDI on the existing firms, the level of employment, and the welfare of population. Moreover, other aspects such as those related to the creation of competitive advantages by means of economic policy directed to R&D and the need to improve the performance of firms in the international market are not accounted for.

A full openness of economies, based on requirements following this view is expected to bring benefits to the host economy, for competition would put national firms under pressure to raise their efficiency, and consumers would benefit from better prices and a wider variety of supply. On the other hand, given that industrial policies have simply become a mechanism to provide means to boost the competitiveness of incumbent firms, facing new entrants and eventually becoming new competitors in the world market, it may also as well cause firms to be eliminated by competition. The lack of competition policies in many developing countries is bound to make this outcome even more dramatic.

This discussion however cannot be carried out according to the principles of perfect competition, mainly when technological innovation, product differentiation and economy of scale are at stake. The fact that small firms cannot compete should not be seen as market failures, but as a result of how real competition works. The very dynamics of market is conducive to the formation of large firms on the grounds of their higher efficiency, something that cannot be understood as a market failure. (Lipsey, 1997)

To a large extent, investigations about FDI in food industry has used an approach designed by Dunning (1994) in his attempt to reveal the relationship between foreign investors' strategies and the position taken by national governments based on national comparative advantages. There are generally four motivations followed by entrepreneurs in promoting FDI:

- resource seeking, both physical and human;
- market seeking, both domestic and regional, as in the free trade areas;
- efficiency seeking, by which firms try to exploit economy of scale and scope and seek an efficient insertion in the productive value chains;
- strategic asset seeking in terms of technology, organizational capabilities and existing markets for expanding production. (Dunning, 1994).

The first two strategies are typical of initial investments, thus explaining the reasons lying behind the actions of companies towards new markets. The events of new trade area, of which the Single European Market is the most noticeable example, have also justified those actions by foreign investors. The last two motivations are mostly related to the prevailing conditions in existing markets, mainly when final consumption is limited and dispute between firms intensifies.

By all means, the existing terms of competition have favored even further the process of concentration in food industry. Large companies have been mostly responsible for the increase of this industry's FDI in recent years, carried out by either installing new plants in such a dimension as to outcompete incumbent firms or setting up joint ventures or other forms of contract. In one way or another, the trends of recent years indicate an unmistakable superiority of large investors in food industry, both from cross-country in Europe and from foreign countries, particularly the US.

The design of a new set of strategies by companies undertaking foreign investment has reinforced competition in which concentration, through mergers and acquisitions, has been a persistent rule of the game. Although the degree of attractiveness to inbound FDI varies among countries and sectors of activity, what should be taken into consideration is its impact on national economic development. That is, to what extent can leading firms make national competitors become more competitive in the international market and spill over the benefits of their influence? Because national boundaries no longer set limits to market expansion, firms tend to compete in a more open environment. For those incumbent firms relying on the protection of national policies, new coming investors definitely pose new challenges, and intensify competition.

These trends, however, related to both inbound and outbound FDI are expected to be more intense within the group of industrialized countries, which share similar standards of consumption, level of income, growing market strength and technological development. The share of those countries as primary source of outbound FDI flow and stock in the period 1990-1994 was 89.4% and 79.4%, respectively, whereas only 10% of outward FDI went to developing countries[1] (Dunning and Narula, 1996). Therefore, despite a considerable inflow of investment towards these countries, one cannot raise expectations that the overall performance of the host countries' industry will be improved. A central factor affecting this is the rate and features of technological transfer. In other words, the extent to which incumbent firms can absorb innovations and become more competitive is the key question. It is not a matter of changing trade by

[1] Latin America has been an important target for large companies. MERCOSUR and the prospect of the increase in food consumption after price stabilization in Brazil became important attractions to large firms. "By building up Nabisco's own brands and acquiring local ones in Mexico, Brazil and elsewhere, it has become one of the largest American food groups in Latin America. Richard Thoman, its chief executive, says that the regions relatively young population and improved economic and political outlook make it an attractive market. So does its size." (The Economist, 1993, pg. 14) After the implementation of Real Plan in Brazil, more than thirty national large and medium sized companies were sold to multinational corporations. (Castro, 1998)

increasing differentiated products, but also of innovation process more widespread among competing firms.

