The Profit Behind Your Plate

Critical Issues in the Processed Food Industry

December 2006

Myriam Vander Stichele & Sanne van der Wal

This SOMO report analyses the contribution that primary and full processing of food can make to poverty reduction and sustainable development within the current international context. First, the report provides insights into the level of production, sales and international trade of processed food. Next, it discusses the structural, market, private and government obstacles to exports and the development of a domestic processed food industry in developing countries. The report identifies the many problems which are still not sufficiently addressed in order to make food processing beneficial to all stakeholders and to sustainable development. However, the report does not focus on the critical issues of farmers and other suppliers to the processed food and drink industry.

Processed food and drinks are usually produced in the country or region where it is consumed. Trade in processed food is only 6% of what is consumed worldwide.
An important current trend affecting the whole processed food sector is that prices for processed food companies, from the top global brands to small food manufacturers, are under serious pressure from supermarket strategies and supply requirements.

The study aims to provide arguments for civil society organisations to feed the debate on trade and investment, corporate accountability and globalisation. The final chapter provides arguments to make purchasing practices more equitable and give stakeholders more rights to seek remedies against the abuses of foreign food companies and supermarkets.

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Colophon

The Profit Behind Your Plate:
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Executive summary and conclusions

The processing of food and drinks and their exports has traditionally been seen by developing countries as a way to diversify out of low-priced, volatile and environmentally damaging commodity production and trade, and to get more added value and foreign exchange earnings.

This report analyses particular obstacles for the development and trade of processed food from developing countries, and the contribution the processed food industry can make to poverty reduction and sustainable development in the current national and international context. The report does not focus on the many problematic issues of farmers and other suppliers to the processed food and drink industry.

There are two categories of processed food which are different in terms of production, trading, market structure and corporate strategies.
Firstly, there are the land-based food products, which undergo primary processing such as crushing, or the semi-processed food and drinks. They mostly constitute the ingredients for the fully processed food manufacturing. These products are highly traded around the world. The market for some of these products is highly concentrated at the national, regional or global level, for example for soy oil, with a very few companies sourcing (but usually not actually growing commodities), semi-processing, trading and selling. The same agribusiness multinational can be dominant in the processing and trading of different commodities, such as Cargill, Bunge, Archer Daniels Midland (ADM). Most of the global leading companies in this sector have their headquarters in the US.

Secondly, there are manufactured food and drinks, or packaged processed food and beverages, ready to eat or drink, and for direct sale to the consumer. This market is diverse, with new trends of ready-to-eat meals, healthy or functional food, especially in the saturated developed country markets, and more basic food such as bakery and dairy products being sold in developing countries. Processed food and drinks are traded much less and are usually produced in the country or region of consumption; one reason for this is that local tastes still play a dominant role, notwithstanding some worldwide standardisation of food and tastes. This market shows little concentration at the global level, with the number one food multinational, Nestlé (Swiss), only having 3.3% of the world market (2004). However, the top 10 companies at the global level have much larger market shares at the national or regional level, particularly for some packaged food and drink products for which they own the production formulas and the sales of which are heavily influenced by marketing.

Overall, trade in processed food is only 6% of what is consumed worldwide. There were no clear figures to indicate whether developing countries' trade in these products showed a slight increase or decrease. It is clear though that least developed

countries captured just a marginal share and that half of developing country trade by value is captured by just four countries - Argentina, Brazil, Malaysia and Thailand - of which probably quite some part was captured by the multinationals mentioned above. More research is needed in this area.
Traditionally, the supply side problems faced by developing countries to export, especially to developed country markets, are mostly claimed to be a lack of available infrastructure (roads, storage facilities, etc.); lack of government support and legal frameworks; high demands in the areas of hygiene, safety and quality; lack of reliability (on-time delivery), learning capacity and information about markets by suppliers, etc. This report, however, also emphasises the structural, market, private and government obstacles to the development of exports and the domestic sectors of developing countries.

Sales of processed food are increasing where incomes are increasing and also because of changing lifestyles and consumer technology (such as fridges, microwaves) with more preferences for pre-cooked meals and chilled food. The higher forms of processing - for some products at least - are taking place mostly in developed countries: developing countries were only able to increase their share of the added value generated in the processed food sector (1995-2004) by a marginal amount, up to 24.5%. The prices for manufactured goods have been declining less than real farm gate prices, but retail prices have declined the least. For developing countries which import manufactured or higher-processed food and export less or unprocessed foods, this means deteriorating terms of trade. More research into these terms of trade is needed.

An important current trend in the processed food sector is that prices for processed food companies, from the top global brands to small food manufacturers, are being seriously put under pressure by supermarket strategies.
Firstly, by the increasing sales by supermarket chains of their own private labels - also called house brands - which now have a market share of more than 12% of global packaged food retail sales. Private labels are now ranging from cheap, low-quality goods to higher quality products or exclusive products of a supermarket chain that sometimes uses different kinds of private labels. They are also introduced by supermarkets in developing countries, where they can challenge local brands. More research needs to be carried out into the conditions under which private labels are produced – by small, medium or brand product manufacturers – in terms of workers' conditions and income, profits and retailer buyer power, environmental impact, impact on the supply chain, benefits for developing country processing industry, etc.
Secondly, supermarkets, hypermarkets and discounters are increasingly becoming concentrated into a small number of players, and as a result of buyer power, and sometimes abusive practices, are able to squeeze the prices of food companies, even the largest food multinationals. The rapid expansion of the same small number of supermarket chains in developing countries affects the food and drink companies in these countries, especially the smaller ones, as supermarkets require large volumes

at high quality and low prices, and source from outside the country if this is more profitable.

Packaged food companies have reacted to supermarket trends and new consumer demands with a wide range of strategies to compete against their rivals and reverse their declining profit margins by cutting costs, including shedding many jobs, increasing efficiency and making supply chains more integrated, enabling inputs to be globally sourced. Where possible, multinationals have concentrated manufacturing into one or a few units per continent. Food and drink companies are trying to respond rapidly to consumer demands for healthier, higher quality, environmentally friendly and new products, and increasing or innovating their marketing, some of which has been criticised for being irresponsible or illegal. One of the strategies developed by food multinationals present in the South is creating smaller packaging sizes, in order to increase sales to the poor.
As it is important in the processed food sector that food and drinks cater to local tastes and consumer demands, the food and drink industry of the North has expanded in developed countries, and especially in developing countries with profitable markets, by means of investments, mergers and acquisitions, divestments of non-core or non-profitable operations, strategic alliances, joint ventures with experienced local companies, co-branding and cross trading. This has led to concentrations which are opaque and difficult to investigate. These strategies by multinationals make it difficult for developing countries who want to diversify away from primary commodity production by building up their own domestic processed food and drink sector, or expanding domestic enterprises, even when consumer demand is rapidly increasing in the home market. The growing complexity and sophistication of Western food products and markets, where fresh processed food sales are increasing, make it increasingly technologically and financially demanding for Southern food and drink enterprises to access and export to Northern markets, even if tariffs and other trade barriers were to be removed. Some cooperatives have successfully been able to overcome these difficulties, while others have failed.

Although the WTO Agreement in Agriculture, other WTO rules and other agreements have liberalised processed food trade, this report shows evidence that exports from developing countries in all (primary) processed food and drinks still face many obstacles, mainly: high tariffs, tariff escalation, unequal access compared to member countries of a trade bloc, anti-dumping rules, countervailing duties, emergency safeguard measures, special safeguard measures under the WTO Agreement on Agriculture, food standards and certification, export and domestic support subsidies to the processed food industry in the North. By allowing most of these measures, WTO agreements lead to unfair competition for exports by food processors from developing countries. This marginalises or eliminates small food and drink producers, and disadvantages the food-export orientation policies implemented by developing countries wishing to participate in the global economy. There are no WTO rules or other rules that guarantee that developed countries' exporters are getting a price that covers the (increasing) cost of applying the standards and providing the necessary proofs for it. Whether new WTO negotiations will improve the situation of processed food companies in developing countries remains to be seen. The lobby of the processed food and drinks industry has an important influence, for example on the negotiation position of the EU, which defends their interests by demanding greatly improved access to processed food markets in developing countries. Unfair competition from indirect subsidies could also continue if WTO talks restart on the basis of the same proposals as are currently on the table.

Food and drink processors in developing countries are also facing competition in their domestic markets from food and drink multinationals and supermarkets investing in and taking over local industries, rather than importing. Such investments are supported by many measures taken by developing countries to attract foreign investment. Foreign food and drink investors are receiving advantages as a result of unilateral measures such as exemption from tax payments, from import or export restrictions or even labour laws. Through bilateral investment agreements (BITs), the TRIMs and GATS agreements under the WTO, investors in processed commodities and food, and supermarkets receive legal protection against government measures that could disadvantage or harm their profit making. These investment measures allow food multinationals and supermarkets to establish or take over local food and drink processing industries and retailers as soon as a developing country market is becoming profitable for them. Moreover, these investment agreements can prevent some measures that would be needed to support local and small food, drink and commodity processing companies, or even financial stability. As these agreements do not impose obligations on investors or home countries, they are imbalanced in favour of the latter and do not encourage solutions and legal mechanisms to solve problems of undue and unfair behaviour and political influence by foreign commodity, food or drink and retail investors.

This report identifies many problems which are still not being sufficiently addressed by the industry in order to make food processing beneficial to all stakeholders and to sustainable development. Some of the most problematic issues related to operations of the food processing industry include undermining union freedom in countries with bad labour rights, lack of equal opportunity and pay, increasing numbers of temporary (migrant) workers with fewer social rights, the role in the obesity epidemic, and legal and illegal negative environmental impacts. The infringement of these rights and the negative environmental effects (allegedly) involve the world's leading food companies, and are not simply problems that are caused by anonymous "bad guys", "laggards" among the industry population, or only small and medium-sized enterprises.
Many leading companies in the fully packaged food industry are however active in individual or joint corporate social responsibility (CSR) initiatives, sometimes being involved in various initiatives at the same time. Because food is a daily necessity and brands are easily recognised, companies are vulnerable to reputation damage and

reactions or demands by consumers. Therefore the food industry is certainly one of the leading sectors when it comes to CSR. The leading companies in the food industry, such as Unilever, Danone and Coca Cola, are, however, active in more mainstream initiatives, such as the Global Compact, SAI platform, World Business Council of Sustainable Development and various voluntary sub-sectoral initiatives, and are involved much less - or not at all - in initiatives that are viewed as more credible by civil society organisations such as organic, FairTrade and to a lesser extend sa8000 and ETI. Apart from being more demanding in terms of commitments and sustainability effects the former initiatives may still be too marginal or ill-adapted to the scale of leading processors and the problems in this industry. Moreover, most initiatives in the overview focus on CSR issues in *production* –where arguably problems are greater- and not on (*higher) processing* in the supply chain, except for obesity and packing issues.
In order to deal with national, regional and international concentrations in some parts of the processed food industry, this report shows that there are not enough competition policy instruments. There is also insufficient capacity to deal with less transparent forms of concentration and abuses that are used in the processed food sector, such as strategic alliances and cartels or abusive selling practices. When not discovered, developing countries' industry and consumers can suffer from higher prices and less access or choice.

Insufficient measures have so far been taken to deal with buyer power and the exploitative pressures by dominating supermarkets on producers' income. A few countries have legislated to rebalance the relationship between supermarkets and suppliers, and against abusive practices such as below-cost selling. However, many more countries need to take action and also deal with the wider problems resulting from buyer power, especially in the relationship between Northern supermarkets and Southern suppliers. A major obstacle to developing more and better competition policy and making competition authorities take action against concentrations and buyer power is that competition policy is aimed at protecting the interests of the consumer, and not the supplier (except in some countries, such as South Africa).
The lack of competition policy instruments means that current free trade and investment agreements are wrongly based on the assumption that there are large numbers of competitors in all sectors. While government barriers to trade and investment are being removed, the removal of private barriers to market entry and trade, especially for developing country producers, is not progressing at the same speed.

As a result of these trends, market structures and legal frameworks, some large food companies and multinationals, and a select group of supermarket chains have expanded enormously and have captured profit making opportunities in developing countries. Their influence is restructuring developing countries' agricultural systems and processing industries in such a way that many poor and marginalised groups might remain excluded.

Only a small minority of enterprises or workers in developing countries can share the income from the growth and exports of the processed food industry. To reverse this trend, measures must be taken by governments and companies to make purchasing practices and contracts more equitable, giving stakeholders more rights to seek remedies against the abuses of foreign food companies, including in the home countries and through international agreements. The public also needs to be better informed, based on more research and investigations, so that they can take action when they shop and raise the public and political debate: the activities undertaken by UK NGOs to tackle the growing influence and buyer power of supermarkets is proof that more political action is possible.

Contents

Introduction

This report is part of a series of SOMO reports that identify structural and corporate obstacles to poverty eradication and sustainable development, with a particular focus on developing countries. The focus of this report is on whether developing countries can create more added value by processing agricultural products, from primary processing to packaged food and drinks to the consumer, in a way that contributes to the eradication of poverty and sustainable development.

Given the decreasing commodity prices in real terms, many developing countries have long seen the importance of moving from commodity production to the processing industries , including for export. The benefits are considered to be: more sales at higher prices, better incomes and employment, exports that are easier to store and transport, higher foreign exchange earnings, improved stability of commodity prices and producers' income, transfer of technology for production and handling of food, availability of better products and diets.
However, given the increasingly complex structures of local, national and global markets with their supply chains and value chains that include developing countries, there are doubts regarding whether developing countries can increase their participation in the processed food industry, trade and exports, and capture benefits and extra revenue as a result.

- Chapter 1 of this report looks at the level of production, sales and international trade of processed food, and the role of developing countries.

- Chapter 2 analyses the major players in the food and drink industry – from primary processing to retailing -, their strategies and level of concentration, and their impact on developing countries' expansion of their own processed industries.

- Chapter 3 identifies existing malpractices in the processed food and drink industry, which are undermining the benefits for developing countries, people and the environment. The chapter also provides a short overview of existing corporate social responsibility initiatives that should tackle some of the problems.

- Chapter 4 examines the role of standards, trade and investment agreements and their negotiations, related to the exports and retailing of processed food and drinks, linking them to the phenomena and strategies explained in the previous chapters.

- Chapter 5 looks at why competition policy is still not offering some solutions to the problems identified in the sector.

Within the scope of this report, some issues have not received full attention and some need more research - the impact of the processed food and drink sector on the income and conditions of farmers and commodity plantation workers, for example.

This report hopes to make a contribution towards raising and strengthening the debate on how politicians, civil society, consumers and businesses themselves need to find solutions to problems in the sector that are undermining poverty eradication and sustainable development. This report offers some recommendations to that extent. What is worrying is that - in the negotiations on free trade in agriculture, for instance - many political decisionmakers do not have enough understanding of how the agribusiness market has changed and how some sectors have become directly or indirectly concentrated, with a few companies globally controlling some of the sectors. The role of investment policies and the link to trade policy is another issue which is given little attention.

SOMO sees this report as an invitation to further research and activities by researchers and non-governmental organisations throughout the world, which could lead to structural change in the processed food sector. SOMO welcomes comments and recommendations, and will use them in its activities and research on these issues in the coming years. Comments can be sent to: info@somo.nl, and new information will be published on www.somo.nl.

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Amsterdam, December 2006

Chapter 1
Processed food: outline of production, trade and consumption

1.1. Introduction

This chapter will provide a short overview of the processed food sector. Key figures and trends will be discussed on trade, production, products, retail sales and prices. The focus and the analyses of these trends will be primarily on developing countries.

In this report, processed foods are agricultural products intended for human consumption that have received some higher form of processing. This means that many semi-processed food products (vegetable oils, sugar, dairy, meat etc) are included in the analyses and figures but fresh fruits and vegetables and unprocessed commodities such oil crops and cereals are not. In addition many food-commodities that have received "simple" processing, such as tea, coffee (beans) and cocoa before they enter the world market are generally not considered to be semi-processed foods in the literature and therefore are (also) not included in the figures on world trade and production. Nevertheless, some of these food products/commodities are discussed in this chapter and other chapters in this report. The reason being that data was readily available for these products on the value added throughout the supply chain from producer to consumer, which is an important focus of this report. Another reason is that in the case of tea, for example, most processing is already carried out in the country of origin, and the exported product is already ready to drink.