An important aspect of FDI is the potential emerged in the host countries for further expansion. Bearing in mind the persisting conditions for increasing competitiveness and economic development, consolidation of FDI is very much dependent on the likelihood of seizing new opportunities for further investment on a sequential fashion. According to Dunning (1994) 90% of MNEs activity is carried out from existing assets. To a large extent, thus a high proportion of sequential investment reflects the attractiveness persisting in host countries depending on how those requirements above mentioned are materialized.

2. Concentration Process in the Food Industry

Food industry is an important activity in the developed world, being responsible for about 15% of total manufacturing output in seven main countries[2]. Among them, Australia has the highest output, with 20.8% and Japan, the lowest, with 9.8% (Traill, 1998). Although it has followed the same trends as the industry as a whole, many differences still remain, mostly accounted for by a yet low rate of convergence between the production and the consumption pattern. As argued above, in the complex trends towards a globalized food market, and its concentration in the developed world, FDI has been recognized as the driving force of market integration. Moreover, despite the fact that the main market of the top multinational food and drink companies is located within the group of industrialized countries, they have widely expanded their investments also towards developing countries.

To a large extent, the profile of food industry within the developed world has been determined by the expansion of FDI. Foreign production undertaken by MNEs' affiliates of the American food industry has been 4.3 times higher than the exports by those companies. Although in a smaller

[2] USA, Japan, Germany, France, the UK, Canada, Australia.

dimension, food industry from other six developed countries acting in foreign markets, has also had production abroad growing faster than its exports (Traill, 1998). According to Henderson et al, (1998), fifty leading US food manufacturers had the value of the sales by their affiliates in 1992-93, surpassing the value of the companies' exports by 12 times. These evidences are very supportive to the fact that the nature of trade is changing and therefore becoming more interconnected with the expansion abroad of production assets.

Furthermore, food manufacturers expand their sales by means of licensing, or other forms of contract, whereby the licenser keeps control of the manufacturing conditions, i.e., technology, without expanding production capacity. Most of large MNEs have been engaged in some form of contract operation. Not surprisingly, the majority of them have taken place among industrialized countries. Of thirty contracts set up by American companies, detected in 1990, seven took place in Canada, six in Japan and five in the UK, being the others scattered among different regions. From the companies whose headquarters are in the UK and in France, the contracts observed were directed towards the US, in a number of five and two, respectively (Henderson, et al, 1998).

In the period between 1988-93, 23% of European companies were acquired by American competitors (The Economist, 1993). Consequently, most of international operations by food industry have taken place in countries where there are similarities in their overall economic conditions, such as level of income, consumption standard, etc., making them more attractive in comparison to developing countries. Additionally, the underlying aspect of this move is that most investors are attracted by market expansion, particularly in free trade areas.

Food production in host countries has significantly been a result of strategies designed by MNEs to reduce uncertainties and close the gaps between the production process and final consumption. This has been described by Rugman (1997) as internalization whereby, " MNEs can monitor, meter and regulate internally the nature and extent of its firm specific advantage (FSA)" (pg123), and therefore minimize transaction costs. If, on the one hand, FDI reflects the strategies of MNEs to strengthen position in a world competitive market, on the other hand, it has ended up being conducive of a strong process of concentration, by means of mergers and takeovers.

As already pointed out, not all FDI is directed to create production capacity, exclusively controlled by foreign affiliates, as there can also be significant arrangements through joint ventures, licensing, etc. The closer food consumption becomes to the international prevailing standards, the more widespread are the initiatives to establish franchising and other forms of licensing, mostly in the retailing segment.

The strengthening of large enterprises has been a result of a pressure created by at least one of the following conditions:

- food demand became stagnated in the most affluent markets of Europe and the USA., leading consumers to give priority to differentiated products
- own labels became more widespread, led by the supermarket segment of retailing sector, able to impose strict conditions to sell the industry's brands which only the large ones can cope with.
- combination of cost reduction, scale increase and product diversification.

These are aspects imposing a restrictive environment and huge challenges for competing firms. In short, the more successful firms are in increasing production and reducing costs of differentiated products, the larger their market share can be.