The processed food sector is massive: worldwide processed food sales amounted to 3.2 trillion US dollars, or about three-quarters of total world food sales in 2002[1]. 60% of all processed food sold worldwide are bought by consumers in the US, EU and Japan. The processed food industry is one of the world's major industries, employing millions of people worldwide. In the EU, for instance, the food and drink industry is the largest of all processing industries in terms of people employed and turnover. With just over 1 billion US dollar turnover in 2004, the food sector accounts for 14% of all EU processed industry turnover and employs 4 million people[2]. Among developing countries it is the most important manufacturing industry (ISIC divisions), capturing a total of 13.1% of total manufacturing added value (2004). With 29.9 % of total manufacturing value, food processing is even more important in the least developed countries[3].

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1 A. Regmi & M Gehlhar "New Directions in Global Food Markets," Agriculture Information Bulletin (USDA), 794 (February 2005), p1; Figures in the "New directions …" article are based on Euromonitor data, a commercial vendor of market data, from 2003. Figures apply to retail and food service sales of packaged food (about 63%) and drinks (37%) ("New directions.. p.6).

2 CIAA, Data and trends of the EU food and drink industry 2005 (Brussels: CIAA, 2005).

3 UNIDO, The International Yearbook of Industrial Statistics 2006 (Abingdon: Marston Book Services

1.2. Popularity of processed food

Worldwide sales in processed foods grew considerably over the past three decades[4]. Consumers have more money to spend on food than they used to - global gross national income per capita in inflation-adjusted US dollars doubled on average over the last four decades of the last century[5] - and consumers with higher food budgets tend to buy more processed foods, both in absolute and relative terms. People in high-income[6] (developed) countries, for example, spend about 1000 US dollars on packaged food per year, while consumers in low-income (developing) countries spend only about 20[7]. And while low-income country consumers spend as much as 45% of their income on food and high-income country consumers only about 15%, the share of processed food in their food expenditures rises from 15 to 50% respectively.

1.2.1. Processed food sales grow in developing countries in particular

With much higher growth in population, urbanization and income[8] than developed countries, more people with busy lives and increased participation of women in paid employment, developing countries are very attractive markets for processed food retailers and producers. Processed food sales in these countries are growing at a much faster pace than in developed countries (see Figure 1). This accelerated growth is to a large extent being boosted by changing diets, for instance increased consumption of animal-based products (meat and dairy) and other processed products such as meal preparation items (oils, sauces), pastas and cereals. In developed countries, growth in processed food sales is especially associated with increasingly hectic lifestyles, growing numbers of single-person households and other tendencies that call for labour-saving, convenience and/or ready-to-eat foods. Added qualities such as health claims, innovation and mere attractiveness through advertisement, availability and variety drive processed food sales, particularly in developed countries[9]. Food companies adapt their business strategies to accommodate and/or initiate these changes in preferences (see Chapter 2 for a more detailed discussion).

Ltd., 2006), p.65-67; data excludes China, processed food are in this case ISIC code 15, food and beverages.

4 A. Regmi & M Gehlhar “New Directions in Global Food Markets,” Agriculture Information Bulletin (USDA), 794 (February 2005), p6.

5 A. Regmi & M Gehlhar, “Consumer Preferences and Concerns Shape Global Food Trade,” FoodReview, 4 (3) (September – December 2001), p4.

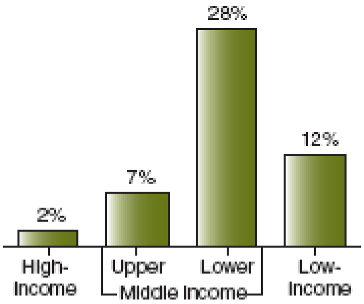
6 World Bank classification, low income and middle income countries are considered to be developing countries, high-income countries are developed countries.

7 A. Regmi & M Gehlhar “New Directions in Global Food Markets,” Agriculture Information Bulletin (USDA), 794 (February 2005), p 8-9.

8 A. Regmi & M Gehlhar, “Consumer Preferences and Concerns Shape Global Food Trade,” FoodReview, 4 (3) (September – December 2001), p4.

9 Euromonitor, The World Market for Packaged Food, June 2006, <http://www.euromonitor.com> (3 August 2006).

Figure 1: Growth in annual retail sales of processed foods 1996-2002 in aggregated countries[10]



1.3. Trade in, and production of processed food

World trade in processed food has grown from roughly 20 billion US dollars in 1970 to about 200 billion in 2002 (see Figure 2). In 2002, however, only 6%[11,12] of processed foods consumed worldwide were processed foods that had been traded internationally. By way of comparison: 16% of major bulk commodities produced are traded internationally[13].

There are several factors that explain why world trade in processed foods is relatively minor. On the one hand, current multilateral trade rules favour trade in unprocessed or semi-processed commodities at the expense of more processed products (see Chapter 5, for a more detailed discussion). This is an important reason why commodities and semi-processed products are traded internationally more than are manufactured foods (packaged and/or more processed food items)[14]. On the other hand, multinational food processors which have expanded their markets worldwide mostly turn to local processing to cater for local preferences while reducing transportation costs. In other words, accelerated processed food sales by these companies are sustained through foreign direct investment (FDI) rather than through trade. Export sales by US food companies, for example, are a fifth of their sales through FDI, which amount to 150 billion dollars[15].

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10 A. Regmi & M. Gehlhar, “Processed Food Trade Pressured by Evolving Global Supply Chains,” Amber Waves (Economic Research Service/USDA), 3(1) (February 2005), p14.

11 Idem, p1.

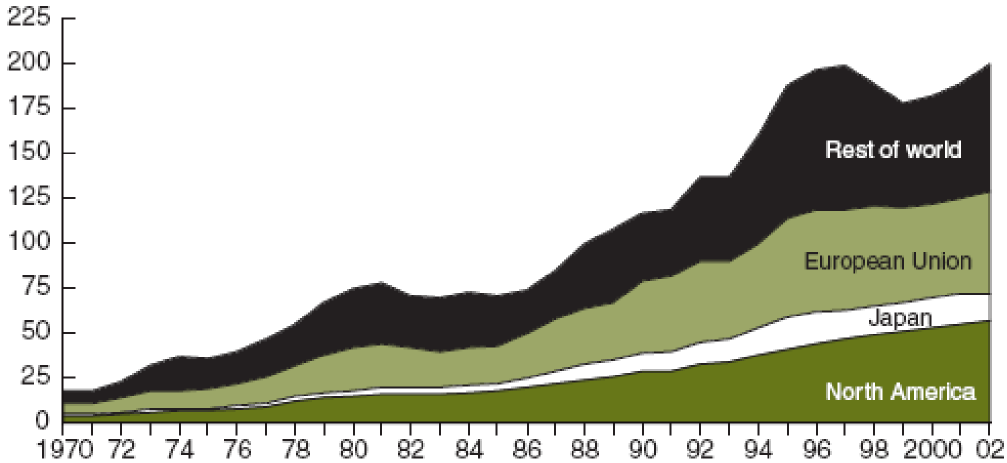
12 M. Gehlhar, United States Department of Agriculture, e-mail 09-08-2006; Data excludes intra-EU trade of roughly 100 billion US dollars which would make it roughly 10%. Data for this figure excludes commodities such as tea, coffee and cocoa.

13 A. Regmi & M. Gehlhar, “Processed Food Trade Pressured by Evolving Global Supply Chains,” Amber Waves (Economic Research Service/USDA), 3(1) (February 2005) p1.

14 Idem, p12.

15 Idem, p14.

Figure 2: World trade in processed food in US billion dollars



source: Economic Research Service/USDA

1.3.1. Processed food from developing countries

The literature on processed food trade indicates that both developed and developing countries have profited from increased trade in processed foods. As already mentioned, most processed foods are sold and consumed in developed countries, so it is no surprise to find that developing countries captured a much smaller part of worldwide processed food trade than developed countries (see figure 2). While no precise and/or recent figures could be found in the literature on world trade processed food trade patterns, two sources (ACIAR and USDA) suggest this share to be between 27%[16] and roughly 36%[17] of world processed food trade in value. These indications are in line with UNIDO figures on added value captured by developing countries of total added value in the processed foods sector worldwide, which amounted to 24.5% in 2004[18].

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16 P. Athukorala et al., "International Food Safety Regulation and Processed Food Exports from Developing Countries: the Policy Context and the Purpose and Scope of the Research Project," The Australian Centre for International Agricultural Research (October 2002), p44; These figures are somewhat different than those from the USDA, which is the result of a different selection of data sets included. Awkwardly their figures include data on feed and tobacco. And some developing countries such as China are not in the sample.

17 A. Regmi & M. Gehlhar, "Processed Food Trade Pressured by Evolving Global Supply Chains," Amber Waves (Economic Research Service/USDA), 3(1) (February 2005) p1; figure is an estimate of this share from their figure on processed food trade. In the figure "the rest of the world" is taken to be roughly equivalent to the share of developing countries although it almost certainly includes data from countries such as Australia and New Zealand.

18 UNIDO, (2006) p50.

Box 1: Why consumer-ready processed foods are traded less than other (processed) foods

Most consumer-ready processed foods are processed in the target markets. Factors affecting the geography of processed food include not only tariff escalation, transportation costs and varying national consumer preferences, but also growing conditions. A distinction can be found in the literature between land-based and manufactured foods.

Manufactured (non-land based) foods are typically products in which processing has transformed the many ingredients that have been used into a totally new product, such as breakfast cereal, bread, frozen pizza, candy, beer and soft drinks. These ingredients are often commodity or land–based products such as meat products, milk, coffee, tea, flour and sugar. These inputs can be sourced from anywhere and need not, and sometimes cannot, be produced in the target market countries. In contrast to land-based products, manufactured (more processed) food can be produced anywhere, provided you have the right infrastructure (processing facilities, transport)[19]. Because of these factors, among others, multinational food companies tend to produce these manufactured foods through foreign direct investment (FDI) in the country or region of consumption.

In order to produce land-based products, favourable growing conditions are necessary. They therefore cannot be produced everywhere, and are less likely to be produced through FDI. The leading food multinationals focus on processing and generally do not invest in production of commodities. Land-based processed products have generally been less processed than manufactured foods (drying, freezing, slaughtering, canning). These products tend to be highly traded internationally and processed close to *production*. In contrast, manufactured products tend to be traded locally only and are produced close to *consumers*.
However the distinction between land-based and manufactured food does not always explain the differences in processing locations. There are some exceptions in each category. For instance the ingredients for beer (water, barley (or other grains) and hops) are widely traded internationally and beer does not resemble its original inputs (although in some cases arguably beer looks much like water). These factors make beer a typical manufactured product. Yet some international brewers, such as Heineken, export beer overseas to give their product an air of exclusivity despite higher transportation costs.

The same goes for some land-based processed products as well. To grow tea, which in the literature often is considered to be a commodity rather than a (semi-)processed product, for instance you need suitable “inputs” (e.g. suitable climate, enough land, (cheap) labour and processing facilities). Additionally, because tea leaves need to be processed (withered) right after harvesting, most of the processing of tea takes place in tea-producing countries. Tea is traded extensively internationally, and additional processing, mostly packing for consumer convenience and blending, takes place in countries that import tea. Tea can therefore be considered to be a typical land-based product. Nevertheless, there are companies such as Dilmah that successfully export ready-to-drink tea from Sri Lanka, one of the world´s leading tea exporting countries, to consumers in tea importing countries.

[19] Idem, p15.

However trade from developing countries is considerable. For example total EU imports of processed food amounted to roughly 52 billion US dollars in 2005. With 6 and 4.7 billion US dollars respectively, Brazil and Argentina are the leading exporting countries to the EU, outperforming the third leading country, the US, by and large. Other leading developing country exporters to the EU are China, Turkey and Chile with 2.2, 1.8 and 1.2 billion US dollars[20].

The available data on the development of the share of developing countries in global processed food trade over time is contradictory: ACIAR indicates a small growth from 26% to 28% from the eighties to the nineties, USDA data suggests a small decrease in this same period. FAO data indicates that the share of developing countries in trade in processed agricultural products (including non-food commodities such as tobacco and cotton) decreased from 27% in the years 1981-1990 to 25% in 1991-2000[21]. More research is needed to gain more precise and recent figures on both the size and development of the share of developing countries in processed food trade worldwide. No readily available precise figures on world processed food sales and trade over time could be found.

When zooming in on developing processed food exports, it is clear that trade from developing countries is concentrated: roughly half of all developing world exports by value were captured by just four countries in 1999[22]. In descending order of importance, these were Brazil, Thailand, Malaysia and Argentina. However it should be noted that food trade from developing countries is generally concentrated. Two countries, Brazil and China already account for a quarter of all developing country agricultural exports by value (UN Comtrade, 2003)[23].

There is also evidence that generally high and middle-income *developing* countries shared more in the growth of trade in processed food than low-income countries[24,25]. An analysis by ACIAR found that countries such as Bolivia, Chile, Indonesia, Korea, Malaysia and Thailand experienced annual growth rates close to or exceeding fifteen per cent from 1970-1999. In contrast, countries that exhibited annual growth rates of five per cent or less were Cameroon, the Dominican Republic, Ghana, Nicaragua, Nigeria, Sudan, Senegal, Tanzania and Zambia. Bangladesh is a notable exception among low-income countries: the country's exports growth was double that of any other low income developing country.

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[20] CIAA, Data and trends of the EU food and drink industry 2005, 2005, p10, <http://www.ciaa.be/documents/news_events/Data_&_Trends_2005.pdf> (22-11-06).

[21] FAO, The State of Agricultural Commodity Markets, 2004, p26, <ftp://ftp.fao.org/docrep/fao/007/y5419e/y5419e00.pdf> (22-11-06).

[22] P. Athukorala et al., "International Food Safety Regulation and Processed Food Exports from Developing Countries: the Policy Context and the Purpose and Scope of the Research Project," The Australian Centre for International Agricultural Research (October 2002), p46.

[23] Calculations by R. Vossenaar (2006).

[24] P. Athukorala et al., "International Food Safety Regulation and Processed Food Exports from Developing Countries: the Policy Context and the Purpose and Scope of the Research Project," The Australian Centre for International Agricultural Research (October 2002), p5.

[25] FAO, The State of Agricultural Commodity Markets, 2004, p26, <ftp://ftp.fao.org/docrep/fao/007/y5419e/y5419e00.pdf> (22-11-06).

To illustrate further: according to the FAO the share of least developed countries in world trade in processed agricultural products declined from 0.7% to 0.3% from the 1980s to the 1990s[26].

→ **Critical issue**

While on the supply side, trade in processed foods has been greatly facilitated by lower transport costs and improved technologies for packaging and processing, these very same factors still form an insurmountable barrier for many developing countries, and especially LDCs, to access markets. Many developing countries lack the appropriate technology, infrastructure (distribution, storage), marketing knowledge/ capacity and other financial or human resources to seize opportunities for trade in processed foods (see chapter 2 for a more detailed discussion). In addition, along with concentration at the country level, there is also concentration at the corporate/industry level. Bulk commodity trade and processing is often dominated by multinational food companies. And while concentration in for instance packaged food worldwide is rather low in some specific higher-value chains concentration can be high. Such concentration can hinder market entry for developing country food processors (see Chapter 2 for a more detailed discussion)

1.4. Focus on products

Trade in processed agricultural products (juices, meals, cakes, canned and preserved products…) grew more quickly than trade in primary agricultural products (cereals, beans, fresh fruits and vegetables..) over the past 20 years[27]. During this period in particular, processed forms of fish, fruit, vegetables, tropical beverages, cereals, pulses, and poultry products have shown exceptionally high export growth rates.

When looking at developing country exports, some remarkable shifts can be found in the types of processed foods exported from 1970 to 1999[28]. Most notably, the export of processed fish products grew over the last three decades. Exports of dairy products, flour and cereals, preserved fruits and vegetables also grew, although to a much less pronounced extent than those of processed fish. Trade in sugar and molasses and meat products diminished sharply in the same period.

Concentration in developing world exports is especially high in meat, animal and vegetable oils, various animal products, beverages, spirits and vinegar, sugars and confectionary. The two largest exporters for these products control between 40% and 60% of all developing country trade by value (UN Comtrade, 2003)[29].

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26 Idem.
27 Idem.
28 P. Athukorala et al., "International Food Safety Regulation and Processed Food Exports from Developing Countries: the Policy Context and the Purpose and Scope of the Research Project," The Australian Centre for International Agricultural Research (October 2002), p6.
29 Calculations by R. Vossenaar (2006)

Box 2: The tea sector in Indonesia

With an annual production of 165,000 and an annual export of 105,000 tonnes, Indonesia is the eighth largest producer of tea in the world, and fifth largest exporter (2004, Faostat 2006). 64% of total tea production was destined for export markets in 2004. Tea is an important source of income for Indonesia. However, while revenues vary from year to year according to world supply and demand and internal supply chain factors, revenues are decreasing on average. There are several factors that explain this trend. Firstly, world tea prices corrected for inflation have sunk dramatically in real terms. This is the result, among other things, of worldwide overproduction (production outpacing consumption). On average, however, regular prices for Indonesian tea have fallen over the last 9 years as well. In addition, there is the trend that prices for Indonesian tea have decreased compared to those of Sri Lankan tea, the leading tea exporter in the world. Fluctuating quality, marketing weakness, high freight costs and lack of government support are undermining Indonesia's competitiveness on the world tea market. It should be noted that the government is an important actor in this country's industry: 31% of the acreage planted is run by government estates and most of the production is destined for export. Indonesia's exports are strongly focused on bulk black tea. In 2001, only about 6% of tea exports consisted of consumer packaged (ready to drink) tea. The main factors that have hindered the capture of more value added in the supply chain via packaged tea exports are the value added tax levied on tea since 2001, lack of investment incentives and government support, and tariff harmonisation (see Chapter 4).

Source: V.R. Kustanti, Business Watch Indonesia, Tea Sector in Indonesia (2006) (unpublished report); FAO, The state of agricultural commodity markets 2004, Annex 1, Table 1.

→ Critical issues

FAO data for cocoa and coffee shows that higher forms of processing are increasingly taking place in developed countries, for at least some products. For example, the top ten coffee-producing countries saw their share in world roasted coffee exports fall from 8% between 1975–80 to 2% between 1998–2002. At the same time, however, roast coffee exports as a share of total coffee exports increased from 3% to 16%. Similarly, chocolate exports as a share of total cocoa trade increased from 22% in 1975–80 to 58% in 1998–2002 while, during the same period, the share of the top ten cocoa producing countries declined from 2.4% to 2%[30].

The costs of the ingredients used to make a processed food such as coffee or chocolate represent only a fraction of the retail price. This means that most added value is generated upstream. Decreasing shares in processing usually mean decreasing shares in profits, at least for cocoa and coffee producing countries. When looking at total added value generated in the processed food sector

[30] FAO, The State of Agricultural Commodity Markets, 2004, p.26, <ftp://ftp.fao.org/docrep/fao/007/y5419e/y5419e00.pdf> (22-11-06).

worldwide from 1995 to 2004, however, the share that developing country industries captured grew slightly, from 22.4 to 24.5 %[31].

Box 3: Dilmah

Dilmah tea is an example of a processed food (drink) product that is produced, processed and packaged in a developing country and successfully marketed in and exported to 90 countries worldwide. Based and originated in Sri Lanka, Dilmah is a brand of tea being marketed as a 'single source' Ceylon (Sri Lanka) tea. In this, it attempts to distinguish itself from the larger tea brands, that mostly blend tea originating from various countries worldwide. The brand exists since 1985 and claims to be among the top ten largest tea brands in the world.

The Dilmah brand is owned by the MJF group, named after its founder Merril J. Fernando. The group owns various tea packaging and export companies and the majority share of a plantation company creating a vertically integrated tea business. The group also has a strategic alliance with two other large plantation companies. The packaging and producing divisions of the group are: Ceylon Tea Services, which exports bagged tea under the Dilmah brand, MJF exports Ltd. which sells tea in bulk to traders and blenders and MJF Teas Pvt. Ltd., specializing in the Soviet States, where it markets and sells tea in retail under the Dilmah brand. Other activities of the group include a spa, tourist resorts and a charitable foundation.

According to their website, the MJF group itself employs approximately 800 people, while there are 25,000 employees working at plantations supplying to and/or owned by the group. The three plantations produced an estimated 23,000 tons of tea in 2003, of which the group exported 8,000 tons.

Source: Dilmah website www.dilmah.com (14-12-2006)

1.4.1. Prices

No readily available indication of processed food prices worldwide over time could be found. Data is available on commodity prices, however, which include those of some processed foods. Over the last four decades, real world market prices (prices corrected for inflation) for agricultural commodities have declined by about 50%. In the case of coffee and cocoa, real prices plummeted by almost 80% and 75% respectively from the beginning of the seventies to 2002. Other commodity prices that fell above average include butter, wheat, rice and sorghum[32].

Yet prices for commodities are in general highly volatile. Since about 2002, commodity prices have rebounded or have at least levelled off[33]. In other words, food and beverage makers were dealing with higher prices for many key commodities, such as dairy, wheat

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[31] UNIDO, (2006) p50.

[32] FAO, The State of Agricultural Commodity Markets, 2004, p.38, <ftp://ftp.fao.org/docrep/fao/007/y5419e/y5419e00.pdf> (22-11-06).

[33] Idem, p.8.

and sugar, over the last 3 years (from 2003) and especially in 2004. While food companies were able to pass along these higher cost to consumers in the form of a higher retail price, retail prices have generally been under pressure from competition between retailers (price wars) and private label sales[34].

Box 4: Deteriorating terms of trade for developing countries?

As discussed above, the relative amount of money that finds its way to farmers in the USA indirectly via the sales of processed foods is declining. At the same time commodity prices are falling on average, reflecting a global oversupply. For the many developing countries whose economies depend heavily on exports of primary and semi-processed food commodities, these factors put revenues under pressure. In addition if prices for imports of developing countries are become higher terms of trade for these countries are deteriorating.

Specific comprehensive international data on net trade of processed foods and/or the ratio of net trade in food commodities to processed foods are not readily available in the literature. However, FAO data on agricultural imports and exports clearly shows that in terms of trade, the ratio of prices of exported goods to the prices of imports have deteriorated significantly since the mid-eighties for developing countries. For instance, from 1985 to 2001, prices for least developed country agricultural exports fell by half relative to those of the agricultural products they import. This trend was even more pronounced for prices of agricultural exports versus prices of manufactured goods (not processed foods specifically) imported[35]. Similar effects might occur for trade in processed foods, clearly more research is needed in this area. Bearing this trend in mind, it is also important to know where the inputs for processed foods sold on developing country markets are sourced from. It is possible that dietary upgrades, such as more animal-based products, as we have seen in chapter one, have led to increased imports, making developing countries more dependent on food imports.

Research by the USDA shows that consumer expenditure on food in the USA rose by 37% in the nineties, but that the farm value (the money that is spent on agricultural inputs for (processed) foods) increased by 13% only. The surplus was mostly taken up by higher costs for labour, packaging, corporate profits and energy inputs. For example, the share of advertising cost in total food expenditures doubled in this period [36]. USDA research also indicates that the retail price of a basket of food rose by about 72% from the early eighties (1982 to 1984) to 2001 while farm gate value of the same basket increased by only 6%. This meant that the value of the commodity as a proportion of the retail price of the total basket dropped from about 35% to 21%.[37]

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[34] See for instance: Euromonitor, The World Market for Packaged Food, June 2006, p.11 <http://www.euromonitor.com> (3 August 2006).

[35] FAO, “The State of Agricultural Commodity Markets”, 2004 p.12 &13.

[36] H. Elitzak, “ Food Marketing Costs: A 1990’s Retrospective,” FoodReview 23 (3) (Sep-Dec 2000); data excludes imported food.

[37] USDA website, “Food Marketing and Price Spreads: USDA Market Basket”, June 2002, <http://www.ers.usda.gov/Briefing/FoodPriceSpreads/basket/table1.htm> (8 august 2006); Both retail price and farmgate value fluctuated during this period

The above USDA statistics exclude imported foods and commodities. In relatively simple processed foods such as coffee and tea, farm value to retail price ratio is actually much lower. Therefore, if processed foods based on commodities from outside the USA were to be included, this farm value to retail price ratio is likely to be lower indeed (see section below on economic issues).

There is evidence that food factory gate prices are declining less than farm gate prices. DEFRA (Department for Environment Food and Rural Affairs, UK) compared both real farm, factory and retail prices of food in a number of EU countries over a period of time. The results show that all these prices fell over a period of between 10 and 25 years. However, the decline was most pronounced for real farm gate prices (at around 3% per year) and less pronounced for real factory gate prices. With close to 0.8 %, per year real retail prices experienced the smallest decline. Comparison of factory gate prices and retail prices of food and drink in Germany, Italy, France, UK, Japan and the US reveal that factory gate prices fell on average 1.5 % faster than retail prices during the 1990s. The most pronounced relative decline was recorded in the US during this same period (about 2.1%)[38].

[38] DEFRA, Development of Competitiveness Indicators for the Food Chain Industries, 2002, p.53-57 <http://statistics.defra.gov.uk/esg/reports/competit.pdf> (22-11-06).

1.5. Conclusions

Processed food sales are growing worldwide, and particularly in developing countries. Yet worldwide sales dwarf world trade in processed food reflecting the fact that most processed foods are produced in the countries where they are consumed. However there is considerable and growing trade in especially (land-based) semi-processed products. Trade in more processed consumer-ready manufactured products is more restricted. While the patterns of trade and added value in processed food outlined in this overview are insufficiently clear to be able to draw definite and specific conclusions, it seems important for developing countries to focus on processed foods production for both foreign and domestic markets.[39] Other trends that are in favour of such growth strategy are the fact that factory gate prices tend to be more stable than farm gate prices and the fact that food processing industries in developed countries have become such major sectors with corresponding turnover and employment. However capturing (overseas) processed food markets requires large investments in marketing and infrastructure, especially for higher-processed manufactured products. Additionally, competition is fierce: trade from developing countries is concentrated, as is the processing industry both at the primary processor level (semi-processed commodities) and at the higher processing levels for ready-to-eat products (see Chapter 2 for more details on the latter). More analyses of trade, added value, FDI and the economic impact of the sector in various sub sectors of the processed food industry is important in order to learn which specific strategies (e.g. focus on which processed foods, markets etc) can be best adopted by developing countries.

[39] See for instance: J. Wilkinson, “The Food Processing Industry, Globalization and Developing Countries,” Electronic Journal of Agricultural and Development Economics, vol1(2) (2004), p184-201.

Chapter 2
The importance of market structures and company strategies for developing countries

2.1. The processed food markets

The processed food sector is only a part of the global food value chain, as shown in Figure 3. However, as will be explained in this chapter there are strong links between the various parts of the chain which also influence each others' strategies.

Figure 3: The global agrifood business chain and its top companies

Note: CR5 represents the market share of the top five companies listed in the global retail industry
Source: Based on stock market data, http://www.wsj.com and WDI 2005, quoted in J. von Braun, The World Food Situation - An Overview, (Prepared for CGIAR Annual General Meeting, Marrakech, Morocco), 6 December 2005, p.5 <http://www.ifpri.org/pubs/agm05/jvbagm2005.asp> (viewed 30 October 2006).

The food-processing industry can largely be divided in two main groups of companies with a different range of products, which have different strategies for the production, trade and sales of their different products (see also Chapter 1,
Box 1)
Firstly, there is the market of the primary and middle stages of processing of commodities, or semi-processing of food, such as soy crushing for oil, milling of wheat and maize for flour, and grinding of cocoa.
The other market is that of manufactured food and drinks, or packaged processed food and beverages, ready to eat and for direct sale to the consumer, primarily through retailers and catering. It includes food products such as packaged bakery products, margarines, dairy products (including ice cream), frozen food and prepared meals, confectionery and biscuits, soft drinks, alcoholic and non-alcoholic beverages, ready tea and coffee.

However, it needs to be noted that some of the very large packaged food companies also engage in semi-processing, such as Nestlé grinding cocoa.

It is difficult to find an overview of the top companies in the world which includes both market categories. Table 1 is an old overview from 2002, with figures of 2005 which are not always comparable. What is striking is the growth of Cargill, ADM and Nestlé in 2005.

Table 1: The top 10 food and beverage companies in the world (2002 and 2005)

Company	2002 food & beverage sales ($US millions)	2005 in bn US$
1. Nestlé S.A. (Swiss)	$54,254	Total sales: US$ 76.11 bn[40]
2. Kraft Foods, Inc. (US)	$29,723	Net revenue: US$ 34.11 bn[41]
3. Unilever plc. (NL)	$25,670	Total sales (including non-food): US$ 49.35 bn[42]
4. PepsiCo Inc. (US)	$25,112	Total sales: US$ 32.56 bn[43]
5. Archer Daniels Midland Co. (ADM) (US)	$23,454	Net sales for the fiscal year ending 30 June 2005: $35.9 bn44
6. Tyson Foods (US)	$23,367	Total sales : US$ 26.01 bn45
7. Cargill Inc. (US)	$21,500	Revenu for the fiscal year ending 31 May 2005:US$ 71.1 bn46
8. ConAgra Inc. (US)	$19,839	Total sales : US$ 14.35 bn47
9. Coca-Cola Co. (US)	$19,564	Total sales : US$ 23.10 bn48
10. Mars Inc. (US)	$17,000	Total sales: _US$ 18 bn49

Source for 2002 figures: Food Engineering, November 2003, www.foodengineeringmag.com : quoted by ILO: http://www.ilo.org/public/english/dialogue/sector/sectors/food.htm <viewed 25 October 2006>

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40 Nestlé, Group figures, 2004-2005: Swiss Francs 91 075 million: value in US$ based on Forbes Global 2000 < http://www.forbes.com/lists/2006/18/06f2000_The-Forbes-2000_Company_13.html> (viewed on 10 December 2006).

41 Kraft Food Inc, Financial Highlights 2005. p. 16 <http://www.kraft.com/pdfs/kraft05ar_print_final_singles_screen.pdf>

42 Unilever, Jaarverslag en jaarrekening 2005: Sales € 39.67 ;net profit € 3.97: value in US$ based on Forbes Global 2000 < http://www.forbes.com/lists/2006/18/06f2000_The-Forbes-2000_Company_19.html>

43 <http://www.forbes.com/lists/2006/18/06f2000_The-Forbes-2000_Company_14.html> (viewed on 11 December 2006).

44 <http://www.admd.com/./AboutUs.aspx>

45 < http://www.forbes.com/lists/2006/18/06f2000_The-Forbes-2000_Company_19.html>

46 Cargill, "Cargill reports fourth-quarter and fiscal 2005 earnings", press release, 23 August 2005, <http://www.cargill.com/news/news_releases/2005/050823earn.htm> (viewed 10 December 2006)

47 <http://www.forbes.com/lists/2006/18/06f2000_The-Forbes-2000_Company_5.html>

48 Ibid.

49 <http://www.hoovers.com/mars,-incorporated/--ID__40297--/free-co-factsheet.xhtml>

It is important to note that 8 of the 10 top global food and beverage companies have their headquarters in the US. Although all the top companies have operations in many countries of the world, this domination of US agricultural and food & drink companies is important in terms of the strategies designed by business in the sector as well as for governments who design policies to support the competitiveness of domestic companies and promote exports, and who decide on trade and investment policies and other market regulation (see Chapter 4). Unfortunately, the market structures in the agribusiness and processed food sectors are not always well known by policy makers and trade negotiators. Much of the detailed market information is held in expensive data bases.