Despite significant increase in the degree of concentration in the retailing sector, mainly supermarkets and fast food chains, investment in processing plants has drawn most attention lately, due to its impacts on domestic market structure and conditions of supply. As a result, the level of concentration increased in all European countries in the period 1987-92, when the Single Market was to be implemented (Oustapassidis, et al, 1995).

Although these conditions can still change according to overall factors such as the path of economic growth and market integration, it is important to recognize that the consuming market in different countries still preserves extreme heterogeneity. According to Traill (1996), consumption standards have diverged internationally, even when socio-economic and demographic aspects evolve in the opposite direction. This, however is more evident between developing and third world countries, where a market segmentation suits the prevailing patterns of income concentration, whereby food consumption is determined quantitatively, rather inhibiting product differentiation. However, even in more affluent societies, idiosyncrasy and habits long formed, have become a challenge to new entrants, mainly those from other countries.

Based on these points, two major questions emerge. Firstly, how have large companies coped with distinct features, enabling themselves to compete with incumbent firms? Secondly, what has been the space and mechanisms for local companies to survive in such environment?

The living together of a variety of types and sizes, typical of food industry in a complex market structure of differentiated oligopoly, reflects not only market niches still not reached by large companies. It also indicates the implementation of successful strategies adopted by small and medium sized firms, mainly towards cooperation with other companies. Despite a predominant presence of large companies, reflecting an unmistakable concentration process, a wide range of small and medium sized firms is still responsible for a sizable share of output and employment. According to Traill (1998), the group of firms employing less than 99 employees in Europe accounted for 98% of the total number of firms, 49% of employment and 32% of total output[3] in 1990. This large proportion of small and medium sized business, more evident in some segments, can be attributed to the limits of the concentration process led by large companies in recent decades. The dynamics of local markets, where consumers still rely on small suppliers like bakeries and butchers, and of a supplying

[3] Although this measure does not reflect the overall pattern of concentration, given that innovation can negatively affect employment, it can still give a broad idea of how concentrated this industry is.

chain that includes small and medium sized firms into a relationship with large retailers, are accountable to explain the survival of such a variety of firms sizes within the sector.

The structural change resulting from this pressure for larger firms to grow and gobble up smaller ones can also be related to strategies to operate in existing markets. In other words, in order to understand the changes in the landscape of food industry, one must take into account not only the operation of market forces, but also the competing strategies designed by firms. Generally speaking, one can define strategy as a mechanism devised by firms to thrust their way into competition and to deal with conditions generated by the overall economic environment. Or as Linda (1993) defines it, " strategy is an operational synthesis between the objectives of company and the organized means to pursue them" (pg. 16).

The recent process of transformation, taking place in the food industry worldwide, has mainly been a result of initiatives taken by large firms to expand their influence, basically through external growth, or merger and acquisition, as opposed to internal growth through the creation of new assets. The direction towards which firms expand is thus determined not only by their competitiveness by resourcing to technology, increasing scale, advertising, etc., but also by their ability to spot the right opportunities to expand production. As Linda (1993) suggests " large European companies are by nature hunters (acquirers) of new markets and enterprises" (pg. 16).

As previously stressed, it is the move by large companies, particularly the MNEs, that has attracted most attention and has been cause for concern. Focusing on the widespread acquisition of local brands by multinationals Linda (1993) predicted that only 10% of the existing number twenty years earlier remain in the year 2000. This irreversible trend is underpinned by changes in market conditions paving the way for investors towards new opportunities, as can be noticed in the demolition of barriers to FDI.

A smaller degree of restriction of governments in home countries to the outflow of investment towards foreign countries, and more receptive attitudes by governments of host countries to incoming firms by adjusting their economies and dropping obstacles, have widened the prospects for those firms with aspirations in foreign markets. Closely related to this, the deepening of regional market integration has been an important factor to intensify competition, as in the case of the implementation of the Single European Market.

As the world economy becomes more integrated, thus causing economic agents to be more exposed to an open competition, firms are bound to change their behavior to survive. This is the case for the completion of the European Single Market, which has changed the spectrum of possibilities for both European and no-European industries. This of course covers a wide range of initiatives and decision making, according to the size of firms, the type of industry and prevailing regulation system[4]. However, distinction should also be made as to contemplate small, medium size and even large national firms trading within the limits of local and regional markets, and MNEs searching for new opportunities through FDI. An interesting way to tackle this question is provided by Kuhl (1992) based on the changes in the European food industry, caused by the entry of new competitors into the market. Based on a survey by the Commission of the European Communities (1989), the author indicates two kinds of strategic action adopted by firms in the context of a single market. Firstly, firms may promote change within their own structure by relocating their assets towards certain activities and adjusting their distribution system. Secondly, firms may intensify cooperation and/or expand their assets through merger and acquisition in order to achieve a scale large enough to reach the foreign market.

It is important to keep in mind that this is a dynamic phenomenon, driven by competition itself in each specific segment of an industry. The permanent structural adjustment incurred by firms implies in a variety of

[4] In terms of competitive and trade policies and also the development of strategies set up by governments.

actions towards both the market and their internal structure. On this internal front, firms can, for instance, develop strategies to launch new products and meet demand based on the existing loyalty of consumers, or else build up on traditional product-lines whereby pre-empting the action of newcomers. Within the context of a wider European Market, food industry's market stretched beyond national borders, becoming thus subject to two events. Increasing production capacity became subject, on the one hand, to differences between consumers of other countries[5], and on the other hand to the decisions of competitors to expand their market by installing affiliates or by increasing exports.

An important outcome of this process was the rise in the number of mergers and acquisitions as well as joint ventures as mechanisms to reach a good position in a market so important as Europe. Many firms from the food industry, as the whole of manufacturing sector, tried to be prepared for the implementation of the ESM. As Oustapassidis et al (1995) pointed out:

> "The EC firms were compelled to expand their community basis to be able to compete in the single market. The foreign firms were also interested in reinforcing their presence before that day. In both cases the merger strategy was used as a fast way of achieving the goals associated with the Single Market"(pg. 4).

Still from the same source, the bigger mergers in Europe in 1991/92 occurred in the food industry. Thus, this indicates that strategies adopted by firms in the European Market has been quite a reaction to overall changes in the economy, as countries become part of free trade areas or single market. As previously pointed out, the need to increase scale, particularly in an expanded market, has been complemented by other mechanisms, such as joint ventures and franchising, in order to achieve a better performance in an expanded market.

Although, so far, there has not been any obstruction by state action to minimize the trends of concentration, competition policy is expected to

[5] The fact that European countries became closer by the action of trade unification, does not yet mean that the standard of consumption converges. Therefore, one cannot say that there is not such a thing as a European consumer.

come to the fore in the future by enforcing antimonopoly measures (Russo and McLaughlin, 1992). This, however is something that might not be as effective as one expects, given the increasing power held by multinational corporations vis-à-vis nation states.

Analyzing from a different perspective, firms face competition in a day-to-day basis essentially by combining increase of scale with diversification of product-line and traditional strategies related to price. An underlying instrument to achieve this goal concerns investment in R&D and in the implementation of new technologies, both on the production structure and organization, despite the handicaps still persisting in food industry, mostly related to the limits to consumption diversification. Grunert et al (1998), using data by Commission of European Community pointed out that expenditures in R&D to sales ratios for large food companies are 0.5%, much lower than drug industry (12%), electronics (8%) and motor vehicle sector (4%). However, it is widely accepted that despite the fact that innovation to create new products can be delayed by cultural and inherited factors impregnating consumer's behavior, much effort has been put forward by firms of food industry to differentiate products by means of designing and advertising. A good illustration of this is found in the ability of industry to generate products and services to suit changes in demand, like ready-to-cook food, fast food, healthier food, etc., according to the respective conditions.

In general, as far as product innovation is concerned, competition in food industry is in principle determined by the simple challenge of making something different, though essentially similar to competing brands. In short, how to change a commodity into a unique product is what can make a firm more successful than others. This, of course, favors large companies, both because they can combine scale and scope more efficiently and also because sunk costs can be more easily absorbed. On the other hand, this ends up having implications for market structure, consolidating certain competing conditions and also raising the levels of barriers to entry.

3. Factors Affecting Structural Changes in Food Industry

The path of structural change in any industry has been related to both market conditions and the performance of firms, in such a way as to increase their market share. This of course varies widely, according to the type of industry and the specific conditions of final market access. In food industry, at least three factors have acted to set limits to small and medium sized manufacturing firms to some extent confining them to the fringes of market: regional trade integration; greater importance of own label products; and costs of advertising and R&D.