2.1.1. The primary processing industry

Commodity processing companies are often referred to as agribusiness companies, as opposed to food manufacturers or food-processing companies producing directly for consumers. Their semi-processed products, such as palm oil and soy oil, syrups, starches and concentrated fruit juices constitute ingredients for the products of packaged-food companies, including large food multinationals, and for the food service industry (e.g. fast food restaurants). These agribusiness companies are therefore not always well known to the public. Another reason why some key global agribusiness companies are not well known is because they are family-owned companies who are not listed on the stock exchange and have a much lower obligation to disclose data about their production, trade and profits worldwide. Examples of such important family firms are: Cargill, Louis Dreyfus (Fr) and Nidera (NL). This prevents the openness and access to information needed to better understand the agribusiness markets.

What is characteristic of the semi-processed food market is the level of concentration at the national, regional or global level for many products. Not only do the top companies have very large shares of the market of a certain product, the same companies dominate many product markets. Moreover, they not only dominate the semi-processing, but also other parts of the value chain, in particular the trading and transporting of raw materials as well as the semi-processed ones, and also the fertilizer market. Moreover, some of these companies engage in other related activities such as financial services, shipping and real estate.

The following few companies are playing a dominant role[50] on world markets, with operations in many countries around the world, not least in developing countries:

- Cargill: has large shares of the world market in producing, trading and primary processing of wheat, cocoa, soy, rice, barley, beef, corn, fats, feed supplements, flax, food supplements and additives, genetically engineered products, oats, oils, pork, poultry, rape, sugar, vegetables.
- Bunge: see Box 5

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[50] Exact figures are difficult to access because of the family structures of the companies or expensive databases

- ADM: claims to be one of the world's largest agricultural processors of soybeans, corn, wheat and cocoa, producing soymeal and oil, corn sweeteners, flour, cocoa and chocolate, ethanol and biodiesel. It claims to have a wide portfolio of other value-added food ingredients, animal nutrition and industrial products.[51]

Box 5: Bunge – a major agribusiness and food company

Bunge is an agribusiness and food company with operations in 32 countries all over the world. In 2005 it had sales of US$ 24.3 bn, a net income of US$ 530 million, and employed around 23,500 employees.
Bunge is one of the largest companies worldwide in the agrochemical, agrifood and food sectors. The company claims to be the world's largest processor of oilseed, the largest producer and supplier of fertilizers to farmers in South America and the largest exporter of soy from Latin America, and a leading biodiesel producer. In Brazil, more than half of the country's meat producers use its products. It is estimated that Bunge together with Cargill and ADM currently dominate 90% of the world trade in grain. Three companies control 71% of US soy bean crushing. Bunge is an important trader of genetically modified organisms.
The company made most of its 2005 profits out of the fertilizer (agrochemical) and agrifood sectors. Bunge's food division is the smallest of the three because the company wanted to concentrate more on its other activities. Europe is the most important market for Bunge in terms of sales (37% of all sales). The other important markets are North America (29%), South America (22%) and Asia (12%). Bunge is a limited liability company registered in Bermuda and publicly traded on the New York Stock Exchange. It has numerous subsidiaries and is engaged in various joint ventures such as in Argentina and Brazil, with activities ranging from acid conversion to the construction of a terminal in the port of Guaruja, Brazil.
The company has been carefully expanding its business into China and other Asian countries through acquisitions and new investments. It aims to capture leading positions worldwide in those markets which are "most attractive" for Bunge's products. It continuously focuses on efficiency and cost reductions to increase its profitability but this profitability has come at the price of environmental damage and breach of labour standards. Bunge has been criticised for being linked to illegal and legal rainforest clearing and bonded or slave labour on land from which Bunge purchases soy.

Sources: SOMO, Quickscan Bunge, update 2006; <http://www.bunge.com/about-bunge/our-businesses/goals-strategies.html> (viewed on 7 December 2006); "CHINA: Bunge to acquire soybean plant", Just-food.com, 12 January 2006, http://www.just-food.com/article.aspx?id=86689 (viewed 7 December 2006)

High levels of national, regional and global concentration

In the US, the first part of the 20th Century saw considerable concentration of processing of some commodities such as grain, beef and pork processing, into the same hands (horizontal concentration) while in the second half of the century, a process of vertical integration began which brought several stages in the processing production under the control of the same company (processing of feed, and production and processing of

[51] <http://www.admworld.com/>

poultry, for example). Now, at the beginning of the 21st century, the top four companies involved in the processing of most agricultural commodities have market shares in the US of between 50% and 83% For example, 3 companies (including Bunge and Cargill) control 71% of US soy bean crushing, and 4 companies control 63% of US flour milling. In additional, Cargill alone controls 50 to 60% of the US fertilizer market.[52]
In Argentina Cargill, ADM, Bunge, Toepfer and Dreyfus export 78% of the wheat, 79% of the maize, 71% of the soy flour, 95% of the soybean oil and 99% of the sunflower seed oil. Similar concentrations can be found all over Latin-America.[53]

The level of concentration is often measured by the market share or concentration rate (CR) of the top 4 companies of the market (**CR4**). In the EU, for instance, 75% of the crushing capacity is in the hands of 4 multinationals, mostly the same US-based ones who are also dominating other commodity chains.

At the global level, a few large Western companies are able to capture very large shares of the global market, even if the commodities are produced in developing countries, either by small farmers (such as cocoa) who have to bear the risks of production (bad harvests, pests) or by large plantations. M. Hendrickson and W. Heffernan estimate that Cargill, ADM and Bunge currently dominate 90% of the world trade in grain.[54]

Table 3: Global market shares of top cocoa grinding companies in 2004-2005

Ranking	Company (country of headquarters)	Global market shares
1.	Cargill Foods (US)	14.7%
2.	ADM Cocoa (US)	14.4%
3.	Barry Callebaut (Swiss)	12.2%
4.	Petra Foods (Singapore)	5.8%
CR4		**47.1%**
CR9		60 %

Source: Own calculations based on S. Delodder, From value to volume based growth? The cocoa industry, presented for the European Cocoa Association, Barcelona,17 September 2005, < *http://www.eurococoa.com/activities/concoction/delodder.pdf*> (viewed on 9 November 2006)

This high level of concentration is the case for cocoa grinding (see Table 3: CR4 is 47%) and soya bean crushing, for example. Interestingly, more cocoa grinding is carried out in developing countries, where the country of origin characteristics are preserved, than in Europe and the US where most of the grinding has traditionally been done (still 65% of grinding in 2004-2005). This is explained by better consumer markets and investment

52 "Market Share Matrix Project", no date, <http://www.marketsharematrix.org/open.php?PHPSESSID=9c87268963642c18427ef2cbc6b30e60> (viewed 28 November 2005) (see http://www.agribusinessaccountability.org/)

53 W. Pengue, "A short history of farming in Latin America", April 2004, < http://www.grain.org/seedling_files/seed-04-04-2.pdf> (viewed 15 December 2005)

54 W. Heffernan, M. Hendrickson, The Global Food System: A Research Agenda - Report to the Agribusiness Accountability Initiative Conference on Corporate Power in the Global Food System, June 2005, < http://www.agribusinessaccountability.org/bin/view.fpl/1081.html> (viewed October – December 2006).

conditions in developing countries. [55] However, this does not mean that they continue to own or control this processing stage.

Company strategies

Commodity processing and other agribusiness companies have other strategies than processors of food direct consumption. Because their products can be more cheaply and easily transported in bulk, they can more easily source and locate where production and semi-processing costs are lower, whereas food manufacturers are more likely to process close to the consumer. These large agribusiness corporations operate internationally in order to profit from whatever differences in price, demand, subsidies, tax breaks, labour or environmental standards exist between countries and regions. Investments, including mergers and acquisitions by the industry nationally and internationally, investment and trade liberalisation, supported by export-led development policies, have led to concentration of this business within larger producers and traders over more than a decade.[56]

Because the profit margins in semi-processing are not always high, various large commodity processors are moving their activities up the value chain where more profits can be made.[57]

A new area of expansion for the commodity processing companies is bio-fuel, because it can result in huge returns. ADM is already producing ethanol and biodiesel, for example.[58] However, major investments must first be made, while companies have no guarantees as yet that such investments can be recouped.

→ Critical issues

The very high level of concentration of processing of, and trade in, (processed) commodities means that the dominant companies have huge economies of scale and risk-spreading opportunities. This makes it difficult for new developing country commodity processors to start processing and selling on to the world market. Even in their domestic markets, commodities that have been grown in their own country, as they have to compete with the large processing companies.

Some developing country governments that have taken measures to ensure better benefits to their economies, have met with such economic and political

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55 S. Delodder, From value to volume based growth? The cocoa industry, presented for the European Cocoa Association, Barcelona,17 September 2005, < http://www.eurococoa.com/activities/concoction/delodder.pdf> (viewed on 9 November 2006).

56 FoEE website, “The World Trade System: Winners and Losers”, November 1999, <http://www.foe.co.uk/resource/briefings/winners_and_losers.html>, (28 November 2005)

57 See for instance: R. Morais, “The Gnomes Of Cocoa”, 14 March 2005, published on <http://www.forbes.com/global/2005/0314/024_print.html> (viewed on 9 November 2006)

58 <http://www.admworld.com>

pressures, such as refusal to export tea (India)[59] or cocoa (Ivory Coast)[60], that they had to withdraw their measures (export restrictions and export taxes).

The latest rapid developments on the bio-fuel market must be carefully monitored and managed, as there are important social and environmental aspects related to producing and processing commodities (oil seeds, sugar cane, for example) for fuel, such as monoculture and its environmental harm, domination by a few companies, working conditions on plantations, distribution of the benefits along the chain, etc.

2.1.2. Packaged food

The market for packaged food, sold directly to the consumer, is in the literature mostly made up of the products listed in Figure 4.

Such categorisation of packaged food excludes the beverages sector of soft drinks, packaged drinks, and other non-alcoholic and alcoholic drinks, global sales of which are estimated at $ 641 billion.[61] The soft drink industry often focuses its activities on making the soft drink concentrates, licensing the brand to bottlers, and on global and local marketing. The above categorisation of packaged food also excludes ready-to-consume packaged meat, tea and coffee. Recent figures for all categories together are difficult to find.

Of course, retail sales of packaged food are much higher in the markets of high-income countries. Wealthier consumers in these countries are increasingly buying more high-quality and time-saving products and products with health attributes, at the expense of traditional products such as oils and fats. Sales of ready-to-eat meals are 4% of total food retail sales in the US and the UK,[62] for example, a trend that is now also visible In Eastern Europe.
However, market growth is expected to continue to be faster among developing countries, especially the emerging market countries of China, India, Thailand, the Philippines, Indonesia, and Vietnam.[63] This growth is mainly the result of increased demand (see Chapter 1) for basic processed food products such as oils and fats, dried food, and dairy products. But the breakfast cereals market has also registered spectacular sales growth in some developing countries, even if sales are still small in overall terms in these

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59 Fair Trade Organisations, "Report of Dutch India Working Group on Tea Industry", 1994, < www.transfair.ca/fairtrade/fair667.html> (viewed 6 October 2001 by Shatadru Chattopadhayay, Partners in Change, India)

60 Global Exchange, The news on chocolate is bittersweet: no progress on child labor, but fair trade chocolate is on the rise, June 2005, p. 2, <www.globalexchange.org/campaigns/fairtrade/cocoa/chocolatereport05.pdf> (viewed November - December 2006)

61 A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 6.

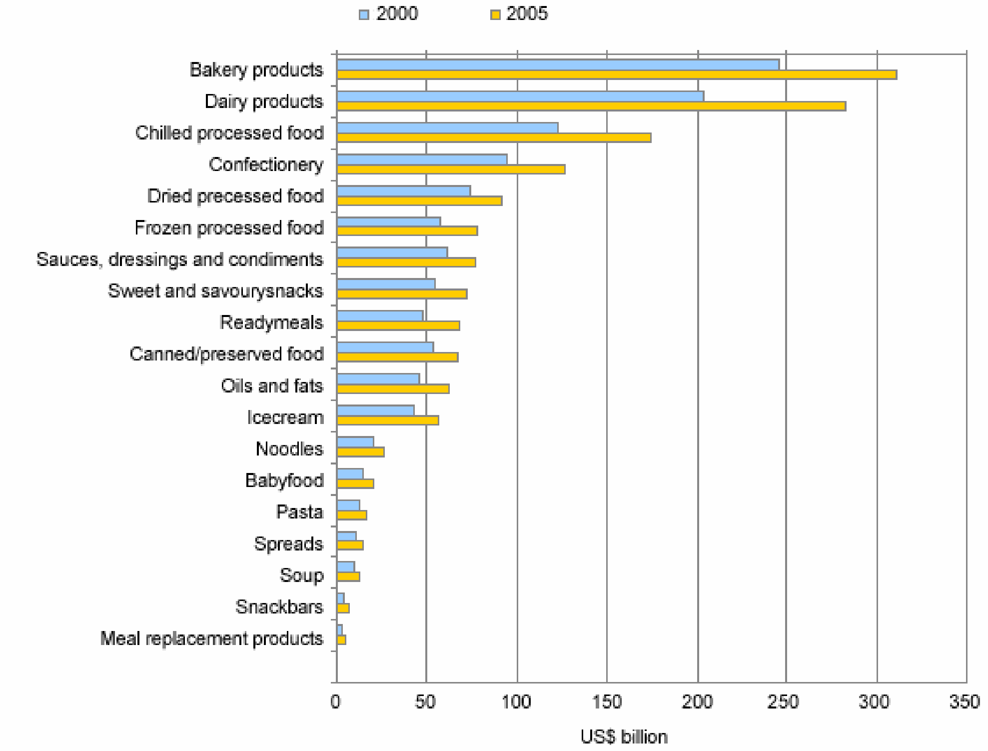
62 Idem, p. 6-10.

63 A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p.11.

countries.[64] In addition, some developing countries are starting to consume ready-to-eat meals and pasta.

Data on retail sales across regions and on foreign investment in the processed food sector seems to suggest that a global market may exist only for limited food products, and that most global food companies adapt to local tastes.[65]

Figure 4: Global packaged food: Retail value sales by sector: Value 2000/2005



Source: Euromonitor International, The World Market for Packaged Food, June 2006, chart 3 , p.13

The main players

The main companies with the largest share of the world market in 2004 were Nestlé (Swiss), Kraft Foods (US, part of Altria Group, formerly Philip Morris Companies Inc.) and Unilever (UK/Netherlands) (see Table 2). These companies have for some years held the top position of between 2.5% and 3.3% of the world market in retail value, with Nestlé making small percentage gains and the other two making small percentage losses of market share.

[64] Idem, p. 6, 14.
[65] Idem, p. 17.

Of the top ten global companies in packaged food, 6 companies are from the US while the others are European. Of the top 15 global companies, 10 are US-based while 5 or 33% have their headquarters in Europe.

Table 2: Global ranking of packaged food companies according to shares (%) of retail value, 2001-2004

Ranking	Company	2001	2002	2003	2004
2004					
1	Nestlé SA (Swiss)	3	3.2	3.3	3.3
2	Kraft Foods Inc (US)	3	3	2.8	2.7
3	Unilever Group (NL)	2.6	2.6	2.6	2.5
4	PepsiCo Inc (US)	1.9	1.9	1.9	1.8
5	Danone, Groupe (Fr)	1.2	1.2	1.3	1.4
6	Mars Inc (US)	1.1	1.1	1.1	1.1
7	Cadbury Schweppes Plc (UK)	0.6	0.6	1	1
8	Kellogg Co (US)	0.9	1	0.9	0.9
9	General Mills Inc (US)	0.8	0.8	0.8	0.7
10	ConAgra Foods Inc (US)	0.8	0.8	0.7	0.7
11	Campbell Soup Co (US)	0.7	0.7	0.7	0.6
12	Heinz Co, HJ (US)	0.7	0.6	0.6	0.6
13	Hershey Co, The (US)	0.6	0.6	0.6	0.6
14	Ferrero SpA (It)	0.5	0.5	0.5	0.5
15	Dean Foods Co (US)	0.5	0.5	0.5	0.5
Total 10					**13.8 %**
Total 15					**18.9 %**
CR4					**10.3 %**

Source: Euromonitor International, The World Market for Packaged Food, Euromonitor International, June 2006, table 549, p. 598.
Note: CR4 is the level of concentration by the 4 top companies

The world's leading packaged food manufacturer, Nestlé, has a highly diversified product range and is active in most sectors of packaged food, including dairy products, ice-cream and confectionery, in which the company is globally ranked third and second.[66] It is global market leader in 3 of the 19 packaged food sectors: ready meals, frozen processed food and baby food. Nestlé is market leader in four regions. In 2005, its sales were US$ 76.11 bn[67] and its profits were US$ 5.89 bn[68], making it the 50st largest corporation in the world according to Forbes 2000 calculations[69].

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66 Euromonitor International, The World Market for Packaged Food, June 2006, p. 594.
67 Nestlé, Goup figures, 2004-2005: Swiss Francs 91 075 million: value in US$ based on Forbes Global 2000 < http://www.forbes.com/lists/2006/18/06f2000_The-Forbes-2000_Company_13.html> (viewed on 10 December 2006).
68 Idem from: Swiss Francs 7 995 million.

Table 3: Ranking of the top three manufacturers by sector, 2004

Sector	1st ranked	2nd ranked	3rd ranked
Confectionery	Cadbury Schweppes Plc	Mars Inc	Nestlé SA
Bakery products	Kellogg Co	Kraft Foods Inc	Barilla G e R Flli SpA
Ice cream	Unilever Group	Nestlé SA	Lotte Group
Dairy products	Danone, Groupe	Nestlé SA	Kraft Foods Inc
Sweet and savoury snacks	PepsiCo Inc	Procter & Gamble Co, The	Kraft Foods Inc
Snack bars	Kellogg Co	General Mills Inc	PepsiCo Inc
Meal replacement products	Unilever Group	Abbott Laboratories Inc	Atkins Nutritionals Inc
Ready meals	Nestlé SA	Kraft Foods Inc	ConAgra Foods Inc
Soup	Campbell Soup Co	Unilever Group	Nestlé SA
Pasta	Barilla G e R Flli SpA	Nestlé SA	New World Pasta
Noodles	Nissin Food Products Co Ltd	Toyo Suisan Kaisha Ltd	Ting Hsin International Group
Canned/preserved food	Campbell Soup Co	Heinz Co, HJ	Del Monte Foods Co
Frozen processed food	Nestlé SA	Unilever Group	ConAgra Foods Inc
Dried processed food	JA Group	Nissin Food Products Co Ltd	Unilever Group
Chilled processed food	Kraft Foods Inc	Sara Lee Corp	ConAgra Foods Inc
Sauces, dressings and condiments	Unilever Group	Kraft Foods Inc	Nestlé SA
Baby food	Nestlé SA	Bristol-Myers Squibb Co	Abbott Laboratories Inc

Source: Euromonitor International, The World Market for Packaged Food, Euromonitor International, June 2006, summary 4, 600-601.

Number two in the world ranking, Kraft Foods, is the world market leader in chilled processed food and number 2 in bakery products, ready meals, and in sauces, dressings

[69] http://www.forbes.com/lists/2006/18/06f2000_The-Forbes-2000_Company_13.html

and condiments.[70] In 2005, its net revenue was US$ 34.11 bn and its net earnings were US$ 2.62 bn.[71]

Table 4: Ranking of the top three manufacturers of packaged food by region, 2004

Region	1st ranked	2nd ranked	3rd ranked
Western Europe	Unilever Group	Nestlé SA	Danone, Groupe
Eastern Europe	Nestlé SA	Unilever Group	Danone, Groupe
North America	Kraft Foods Inc	PepsiCo Inc	Nestlé SA
Latin America	Nestlé SA	PepsiCo Inc	Bimbo SA de CV, Grupo
Asia-Pacific	JA Group	Lotte Group	Meiji Dairies Corp
Australasia	Nestlé SA	Burns, Philp & Co Ltd	Cadbury Schweppes Plc
Africa and the Middle East	Nestlé SA	Tiger Brands Ltd	Danone, Groupe
World	Nestlé SA	Kraft Foods Inc	Unilever Group

Source: Euromonitor International, The World Market for Packaged Food, Euromonitor International, June 2006, summary 5, 601-602.

Unilever is the world number 3, but ranks first in the sectors of ice cream, meal replacement products, oils and fats, and sauces, dressings and condiments. The fact that these are not the major food products explains the third-place ranking of Unilever in the world market. Unilever is number one in European markets.[72] In 2005, its sales were US$ 49.35 bn and its profits were US$ 4.95 bn[73].

According to Euromonitor, “major players in the packaged food market can be classified into three groups: global players, regional players and sector specialists. Global manufacturers active in a wide range of sectors include Nestlé, Unilever and Kraft Foods, while companies such as Cadbury Schweppes (UK) and Groupe Danone (Fr) are active in a relatively limited number of packaged food sectors. Regional players also tend to be active in a limited number of areas, with Barilla (It.: pasta and sauces), Dean Foods (US, dairy and soy products) and JA Group (Japan, dried processed food) focusing on just one

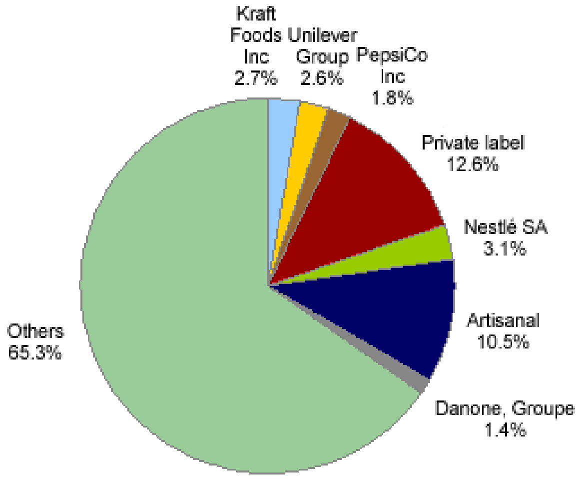
70 Euromonitor International, The World Market for Packaged Food, June 2006, p. 601.
71 Kraft Food Inc, Financial Highlights 2005. p. 16 <http://www.kraft.com/pdfs/kraft05ar_print_final_singles_screen.pdf>
72 Euromonitor International, The World Market for Packaged Food, June 2006, p. 596, 600, 601.
73 Unilever, Jaarverslag en jaarrekening 2005: Sales € 39.67 ;net profit € 3.97: value in US$ based on Forbes Global 2000 <http://www.forbes.com/lists/2006/18/06f2000_The-Forbes-2000_Company_19.html>

product area. A third group of companies, including US-based Hershey and Wrigley, are active in just one sector, in this case confectionery."[74]

An overview of the world leaders in the major packaged food areas (see Table 3) learns that Western multinationals are ranked at the top of the market shares in each of the sectors (except for noodles which are a typical Asian product), and that they are often at the top for several kinds of manufactured products at the same time.

The same leading companies also each have their strongholds in different regions, as can be seen from the overview in Table 4.

Figure 5: Packaged Food: Global Company Shares % Retail Value 2004



Source: Euromonitor International, The World Market for Packaged Food, Euromonitor International, June 2006, chart 5, p. 16.

Level of concentration

The level of concentration in the global packaged food sector is very low (see Figure 5) compared to the semi-processed food sector. The biggest food multinational, Nestlé, has only 3% of the world market. The "CR4"[75] or global market share of the top 4 companies is 10.3%, which is relatively low. Moreover, between 2001 and 2004, the combined share of the top 4 packaged food companies fell slightly, and the combined share of the top 20 showed no growth but remained unchanged at 21%.[76] This means that the world market of packaged food is not yet dominated by a few large companies. The processed food

[74] Euromonitor International, The World Market for Packaged Food, June 2006, p. 15, see also p. 599; information between brackets added by the authors of this report.

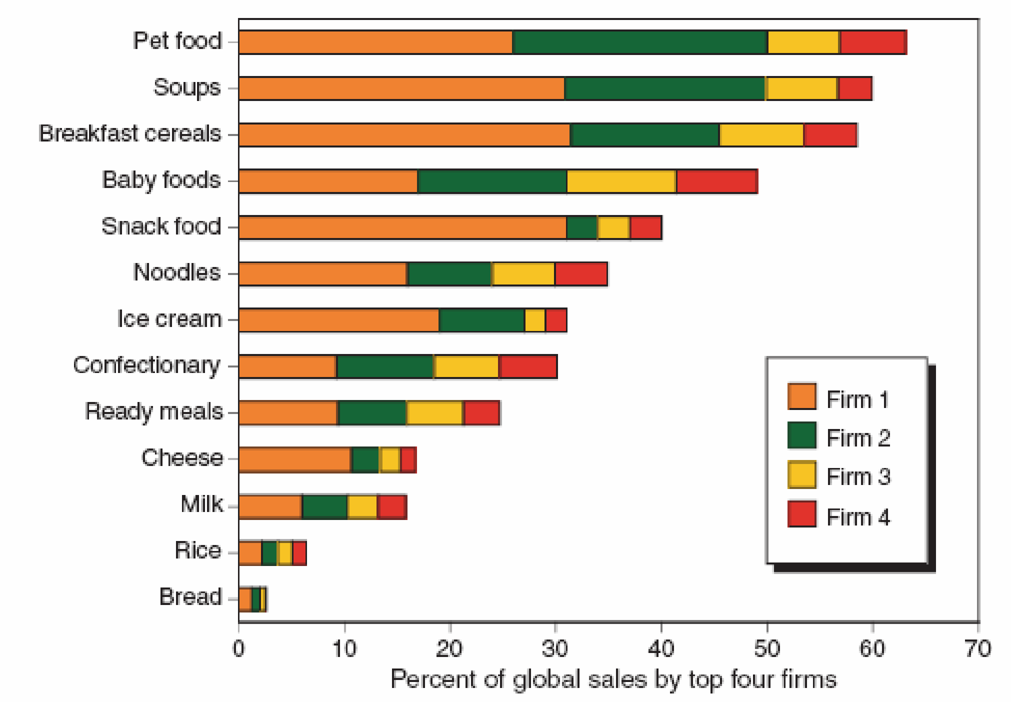
[75] See above: the concentration ratio of the four companies with the largest market share is a standard measure for calculating the level of concentration.

[76] Euromonitor International, The World Market for Packaged Food, June 2006, p. 15.

market for the consumer is still fragmented, which should leave possibilities for smaller and local processors.

What needs to be noted is that the concentration figures above do not include the large global market share of 12.6% held by private labels, i.e. supermarket-branded products which are produced by a variety of processing companies (see Figure 5). They seem to be stopping the top food multinationals from increasing their global market share and taking up new opportunities.

Figure 6: Higher market concentration in sales of branded products



Source: A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 70.

Much higher levels of concentration occur in each category of different packaged food products and in the different regions of the world. In these categories and regions, new market opportunities for smaller developing country processing companies might be much smaller, in the domestic market and for exports. Examples of product categories of packaged food for which market concentration is high, are soups, where 4 companies have around 60% of the global market, and breakfast cereals, where 4 producers have 60% of the global market (see Figure 6).[77] It is estimated that 85% of the world tea market is dominated by 3 companies, of which Unilever is number one.[78]

[77] M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 70.

[78] A Report By SJM Study Group On Reforms in Agricultural Marketing, http://www.swadeshi.org/dynamic/modules.php?name=Content&pa=showpage&pid=198 (viewed 10

It is often the same leading food multinationals which have been able to acquire larger market shares for packaged food products than other companies at the global level, namely Nestlé, Kraft, Unilever, PepsiCo, Danone and Mars (see Table 4 and Table 5).

In 2005, the global market share for confectioners had little changed compared with 2002 (see Table 5: confectionary) with Nestlé 7.5 %, Kraft 5%, Mars 9.5% and Cadbury Schweppes ca. 9.3% and Hershey Foods ca. 6.2% (CR 4 = 32.5%).

Table 5: Global sales share of top six manufacturers by product category, 2002

	Nestlé	Kraft	Unilever	PepsiCo	Danone	Mars
	%					
Confectionery	9.0	5.6				9.4
Bakery products	0.5	3.0	1.0	1.2	1.7	
Ice cream	8.9	0.1	19.3		0.2	1.9
Dairy products	4.4	3.7	0.3		4.8	
Savory snacks	0.1	3.0		32.4	0.3	0.3
Snack bars	3.1	4.0	5.7	9.9	1.3	1.7
Meal replacement drinks	0.2		38.7			
Ready meals	9.7	5.7	3.0	0.2		0.8
Soup	6.9	0.2	17.3			
Pasta	4.6	3.1	0.1	0.4		
Noodles	1.3	0.4	1.3			
Canned food	0.7	0.6	1.1	0.4		
Frozen food	6.1	2.6	4.2			0.4
Dried food	2.3	3.2	3.3	0.2		0.8
Chilled food	0.9	2.6	0.2			
Oils and fats	0.3	0.4	13.4		0.6	
Sauces, dressings, condiments	3.0	4.3	10.7	0.8	0.7	0.7
Baby food	16.9	0.2	0.2	0.1	2.6	
Spreads	0.6	2.2	7.1		0.2	0.4
Dog and cat food	25.7	0.5				24.0

Source: Euromonitor, 2003 QUOTED IN A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 66.

December 2006)

Table 6: Unilever's market share at regional, country, and product levels

Product category	**Total packaged food**					
Market	Global					
Market share %	2.7					
Market	W. Europe	E. Europe	N. America	Latin America	**Asia** Pacific	Africa and Middle East
Market share %	4.2	1.4	2.7	3.6	0.9	3.0
Product category	**Ice cream**	**Soup**	**Replacement drinks**	**Sauces, condiments**	**Oils, fats**	**Spreads**
Market	Global	Global	Global	Global	Global	Global
Market share %	19.3	32.9	38.7	10.7	13.4	7.1
Market	W. Europe	E. Europe	N. America	Latin America	Asia Pacific	Africa and Middle East
Market share %	30.5	25.7	49.9	32.6	4.4	22.0
Market	Austria	Poland	United States	Argentina	Indonesia	South Africa
Market share %	59.6	38.4	50.1	43.0	37.2	46.6
Product category	**Impulse**	**Instant**	**Slimming drinks**	**Catsup**	**Spreadables**	**Yeast-based spreads**
Market	Austria	Poland	United States	Argentina	Indonesia	South Africa
Market share %	81.2	76.5	79.1	76.8	83.9	94.9

Source: Euromonitor, 2003, quoted in A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p.69.

In some regions, the leading food multinationals have achieved very large shares of the regional or national markets, which is often the result of a selective acquisition strategy in core products and pressure from retailers who want to have only a few products on their shelves.[79] Food multinationals may also have different core products in different regions or countries.[80] Examples are Unilever, which has more than 50% market share for some packaged food products in certain countries, such as Austria and Indonesia (see Table 6). Also Nestlé has 60% of the Latin American market for baby food, and even has a virtual monopoly (91%) in Brazil for baby milk formula products, while Nestlé's total market share

[79] M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 69.
[80] Idem, p. 68.

of packaged food in Latin America is only 6.3%.[81] In the US, 89% of the soft drink (including fruit juices) retail sales are from products of just 3 companies: Coca-Cola (US), PepsiCo (US) and Cadbury Schweppes (UK).[82] In India, 45% market share of the packaged tea market is in the hands of Hindustan Lever (51.5% of which is owned by Unilever), while Tata Tea is the number with around 18% market share.[83]

In the European Union, 99.1% of the total number of food and drink companies are either small or medium-sized, yet 51.5% of the turnover in the sector was achieved by 0.9% by the large food and drink companies (more than 250 employees) that are operating in the EU![84] Note that also Nestlé (Swiss) and many US food companies are operating in the EU. The EU food and drink processing companies in general are able to generate a trade surplus, in contrast with their US counterparts. The sector with the highest export figures from the processed food and drinks industry is that of the beverages (especially wine and spirits).[85] The European drink and beverage sector is dominated by multinational corporations, such as Diageo (UK, including brands such as Guinness, Stripe, Smirnoff, and Johnnie Walker, Heineken (NL), Inbev (B), Pernod Picard (F), Carlsberg (DK) and Cadbury Schweppes (UK) play an important role. The wine industry is much more dispersed.