It is recognized here that food industry is a very complex activity, in which a wide variety of agents, small and large live together in attached market segments, depending on the extent of major transformations affecting the conditions to market access. Even so, as mentioned earlier, the prospects for operating in a wider market are enticing to firms in a position to increase productive capacity. As it is well known, large market is essential for firms to grow, and more importantly to combine product differentiation and economy of scale. Therefore, firms increase the possibility of a higher return, not only on the grounds of a bigger final market, but also because they can exploit conditions for vertical integration by incorporating different stages of production. According to Oustapassidis et al (1995), the main motives for mergers in the EU food industries from 1986 to 1992 were related to strengthening their position in the market and diversification of investments.

According to Gilpin and Traill (1995) the development which took place in the food industry in the 1990s, produced three strategic responses by large firms. Firstly, given the implementation of the European Market, firms detected an opportunity to strengthen their position through mergers in a dimension that enabled them to face national competitors and most importantly large retailers, who have also grown beyond national borders. Secondly, investments have also shown higher flexibility in order to cover a wider range of products, for which innovation has become crucial.

Finally, increasing scale for a larger market has been decisive, especially in certain product lines. In other words, the strategies to act in an integrated market can be summarized in a combination of increasing scale and product diversification in such a way as to pre-empt the moves of competitors, and to reach a diversified range of consumers. As the authors point out, "large firms are adopting a mixture of efficiency seeking (cost minimization) and product differentiation strategies to meet the changing circumstances"(pg. 29). This is a structural change also affecting the retailing sector. The recent take-over of ASDA by Wall-Mart in Great Britain, making the latter the second largest European retailer indicates how concentration is bound to intensify among supermarkets. This trend reveals not only a more far-reaching asset diversification but also a more intense rivalry between large international conglomerates. Mergers and takeovers are thus a strategy to gather strength to face bigger competitors. The likelihood of Wall-Mart stores expansion in Europe makes many smaller supermarkets potential targets for acquisition, triggering off a battle to increase market share. As Kingfisher's chief executive pointed out, their aim is to prevent Wall-Mart from operating in Britain and becoming an European hypermarket. Fixing the stakes in a market targeted by competitors has been a blatant strategy to survive and to compete internationally.

A second factor affecting structural change, and indeed contributing to concentration, is the widespread growth of own label products by large retailers. Thus, a very specific type of competitor has emerged in the last decade, somehow reversing the traditional balance of power between manufacturers and the retailing segment. Moreover, as supermarkets have also become larger in size[6], operating at national scale[7], their own brands have turned into a high barrier to the entry. As a result, only large firms have gathered strength to reach the final market, despite additional

[6] Using a DELPHI method to forecast changes in food industry, Russo and McLaughlin (1992) found that the average size of supermarket was 31.000 square feet in 1990, being expected by food executives to increase 61% to 50.000 square feet in the year 2000.

[7] Although most supermarkets are nationally based, there is a move towards Europeanizing. This expansion has taken the form of both alliances between national chains and direct operation across the borders. In 1993, 30 largest food retailers were detected as having foreign operations in Europe (The Economist, 1993).

investment in product diversification, larger scale of production, and marketing. Simultaneously, this move towards a larger market taken by retailers triggers off a concentration process among their suppliers, stimulating them to increase scale to compete in this activity. On the other hand, although small and medium sized firms have been able to survive as own label suppliers, the recent trends towards concentration have limited their space. As Gilpin and Traill (1995) point out "such moves would create intense rivalry within the own-label sector and the SMEs that are presently able to compete may find themselves squeezed out by lower cost and technologically-more-advanced competitors" (pg. 30).

Therefore, the increasing weight of retailers with own-label products has affected competition within the food industry in two different ways. Firstly, given their proximity to final consumers, retailers are able to monitor their behavior more closely, and therefore adapt to changes in consuming habits. As argued by Traill (1998), retailers have lower costs related to market research and advertising compared with the manufacturing segment, particularly when new products are launched. Additionally, more strict conditions can be imposed for branders to sell their products through the retailing chain. Secondly, given a larger scale of retailing operations, their suppliers are inevitably driven to higher levels of scale. This has also attracted large manufacturers who find supplying retailers a profitable business and therefore an opportunity to use full production capacity and as a result outcompeting smaller suppliers. In some circumstances, supplying own label retailers works as a life boat as it allows larger firms to offset eventual losses from their own brands (The Economist, 1993).