→ Critical issues

An important aspect in the concentration of certain food and drink products in the hands of the same Western multinationals is their ownership of many brands, trademarks, formulas and processing technologies (intellectual property rights) associated with manufacturing. While many products and processes are easy to imitate, their licensing agreements as well as their marketing agreements with other firms play a role in determining how a food manufacturer's products are sold in foreign markets.[86]

2.2. Private labels and the role of supermarkets in reducing profitability of the processed food industry

The phenomenon of the use of private labels by retailers - also called "own" labels, house brands or store brands - has been rapidly expanding over the last decade, not least because the share of private labels is more than 12% of the global packaged food retail

81 Idem, p. 68-69.
82 Standard and Poor's, Industry Surveys – Foods & non-alcoholic beverages, 8 June 2006, p. 7.00000
83 An Overview of the Indian Tea Industry, http://www.valuenotes.biz/research/teatoc.asp (viewed 10 December 2006.
84 CIAA benchmarking report 2006 – The competitiveness of the EU food and drink industry, CIAA, Brussels, May 2006, p. 12, <http://www.ciaa.be/documents/brochures/Benchmarking_Report_FINAL.pdf> (viewed 11 November 2006).
85 Ibid.
86 A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 2-3.

sales (see Figure 5), which is around 4 times more than the number one global food company, Nestlé. Private labels contribute to an important change in the dynamics of the processed food industry, in which retailers are already playing an increasingly powerful role.

2.2.1. *Stiff competition from private labels*

Private labels are food and non-food products sold by the supermarkets, hypermarkets, discounters and other mass merchandisers under the retailer's own name or a new name with particular characteristics created exclusively by that retailer or, in some cases, a group of retailers.[87] The retailers are responsible for commissioning the manufacture of the private label products. In the area of food, private labels cover a very large range of processed food products, with the ready-meals sector at the top of the sales percentages in packaged food (26% of global ready meal sales, 77% of ready meal sales in the UK). Other popular private label packaged food products are chilled processed food (milk, cheese, juices, packaged meat), frozen processed food (especially frozen vegetables, chips, fish and meat), dairy products, canned or preserved food, pasta and spreads. Least popular are baby food (but latest trends are showing increases), slimming products and confectionary.[88] Drinks and beverages such as juices, as well as tea and coffee, are also being branded and sold as private labels.

Private labels have evolved from cheap and often low-quality products mostly sold by discounters as alternatives to higher quality brands. Today all large retailers are selling them and using different kind of private labels with different names, from cheaper options to the branded food to high quality private labels. For instance, in its Dutch supermarkets Ahold uses a low-priced Albert Heijn private label alongside another higher quality private label with exclusive products. In addition, Ahold sells hundreds of cheap, sometimes lower quality food products, including soft drinks, under the brand name Euroshopper as a result of an alliance between Ahold and eight other European retailers which collectively negotiate with private-label manufacturers and all sell Euroshopper products in their stores.[89] Some private labels are increasingly being perceived as brands by consumers.

Sales of private labels have shown rapid growth in Western markets, and have achieved important market shares, especially in Europe (see Figure 7), but also in Eastern Europe, the Asia-Pacific region and Latin America, where private labels have traditionally been weak. Food products are strongly represented in the private label area and have 75% of the top 20 private label categories.

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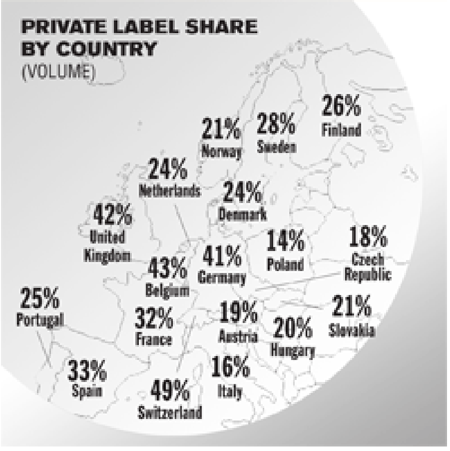
87 See the definition by the association of private label manufacturers: <http://plma.com/tour/> (viewed on 9 November 2006)

88 Euromonitor, 2006, p . 573-576.

89 C. Matlack, R. Tiplady, “The Big Brands Go Begging In Europe - They're on fewer shelves as Europe's private-label business takes off”, Business Week Online, 21 March 2005 , <http://www.businessweek.com/magazine/content/05_12/b3925071_mz054.htm> (viewed 14 November)

Figure 7: Food and non-food private label market share in Europe in volume terms, [2005]



Source: ACNielsen in PLMA's latest International Private Label Yearbook, published at < http://www.plmainternational.com/en/private_label_en.htm> (viewed November 2006)

Factors that explain[90] the rise of private label sales are:

- expansion of large supermarkets, including into developing countries where these retailers bring private labels with them
- introduction of many new private label product lines
- low prices combined with increased consumer confidence in the quality of the private label foods
- marketing support, through advertising, money-back guarantees and being well placed on the shelves
- ability to respond swiftly to consumer tastes and demands for convenience, novelty, low-fat, organic and indulgent foods
- exclusivity of some of the private label products
- the popularity and sales growth of discounters, some of which have almost only private labels on their shelves

Supermarkets have used the profit-making strategy of private labels in order to[91]:

- reverse the increasing market shares of discounters, which were putting the profit margins of retailers under pressure

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90 Mainly based on: D. Burch, G. Lawrence, “Supermarket own brands, supply chains and the transformation of the agri-food system”, International Journal of Sociology of Agriculture and Food, Volume 13, Number 1, July 2005; Euromonitor, 2006, p. 573-574; C. Matlack, R. Tiplady, “The Big Brands Go Begging In Europe - They're on fewer shelves as Europe's private-label business takes off”, Business Week Online, 21 March 2005, <http://www.businessweek.com/magazine/content/05_12/b3925071_mz054.htm> (viewed 14 November)

91 See amongst others: C. Matlack, R. Tiplady, “The Big Brands Go Begging In Europe - They're on fewer shelves as Europe's private-label business takes off”, Business Week Online, 21 March 2005 , <http://www.businessweek.com/magazine/content/05_12/b3925071_mz054.htm> (viewed 14 November)

- rapidly gain market shares by offering low-priced private label food and drinks, including in new (developing country) markets such as China, where retailers can use their experience gained in other markets[92]
- improve net profit margins[93], as retailers ensure that private label products have lower costs for their development (by copying existing products), production (by controlling production or through aggressive negotiation with the manufacturers) and marketing (no or little advertising)
- offer exclusive and good quality products that increase consumer loyalty, as opposed to branded food that can be bought in most supermarkets

The manufacture of private label products is difficult to analyse, because most of the manufacturers are unknown. According to the private label sector organisation, the Private Label Manufacturers Association, manufacturers of private label products fall into four classifications[94]:

- Large national, regional and international brand manufacturers that utilize their expertise and excess plant capacity to supply private labels. Nestlé, Cadbury Schweppes and H.J. Heinz are among those who, it is claimed, produce more cheaply for private labels sitting next to their own products on supermarket shelves.[95] Heinz sold its private label soup business to Del Monte Food (in 2002).[96]
- Small to large quality manufacturers who specialize in particular product lines and concentrate on producing private labels almost exclusively for many retailers. These companies are often owned by firms that also produce their own national brands. One example is PBM Products Inc. (US) which manufactures products such as infant formula for 24 US retailers, including the largest ones such as Wal-Mart.[97] This company has become large enough to be able to provide innovation and marketing services to the retailers.
- Major retailers and wholesalers who own their own manufacturing facilities and provide private label products for themselves.
- Regional brand manufacturers or international primary processing companies that produce private label products for specific markets .[98] An interesting example of a large company producing private-label products is cocoa trader and grinder Barry Callebaut (Swiss), which is a global leading company in producing ingredients for

92 "Expansion in Asia creates private label opportunities", PLMA e-scanner, October 2006, <http://www.plmainternational.com/EscannerInt/October2006En.html> (viewed on 9 November 2006)
93 The net profit margins of private labels of Albert heijn are 10%: "Albert Heijn begint budget-keten met huismerken", Elsevier, 18 oktober 2005, <http://www.elsevier.nl/nieuws/economie/artikel/asp/artnr/69141/index.html> (viewed 10 december 2006)
94 http://plma.com/storeBrands/sbt06.html
95 C. Matlack, R. Tiplady, "The Big Brands Go Begging In Europe - They're on fewer shelves as Europe's private-label business takes off", Business Week Online, 21 March 2005, <http://www.businessweek.com/magazine/content/05_12/b3925071_mz054.htm> (viewed 14 November)
96 Standard and Poor's, Industry Surveys – Foods & nonalcoholic beverages, 8 June 2006, p. 1.
97 Seewebsite of PBM Products Inc (US): <http://www.pbmproducts.com> (viewed on 12 November 2006)
98 http://plma.com/storeBrands/sbt06.html

many big chocolate confectioners, but which now has added a new strategy of moving up the supply chain and producing private label chocolates for large retail chains such as Aldi (Germany), Wal-Mart (US)[99] and Ahold (NL)[100].

Private label food places more responsibility on the retailer for product design, quality and safety control, product liability and traceability, which means that closer cooperation and coordination with manufacturers is necessary.[101] Retailers want to encourage innovation by the producers themselves, and may wish to maintain some level of continuity. However, there are reports that some private label producers are being put under a great deal of pressure, and make very little profit, some going bankrupt as retailers can contract other manufacturers.

→ Critical issues

There is not sufficient information available about the relationship between retailers and private label manufacturers to know how much added value from the private label food products is retained by the supermarkets themselves while squeezing their suppliers, or how many benefits are also reaped by the producers down the supply chain. Nor do supermarkets make enough information public about how environmentally and socially friendly the production of their private labels is.[102]

It is not clear how many opportunities there are for developing country producers to manufacture private label food products. On the one hand, retailers bring over their private label food from other markets to benefit from economies of scale for sale in developing countries where less fresh and sophisticated food products are sold. On the other hand, the need to be near consumers might offer the manufacturers of some products in developing countries an opportunity as suppliers of private labels, in competition with brands from large food multinationals.

Private labels, together with other retailer strategies (see below), have a large impact on the large and smaller processed food companies, their strategies and level of survival, which might be transferred through the value chain (see section 2.3). The competition from private labels allows retailers to increase the pressure on branded food companies by demanding ever lower prices. Nestlé and some others are reacting by increasing their sales at discounters, which traditionally had only private labels or lower priced branded foods, by making deals with discounters even if that puts their own profit margin under pressure.[103] More profoundly, private labels are undermining a fundamental pillar of the

[99] R. Morais, “The Gnomes Of Cocoa”, 14 March 2005, <http://www.forbes.com/global/2005/0314/024_print.html> (viewed on 9 November 2006)
[100] Albert Heijn, Allerhande, November 2006.
[101] A. Regmi, M. Gehlhar, Processed food trade pressured by evolving global supply chains, Amber waves (Economic research service USDA), Volum3, issue 1, February 2006.
[102] MVO Platform, Zicht op duurzaamheid? Transparantie in productieketens onderzocht, December 2006, p. 83-84.
[103] C. Matlack, R. Tiplady, “The Big Brands Go Begging In Europe - They're on fewer shelves as Europe's

profit making strategies of the food multinationals, whose products are often easy to imitate, and are undermining their power in the supply chain: the brand image of their products and the customer loyalty strategies attached to them. Analysts say these pressures contribute to cross border consolidation in the branded food and drink sector.[104]

2.2.2. The impact of supermarkets on the processed food industry

The recent SOMO report on the fresh fruit and vegetable (FFV) sector[105] demonstrated how the growing retail sector is dominating the whole FFV chain, resulting in the concentration in the FFV sector and diminished possibilities for small farmers to benefit from or participate in the supply chain, also in developing countries. Research into processed food manufacturers, and the food processing industry itself, have indicated that supermarkets, hypermarkets and discounters are important actors in their business, which puts strong downward pressure on the profitability of the manufacturers and processors. They are increasingly stating that power, and therefore profits, in the food system are shifting to large retailers and away from the food manufacturers who previously could impose their conditions or terms of operation on retailers and suppliers alike. Why and how large retailers have such an influence on the processed food sector can be described as follows:

Supermarkets and other retailers such as hypermarkets and discounters have become the main sales points for manufactured food and drinks in Western countries, and increasingly so in developing countries. In some Latin America countries, supermarket chains now account for up to 70% of grocery retail sales. Supermarket sales have not reached these levels in Asia, but are growing, and the supermarket presence in Africa is even lower.

Increasingly, market share for retail sales in one country is being concentrated in the hands of only a few retailer chains, particularly in Western Europe (see Table 7), but also increasingly in other Western countries and developing countries. In addition, a few supermarkets that have large shares in their home market are very quickly expanding into other countries, not least in developing countries. As a result, the same small number of internationally operating supermarket chains (see Table 11) belong to the top ten leaders in grocery retailing - which includes many food items - in Latin America, Asia and Africa, although their market share in these regions as a whole does not exceed 7% (see Table 8, Table 9, Table 10).

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private-label business takes off", Business Week Online, 21 March 2005 , <http://www.businessweek.com/magazine/content/05_12/b3925071_mz054.htm> (viewed 14 November)

104 KPMG, "Opkomst huismerken leidt tot ingrijpende consolidatie bij producenten", 23 May 2005, <http://www.kpmg.nl/site.asp?id=2036&process_mode=mode_doc&doc_id=40886> (viewed on 10 December 2005)

105 M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006

Table 7: EU members in Western Europe (15): share of modern grocery distribution[106] of the top 5 retailers in each country (%) in 2004

Country	Market share
Finland	88.2%
Sweden	86.2%
Ireland	83.2%
Denmark	82.4%
Luxembourg	82.3%
Austria	78.7%
Belgium	78.6%
Portugal	71.3%
France	70.4%
Germany	68.4%
Spain	67.9%
Netherlands	67.7%
United Kingdom	56.3%
Greece	53.7%
Italy	41.3%

Source: M + M Planet Retail, Global Retail Concentration 2004, April 2005

Table 8: Top 10 grocery retailers in Latin America, 2005

Rank	Retailer	Grocery retail banner sales Market Share (%)
1	Wal-Mart (US)	6.8 %
2	Casino (Fr)	3.2 %
3	Carrefour (Fr)	2.7 %
4	Censosud	1.7 %
5	Soriana (Mex)	1.5 %
6	Falabella	1.2 %
7	Gigante (Mex)	1.1 %
8	D&S (Distribución y Servicio) (Chile)	1.1 %
9	Comercial Mexicana	1.0 %
10	OXXO	0.9 %
TOTAL		**21.2 %**
CR4		**14.4 %**

Source: Planet Retail - www.planetretail.net,
Note: CR4 is the level of concentration by the 4 top retailers

[106] All tables on the share of the top 5 retailers: Market share based on "modern grocery distribution", which includes hypermarkets, superstores, supermarkets, discount stores, convenience stores and drugstores, cash & carry, delivered wholesale, excluding independent specialist outlets such as butchers and bakers, and open markets. The grocery products include food, and non-food when sold by mixed retail formats.