A third factor, which contributes to the process of concentration in food industry is related to what the literature has defined as sunk costs[8], more specifically advertising and R&D. This is the subject discussed by Traill (1994) highlighting the impact of such costs on market structure. Using the concept of sunk cost as endogenous, the author points out that

8 These are costs which cannot be restored by firms in case they decide to leave the business and move to an activity different from that where the expenditures were made.

"incumbent firms can determine the level of advertising needed to compete in an industry by 'raising the stakes', adopting a high advertising regime. This simultaneously increases the initial set-up costs and the minimum efficient scale of the firm" (pg. 3). Therefore, larger firms are more capable to absorb high levels of advertising expenditures, especially when market becomes larger.

Insofar as advertising is concerned, the food industry shows the highest level in Europe, compared to other sectors, what reinforces the changes in market structure towards concentration. Food market has been influenced by a pressure to substitute traditional products for new and more attractive ones in order to gain the consumer's preference and to surpass the barriers raised by own label retailers. Based on the very simple idea of making something especial out of a trivial product, food industry started having to make their products more attractive to consumers by increasing expenditures in advertisement. The difficulty here, is twofold. On the one hand, because consumers can be supplied by own-brand retailers, mostly at cheaper prices than those of manufacturers, these become under pressure to face such an obstacle to reach the final market, for which advertising is a crucial instrument. On the other hand, as the market tends to become larger, as in Europe, the challenge to reach a variety of consuming habits tends to be bigger. In this case, the effectiveness of advertising will be higher, according to the converging rate of consumption standard.

Another cost incurred by food companies to face competition and therefore underpinning concentration is that related to R&D. Innovation is interpreted here as a result of changes, not only in demand, but also in the competition among rivals. It is arguably recognized that larger firms have invested far more in technology than smaller ones. Moreover, creating new products has become the road to deal with changes in the consuming market. Innovating is also a strategy that raises significant barriers to new entrants, reinforcing thus the concentration process. Despite the fact that food industry is largely dependent on innovation taking place in basic industries, such as chemicals, many created products are a result of strategies developed by the final sectors, say the food industry, according to the challenges posed by market conditions.

The further companies go in combining cost minimization with increase in scale and product differentiation, the more competitive they tend to be, particularly when the market is expanding and competition tightening. When neither of these strategies is adopted successfully, the only way out to survive is by reducing prices. This however, only might influence competitors strategies, when market is generally recessive and consumers are adopting a more cautious approach, as it happened in America and Europe in the 1980s.

4. Conclusion

In the recent context of globalization, market structure of food industry has increasingly become concentrated in the manufacturing as well as retailing segments. Three factors related to market operation were discussed as having decisive influence on business performance in this industry, namely market integration; growing power of retailers; and costs of advertising and innovating.

From the argument shown above, large firms are believed to be more able to face the challenges posed by competition, in particular from the retailing sector. Likewise, market integration greatly favors large businesses, despite the existing stumbling blocks emerging from national economies, mainly in terms of consumption standard and market organization. Therefore, as competition spreads over national borders small and medium sized businesses are bound to be in a more fragile position, despite their ability to survive in certain market niches.

However, a striking aspect of the new market condition is that the highest hurdle in the race to increase market share comes from the retailing sector. Therefore, competition within the manufacturing and retailing segments intermingles and drives market structure to higher level of concentration. Although not thoroughly investigated, advertising and R&D costs are indicated to be relevant to understand competition occurring in this industry. Besides the strategic importance for business performance, these costs incurred by incumbent firms can preclude new entrants from competing simply by establishing a high threshold. These aspects though deserve further research, especially to establish the links between innovation and changes in market structure in food industry more clearly. There is also a permanent feedback, worth investigating, between advertising and creation of new products. Supposedly, large firms are more prepared to compete in a market where new products are frequently being introduced and hence, to a large extent by private-label retailers.

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