Table 9: Top 10 grocery retailers in Asia, 2005

Rank	Retailer	Grocery retail banner sales Market share (%)
1	AEON (Jap)	3.2 %
2	Seven & I	2.9 %
3	Uny (Jap)	1.3 %
4	Daiei (Jap)	1.0 %
5	FamilyMart (Jap)	0.9 %
6	Lawson (Jap)	0.9 %
7	Wal-Mart (US)	0.8 %
8	Lotte	0.7 %
9	Carrefour (Fr)	0.6 %
10	Tesco (UK)	0.6 %
TOTAL		**12.9 %**
CR4		**8.4 %**

Source: Planet Retail - www.planetretail.net

Table 10: Top 10 grocery retailers in Africa, 2005

Rank	Retailer	Grocery retail banner sales Market share (%)
1	Shoprite (South Africa)	5.9 %
2	Pick 'n Pay (South Africa)	5.7 %
3	Massmart (South Africa)	4.9 %
4	Metcash (South Africa)	3.9 %
5	SPAR (South Africa)	2.5 %
6	Woolworths (South Africa)	2.3 %
7	Casino (Fr)	1.9 %
8	Carrefour (Fr)	1.0 %
9	Auchan (Fr)	0.8 %
10	Metro Group (Germ)	0.3 %
TOTAL		**29.2 %**
CR4		**20.4 %**

Source: Planet Retail - www.planetretail.net

Table 11: The leading globally expanding grocery supermarkets and their global market shares, 2004

	Group	Country of Origin	Market share (%)
1	Wal-Mart	USA	6.1
2	Carrefour	France	2.3
3	Ahold	Netherlands	1.8
4	Metro Group	Germany	1.6
5	Tesco	UK	1.3
6	Ito-Yokado	Japan	1.2
7	Kroger	USA	1.2
8	Rewe	Germany	1.1
9	Costco	USA	1.1
10	Aeon	Japan	1.0
11	Target	USA	1.0
12	Casino	France	1.0
13	Aldi	Germany	1.0
14	Auchan	France	1.0
15	ITM	France	1.0
	TOTAL		**23.7%**

Source : M+M Planet Retail

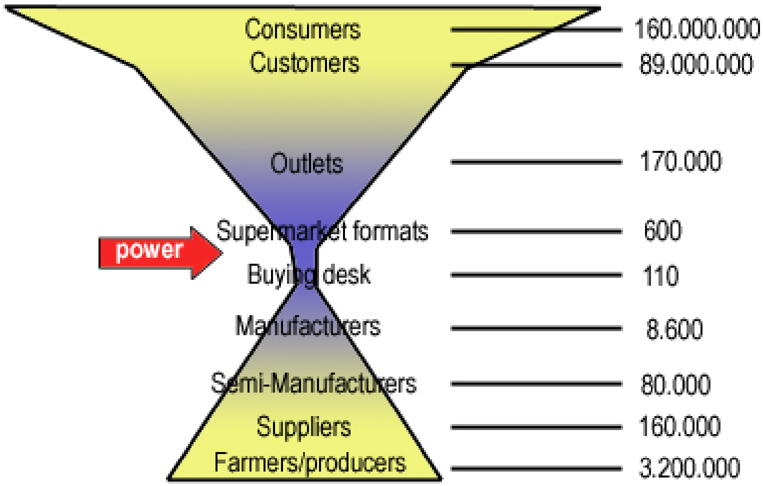
This means that the expanding supermarket sector in developing countries is increasingly foreign owned, through investments, mergers and acquisitions, and joint ventures using trade and investment liberalisation (see Chapter 4). Foreign supermarket chains first enter the richest countries and focus on the richest (urban) areas and richest clients, from whom the most profit can be made, before expanding into other countries and other areas. Their large scale and efficient operations, with a single distribution centre able to service several developing countries in some cases[107], give them cost saving advantages over their smaller rivals, forcing smaller retailers out of business, in developed as well as developing countries. In developing countries, these foreign-owned retailers are often selling products from the large food multinationals that are their suppliers in many other countries, leading to changing tastes and replacement of sales of locally produced foods from smaller processed food manufacturers.

The large supermarkets are trying to rapidly gain market share, and are fiercely competing with rival retailers by offering low prices for a wide range of quality products. The popularity of discounters with their low prices in Europe has also increased competition based on low prices. Large retailers are using a wide range of strategies to attract consumers with low prices, such as private labels, and not least demanding steep discounts from their suppliers, the food manufacturers, including demanding below production prices. A fair number of supermarkets have grouped their wholesale buying activities, i.e. the units responsible for negotiating with suppliers and buying the products, to form a collective **buying desk** grouping several supermarket chains. This centralisation

[107] A. Regmi, M. Gehlhar, Processed food trade pressured by evolving global supply chains, Amber waves (Economic research service USDA), Volum3, issue 1, February 2006.

and concentration of procurement results in even lower sales points for manufactured food companies, the so-called “bottleneck” in Europe (see Figure 8) whereby it is estimated that 85% of all retail food sales in Western Europe have to pass through only 110 buying desks.[108]

Figure 8: Supply chain bottleneck in Europe that leads to buyer power



Note: covers retail food and represents about 85% of the total sales of West European countries
Source: J. Grievink, The changing face of the global food industry- Presentation OECD Conference, The Hague, 6 February 2003.

The concentration in food retail sales into the hands of dominant supermarkets chains gives them high bargaining power, also known as ‘**buyer power’,** or **oligopsony** in markets with a few buying desks or retailers, enabling them to obtain lower prices than other retailers are able to. And while convenience stores are on the rise in Western countries, they often belong to the same supermarket chains. This allows supermarket chains to determine the terms of supply which food processing companies cannot escape, such as not only requiring low prices and deep discounts but often also:

- high volumes
- constant supply
- high quality and safety standards, including meeting high private standards set by the supermarkets themselves, and the ability to trace back production and inputs

Buyer power can also lead to abusive practices towards processed food companies, which have been observed with global retailers such as Carrefour and Tesco[109]:

- slotting allowances or fees for shelf space and for being on preferred supplier' list (listing) -and threats of delisting-; or annual contracts - which the retailer can threaten not to renew

[108] T. Fox, B. Vorley, Concentration in food supply and retail chains, DFID & IIED, August 2004, p. 22.
[109] For full description see for instance: C. Jacquiau, Les coulisses de la grande distribution, (Albin Michel, Paris), 2000; J. Blythman, Shopped – The shocking power of British supermarkets, (fourth Estate, London), 2004.

- changing quality standards without adequate notice or payment for extra work involved
- payment by processed food companies (!) of a percentage of their annual sales through the supermarket ('rebate') or other nontransparent deductions from producer prices
- late payments for products already delivered and sold, which allows retailers to earn interest on the money deposited at the bank during the delaying period
- unfair negotiation tactics
- payments for advertisements and promotions by the retailer
- using all kind of methods to avoid critical publications of their procurement strategies
- minus margins whereby the supplier of a supermarket is not allowed to supply at a higher price than the supermarket's competitors

Supermarkets want to deal with as few suppliers as possible, and are therefore unlikely to have many small suppliers for the same processed food product. The trend is for large supermarkets to reduce the products on the retail shelves to 3 or 4 leading brands in the same product category, alongside their own private label. [110] This increases competition among the processed food companies to be able to supply the leading supermarket chains, to ensure that their products are put at a good selling location/shelf place, and extend the supplying relationship[111] while remaining profitable.

Other ways in which supermarket chains challenge the domestic food manufacturing industry is by their capacity to source worldwide and import at competitive prices. This can be realised on the basis of alliances with manufacturers worldwide, providing opportunities to Southern producers when they are given the possibility to meet the requirements. However, many small domestic food processors could lose out in the competition.

Southern producers could also obtain more possibilities to supply the supermarket chains operating in their country. However, the presence of large international retailers has encouraged Western food multinationals to expand their manufacturing into developing countries where large supermarket chains are operating and compete with domestic food processors, who might not be able to meet the competitive challenge from these products (no figures were found on Southern processed food producers gaining or losing from increased supermarket presence in developing countries).

Consumer pressure for constant change and innovation in the products is also passed on through the retailers to the manufacturers. At the same time, the price pressure on European food processors has resulted in a reluctance to invest in research and

[110] J. Wilkinson, The food processing industry, globalization and developing countries, electronic Journal of Agricultural and Development Economics, Vol. 1, No. 2, 2004, p. 1 , <http://www.fao.org/es/esa/ejade/vol_1/vol_1_2/cover_en.htm> (July-November 2006)

[111] A. Regmi, M. Gehlhar, Processed food trade pressured by evolving global supply chains, Amber waves (Economic research service USDA), Volum3, issue 1, February 2006: a recent review of 751 retail purchasers in 16 European countries suggests that retailers are more and more interested in suppliers who are willing to engage in long-term relationships with the retailer.

development of new products[112], putting even more pressure on their competitiveness. On the other hand, supermarkets play an important role in distributing and promoting the sale of new products or existing products from food multinationals in new markets. This often leads to strategies of greater coordination, alliances and integration, as is the case in Europe[113], leading to vertical integration in the supply chain.

Some analysts predict that even branded foods groups, such as Nestlé, will lose in confrontations with large retailers such as Wal-Mart, and are seeing their profit margins diminish even further. The way the large food and drink processing companies have been dealing with the pressure from the supermarkets and passing it on through their operations and supply chains is described in section 2.3 with a clear trend towards focusing on responding to different demands in new (developing) country markets and the West, as well as cost-cutting strategies resulting in higher levels of concentration of brands into the hands of a group of leading food processing companies. And while international supermarket chains have upgraded food distribution in many developing countries, this has also resulted in more integrated supply chains serviced by fewer producers, changing the dynamics of the free trade markets domestically and at the international level.

→ Critical issues

The demand for high quantities, high quality and safety, traceability, constant supply, etc. and the abusive practices of buyer power makes it difficult for small processing companies, less sophisticated companies from developing countries and newcomers to be suppliers of the large supermarkets at home or abroad, or to remain profitable once supplying. Also, imports and procurement from large food multinationals that are increasingly establishing themselves in developing countries further reduce the potential for developing country processed food suppliers to benefit from increasing retail sales, while their traditional outlets could be disappearing (due to the competition from large retailers.) Some basic processing, however, such as making palm oil or making biscuits, often provides an easy method for the very poor, often women, to earn a living.

Even the leading food multinationals such as Unilever have been under pressure from the buyer power, and private labels, of the large retailers. Dealing with buyer power and the abusive practices of large retailers is not well regulated in many (developing) countries (see Chapter 5), giving small processing companies little protection against unfair competition.

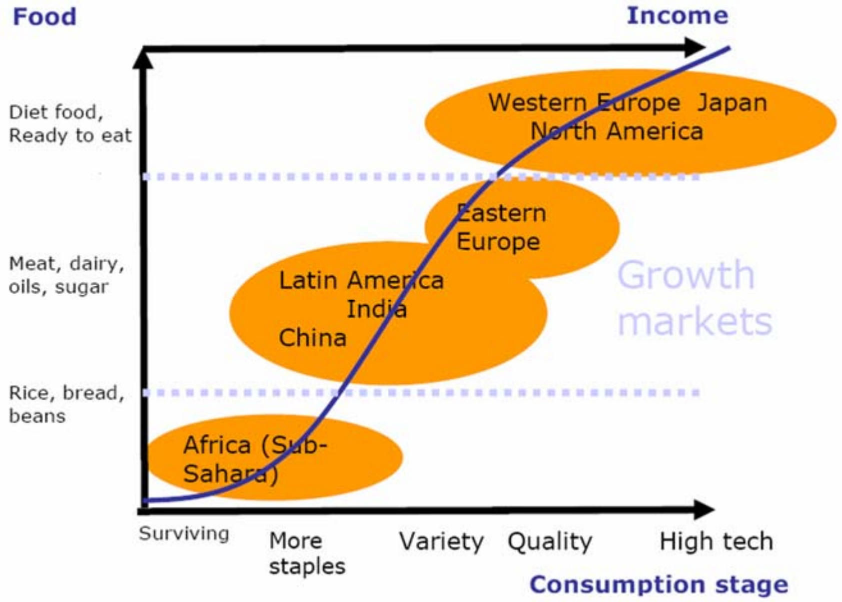
[112] S. Roach, A. ElAmin, "EU companies consolidating to boost R&D investments", Food productiondaily,com – Europe, 7 September 2006.

[113] A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 2.

2.3. Strategies[114] of leading companies

The industry is responding to the major changes and trends described above (see Chapter 1 and Chapter 2, section 2.2.2), including the increasing demand for healthier products and for time-saving products, technological change (e.g. more refrigerators and microwave ovens owned by clients) and improved information technology. The industry may also have to set aside profits in the event of lawsuits relating to obesity, which is being attributed to the food industry (see Chapter 3).[115]

Figure 9: Evolution of food demand



Source: Stéphane Delodder, The cacao Industry: From value to volume based growth, Barcelona, European Cocoa Association, 17 September 2005

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114 Based on : A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005; Euromonitor International, The World Market for Packaged Food, June 2006; J. Wilkinson, The food processing industry, globalization and developing countries, electronic Journal of Agricultural and Development Economics, Vol. 1, No. 2, 2004, p. 184-201; Standard and Poor's, Industry Surveys – Foods & nonalcoholic beverages, 8 June 2006; CIAA benchmarking report 2006 – The competitiveness of the EU food and drink industry, CIAA, Brussels, May 2006, < http://www.ciaa.be/documents/brochures/Benchmarking_Report_FINAL.pdf> (viewed 11 November 2006); "Nestlé picks Malaysia as global halal food production centre", (Electronic newsletter of the Malaysian Industrial Development Authority), 21 August, 2006, <http://www.mida.gov.my/beta/news/view_news.php?id=2656> (viewed on 11 November 2006); P. Elshof, Unilever company profile, June 2005; <http://www.fnvcompanymonitor.nl/download/publications/UnileverCompanyprofile.pdf>; P. Demetrakakes, "Nestlé's packaging wraps up the world: a truly international food company combines local and global strategies in packaging its huge array of products", in Food & Drug Packaging, October 2004; company websites.

115 K. Higgings, State of food manufacturing: period of polarization emerges, published by Food Engineering, (BNP Media), 28 September 2005 (viewed on 4 November 2006).

In order to increase their profits, or at least maintain the value of their shares on the stock market, while their profit margins and cash flow are under pressure, big food processing companies and multinationals have adopted a range of strategies and cost-cutting methods which could also be used by smaller food companies, such as:

Profit making strategies and competing against rival companies

- Expansion into more markets, through investment and exports, especially into the richer emerging markets of developing countries where there are much greater growth prospects (due to population growth, urbanisation and the increasing income of some parts of the population) compared to developed country markets where growth prospects are low.
- Investment that is diversified across a large number of countries, allowing better responses to local tastes and resulting in less need for trading processed food.
- Growth strategies aiming at achieving or maintaining leadership positions in specific sectors in each of the countries in which they operate in order to be profitable (or leave).

Cost-cutting strategies, increased efficiency and more integrated supply chains:

- Automation of production, quality control and supply management
- Outsourcing of support services (such as computer maintenance) and other non-core activities (such as cleaning, transport) but also of core activities such as production, production or primary processing of key ingredients, design and market studies. Outsourcing can take place with other companies in the same country or abroad (in developing) countries; outsourcing is a major trend at Western food processing companies.
- Use and introduction of appropriate technology.
- Mergers and acquisitions (see 2.3.1) and investments in countries from which food can be exported to third countries with lower tariffs, thanks to trade agreements (see Chapter 4).
- Divestment of, and selling off, some activities, sectors and products in order to concentrate on core business sectors and have a number of products and brands that can be efficiently managed (see 2.3.1).
- Cutting personnel costs, including cutting the number of people employed, often with the loss of thousands of jobs and the closure of many manufacturing plants in one year (see
- Box 6 as an example), and short-term contracts for staff.
- Strategic alliances, co-branding and joint ventures (see 2.3.2).
- Closer cooperation with food retailers to meet consumer demands.
- Where possible, trade between the various production and sales units of the company within a region (or worldwide) to benefit from the cheapest production and to be present in the most profitable consumer markets; concentration of production into a few units or countries per region (e.g. by Unilever).

- Flexible organisational structures and close coordination with producers or other actors in the supply chain, in order to be able to respond quickly to new consumer demands.
- Making raw materials and ingredients cheaper, for example by importing rather than sourcing in the country of production, through price pressures and extremely demanding requirements on suppliers and reduction of risks associated with producing ingredients
- Dealing with fluctuations and increases in production costs due to higher prices for ingredients and packaging which reduce profit margins; swapping to cheaper ingredients, for example from cocoa butter to vegetable oils.
- Lobbying for reduced tariffs to allow cheaper imports of ingredients in countries where manufacturing is carried out, and for lower tariffs on processed food exports (see Chapter 4)
- Lobbying against burdensome regulations and, in trade negotiations, against “non-tariff barriers”, i.e. the regulations of trade partner countries (see chapter 5).

Higher quality, healthier, local and new products:

- Catering to local tastes and the specific demands of each market in terms of formulation, format, packaging and presentation of the food products, even in the case of a global brand or product.
- Responding to consumer demands and needs for higher value and more varied products.
- Responding to health concerns by changing products, introducing new products, using organic and whole grain ingredients or developing functional foods (with added healthy ingredients), using less sugars or carbohydrates, and less or different fats, changing labelling, etc.
- Ensuring that production does not have any damaging effects on health or the environment which consumers might disapprove of.
- Constant innovation in products and production methods which includes extensive and improved research and development (R&D) activities and facilities, and investment in these activities by allocating (a large amount of) financial resources to them.
- Constant reorientation by the processing companies in order to remain competitive.
- Responding to higher availability of consumers refrigerators and microwave ovens which allows more fresh processed food to be stored and prepared.
- Owning brands, trademarks, formulas and processing technologies associated with manufacturing, and controlling production and sales through licensing and marketing agreements.
- Using technological advances against competitors.

Increased marketing and sales:

- Additional investment in marketing through advertisements, promotions, websites for direct sale or information about the product (including recipes, etc.).

- Ensuring that consumers are aware of the additional value or quality of the new products (is as important as developing a new product).
- Investing in accessing distribution channels other than supermarkets.
- Adding new technology labelling, such as the product code (EPC) and the newest chips for Radio frequency identification (RFID) used for theft prevention and provision of information to managers and clients.[116]
- Changing packaging to sizes that offer the products at more competitive prices compared to private labels, or that are geared to sales through convenience stores.
- Prosecuting retailers whose private labels are too similar to branded products or who are offering excessively low prices while demanding that supplies continue, as has been the case in the Netherlands.
- Using unfair and unlawful marketing practices (restrictive business practices: see Chapter 3 and Chapter 4), requiring for example that shops not only stock a high-selling product of a food multinational, but also the less popular products.[117]
- Bottom of the pyramid strategies: in order to tap into the markets of the poor – where some profits can be made - methods are used to make processed food products affordable and available to the poor, for example making small packages of margarine or bouillon tablets, supplying vendors in more remote areas.

Not all food manufacturing companies have the same strategies and market orientations, and the same companies might have different strategies for different kinds of products, for several reasons. Some food multinationals want to provide products all over the world, while other food companies only produce for the local market. Some concentrate on a few (unique) products while others have a broad diversity of products.[118] Lately, some global food multinationals have been reducing their wide range of brands and products to a more limited and profitable range of brands and products, which has for instance been the case with Unilever and Heinz.[119] Nestlé has both a wide geographic coverage and a diversified product portfolio, but is still catering for local or regional tastes. For some products, such as bottled water, Nestlé can use a more global strategy. Global umbrella brands allow food multinationals to enter new markets with the experience and economies of scale of existing products and brands while adapting to local tastes and demands, sometimes in alliance with local producers. These products challenge local producers, especially in developing countries, to achieve the same quality and marketing standards.

Small and medium-sized companies are still an important part of the food industry, especially at the local level in developing countries, but also in developed countries. Those who manage to expand their sales are mostly doing so through specialisation, high and exclusive added value and by clustering with other companies.[120]

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[116] Information based on <http://nl.wikipedia.org/wiki/RFID> (viewed on 30 October 2006)
[117] See chapter 3 and 4.
[118] Based on : A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 63.
[119] See: <http://www.heinz.com/2006annualreport/letter.html> (viewed on 11 November 2006).
[120] J. Wilkinson, The food processing industry, globalization and developing countries, electronic Journal of Agricultural and Development Economics, Vol. 1, No. 2, 2004, p. 195.

Box 6: Some key figures for Unilever

Unilever is a leading food, and home and personal care multinational owned by the Netherlands-based Unilever N.V. and UK-based Unilever PLC. In terms of packaged worldwide food sales it is third only after Nestle and Kraft. The company is number one worldwide in tea, ice cream and some culinary products. In addition, it is the world's number one in deodorants and laundry detergents, and number two in hair and skin care products.

	2005	2004
Turnover	€ 39.67 bn	€ 38.567 bn
Net profit	€ 3.97 bn	€ 2.94 bn
Taxes paid	€ 1.23 bn	€ 1.625 bn
Advertisements costs	€ 5 bn	n/a
Employees at end of year	206,000	223,000
Raw materials based on agriculture	65%	n/a

Source: Unilever (2005). Environmental and Social Report,1 and Unilever Annual Report and Accounts.

Unilever's strategy and interests
Since Unilever was founded in 1929, it owned factories and trading subsidiaries in Asia, Africa and Latin America and expanded further to acquire basic raw materials such as vegetable oils for its margarine. Unilever's food sector has remained predominantly a Western European company. Since 1983 however, its acquisitions and expansion focused on a few core-product groups or brands in priority regions, namely large and emerging market countries in North America, Asia, Eastern Europe and Latin America with the aim of increased profitability and diminishing its dependency on Europe for its sales and profits. Between 1999 and 2004, this strategy was used to target high annual-growth figures and to concentrate the production of its major brands and products in 150 key-factories world-wide In 2000 Unilever announced lay offs of 25,000 people or about 10% of its workforce at that time, as a result of restructuring with factories being closed and profits being under pressure.
Between 2005-2010, Unilever is hoping to push a somewhat more conservative profit-making and cost-cutting strategy including:
(a) outsourcing production from 15% to 25% – and higher in some countries such as India;
(b) reducing and concentrating production locations in any region (intra regional sourcing) – in some cases production has already shifted from Australia and the Philippines to Indonesia where for instance Lipton tea is packed for the Australian market;
(c) selective cross-regional sourcing – which, for specific products, could make Unilever Europe source in Asia, or vice versa.
Unilever's operations and profit making have not been without controversy, as Chapter 3 and 4 of this report illustrate.

Sources: M. Vander Stichele, K. Bizzarri, L. Plank, Corporate Power over EU Trade Policy: Good for business, bad for the World, published by the Seattle to Brussels Network, Brussels 2006, p.16; "Unilever to lay off 25,000," Business Legal Reports website, Layoff news, February 2000, <http://compensation.blr.com/display.cfm/id/150538> (viewed 28 ovember 2006); "Unilever to axe 8,000 jobs," CNN Money, April 2001, <http://money.cnn.com/2001/04/27/europe/unilever>, (28 November 2006).

Box 7: The Nestlé strategy, an illustration of management trends at large packaged food industries

"To accelerate the evolution of Nestlé from a respected, trustworthy Food and Beverage Company to a respected, trustworthy Food, Nutrition, Health and Wellness Company demands that we continuously reshape our businesses so that we are able to effectively defend and build our core businesses, strengthen our emerging businesses and create flourishing growth in the field of Nutrition, Health and Wellness. The transformation goes beyond products and brands and extends to the way the Group is structured.
Nestlé is changing from a decentralised multinational company to a global and, ultimately, a global multifocal company. Our new structure comprises:

- A decentralised "generating demand" front-line, that is focused, fast and flexible in our markets – with the consumer and customer at the centre of all their activities.
- A regionally or globally run "ensuring supply" back-line, including factories, back offices and shared service centres, that is slim, cost-efficient and service-driven.
- Strategic, Consumer Insight and R&D-driven Innovation and Renovation led by the Strategic Business Units (SBUs) and R&D.
  Food and Beverages

Source: Nestlé 2005 Management Report - Food and Beverages, 2006, p. 1, <http://www.ir.Nestlé.com/NR/rdonlyres/3760454B-307B-4AFC-9CBE-932B57AF7A05/0/FoodandBeverages.pdf> (viewed on 12 November 2006)

What strategies can packaged food industries use to expand abroad : export or invest?

In order to expand sales in developed and developing countries while remaining competitive, food companies can opt for trading or investing strategies. The choice might depend on the type of products, size and needs of the markets, the cost of production (local ingredients or the possibility for cheap imports).

One option is to export high-value food products from a company's product unit to the country of consumption. This option requires trade liberalisation policies to be in place, so as to avoid price increases through high tariffs. Major food multinationals, such as Unilever and Nestlé,[121] are increasingly opening regional production units, which export to other markets in the region wherever possible.
Another option for food companies to increase their sales is by investing in developing countries, where they process the food near to the consumer, usually in areas where the consumer market is sufficiently large. Infrastructure, regulation and investment liberalisation policies (see Chapter 4) will play a role as well.[122] They need to take into

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121 See for instance: P. Demetrakakes, "Nestle's packaging wraps up the world: a truly international food company combines local and global strategies in packaging its huge array of products", in Food & Drug Packaging, October 2004, < http://www.findarticles.com/p/articles/mi_m0UQX/is_10_68/ai_n6359089> (viewed November 2006)

122 Ibid.

account that some competition authorities or other regulators may intervene and block mergers and acquisitions when foreign firms are getting too large a share of the market which could possibly resulting in increased prices for consumers.[123]

→ Critical issues

Developing country companies usually do not have the financial resources to compete with Western food multinationals in their domestic markets, resulting in the closure or mergers of many SMEs in developing countries. On the other hand, the outsourcing strategies of food multinationals and the private labels of retailers give opportunities for SMEs to enter the supply chain ranging from the initial to the final stages of processing. Also, SMEs have an opportunity to serve small and remote rural local markets which large food companies do not find profitable to serve. Given the importance of SMEs for employment and the dynamics in the market, they might need support, including through regulation, to be able to enter the market and to be able to compete with very large companies under fair conditions. But SMEs need to be aware of the major differences between the different food products involved, as regards both processing and raw material supplies. "In this sense, the rice-based activities of many Asian countries have a totally different dynamic than the readily mechanizable agriculture of much of Latin America, parts of Africa and indeed other parts of Asia. Many traditional processing activities, especially in grains, oil and sugar have reached levels of scale and automation that offer virtually no space for SMEs. Recent developments in the dairy sector, so critical to the small-scale farming sector of many developing countries, would seem to be advancing in this same direction."[124]

The increasing complexity of the processed food market in Western countries (for example, the importance of fresh ready-to-eat meals) and competition from large food manufacturers and private labels, together with the high demands from large retailers mean that Western markets are difficult to penetrate for small, new and developing country food processors. The latter need to have the ability to respond to changing consumer demands and therefore have a flexible structure and supply chain, for example, as well as the financial and human resources to adapt to new demands. New functional foods require a great deal of creativity, human skills and capital resources for newcomers to enter the food market with a high level of added value. Global food companies use their technological and marketing advances to expand, tap into new market segments and compete successfully against smaller companies in the market, and to have strong relationships with retailers where required.

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[123] A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 67.

[124] Wilkinson, The food processing industry, globalization and developing countries, electronic Journal of Agricultural and Development Economics, Vol. 1, No. 2, 2004, p. 196.

Automation, outsourcing, cutting costs of personnel, mergers and acquisitions can lead to reductions of staff at the manufacturing or other units. In the EU, for example, there is a trend towards the reduction of workforce, with 4.9% fewer employees in the EU food and drink industry in 2004 compared to 2003, despite an increase in turnover.[125] Global food companies are also cutting jobs worldwide, as illustrated by Unilever, which is employing 102,000 fewer staff globally in its own operations in 2005, compared to 10 years earlier.[126] Because of the focus on developing new products, certain types of personnel are able to remain or increase, engineering staff, for example.[127] Overall, it seems that growth in the leading food and drink companies is not always translated into more direct employment at these companies, also known as jobless growth. An important impact of mergers and acquisitions is the concentration of manufacturing into fewer locations, leading to consolidation of production.[128]

The pressure for low prices and other high standards by the retailers have contributed to the increasing and wide-ranging mergers, acquisitions, divestments and alliances that result in increasing concentration in the food processing industry, and in fewer opportunities for developing country food manufacturers.

The profit-making strategies of the biggest food processors are geared towards supplying and getting the profits out of the most affluent consumers, not towards ensuring that the poorest are getting better access to food. New products and methods to reach the poor are being used, but are not yet widely developed. It remains to be seen how these bottom of the pyramid strategies will be maintained, and how profitable multinationals want these products to be.

2.3.1. Mergers and acquisitions – and divesting

There have been many mergers and acquisitions over the past decade in the food and drink industry worldwide.[129] Some acquisitions have involved deals of several hundred millions of euros (see Table 12 for the largest ones). These mergers and acquisitions have mainly involved large multinational food companies taking over

[125] CIAA benchmarking report 2006 – The competitiveness of the EU food and drink industry, CIAA, Brussels, May 2006, p. 11, < http://www.ciaa.be/documents/brochures/Benchmarking_Report_FINAL.pdf> (viewed 11 November 2006)

[126] M. Vander Stichele, K. Bizzarri, L. Plank, Corporate Power over EU Trade Policy: Good for business, bad for the World, Seattle to Brussels network, Brussels, October 2007, p. 21.

[127] K. Higgings. State of food manufacturing: period of polarization emerges, 28 September 2005 <http://www.foodengineeringmag.com/copyright/e6b083faeb2f8010VgnVCM100000f932a8c0____> (viewed 30 October 2006): A survey of food manufacturers in the US in 2005 showed that outsourcing is a major trend in the industry, reducing staff. At the same time, budgets for in-house engineering staff are increasing, showing that automation and control systems as well as in-house ownership of expertise and development of new products is important.

[128] K. Higgings, State of food manufacturing: period of polarization emerges, published by Food Engineering, (BNP Media), 28 September 2005 (viewed on 4 November 2006)

[129] For a complete overview of the last 4 years, see: <http://www.fft.com/fftt/servlet/fftt/template/com,M_a.vm> (viewed on 12 November 2006)

local smaller companies or large multinational food companies selling and buying parts of each others' business.

Table 12: Leading mergers and acquisitions 2000 to 2006

Acquiror	Target	Value (bil. $)	Date Completed
Del Monte Foods Co.	Milk Bone Dog Food (owned by Kraft Foods)	0.58	Pending
Del Monte Foods Co.	The Meow Mix Company	0.71	Pending
Cadbury Schweppes PLC	Dr. Pepper/Seven Up Bottling Group	1.18	May-06
HJ Heinz Co.	HP Foods Limited	0.86	Aug-05
Wm. Wrigley Jr. Co.	Lifesavers (owned by Kraft Foods)	1.48	Jun-05
Hershey Co.	Mauna Loa Macadamia Nut Company	0.13	Dec-04
J.M. Smucker	International Multifoods	0.87	Jun-04
Dean Foods	Horizon Organic	0.22	Jan-04
Pilgrim's Pride	ConAgra's chicken division	0.55	Nov-03
McCormick & Co.	Zatarain's	0.18	Jun-03
Cadbury Schweppes PLC	Adams (Pfizer's gum business)	4.20	Mar-03
Nestlé SA	Chef America	2.60	Sep-02
Del Monte Foods Co.	H.J. Heinz (certain businesses)	2.50	Dec-02
Suiza	Dean Foods	2.70	Dec-01
Nestlé SA	Ralston Purina	10.30	Dec-01
General Mills	Pillsbury	10.50	Nov-01
Tyson Foods	IBP	4.40	Sep-01
PepsiCo	Quaker Oats	13.40	Aug-01
Sara Lee	Earthgrains	2.80	Aug-01
Coca-Cola Enterprises	Herb Coca-Cola	1.40	Jul-01
Kellogg Co.	Keebler	4.00	Mar-01
Kraft Foods	Nabisco	18.90	Dec-00
Unilever NV	Bestfoods	24.30	Oct-00
Cadbury Schweppes PLC	Snapple Beverage Group	1.45	Oct-00
ConAgra Foods	International Home Foods	2.90	Aug-00
Unilever NV	Slim-Fast	2.30	May-00
Unilever NV	Ben & Jerry's	0.33	May-00

Source: Standard and Poor's, Industry Surveys – Foods & nonalcoholic beverages, 8 June 2006, p. 16

The mergers and acquisitions have been undertaken by large food companies whose profit margins have been under pressure, for some of the following reasons:

- They have been acquiring companies with existing brands in the countries into which they wanted to expand, rather than introducing new products and brands[130]. Where this takes place within the range of product categories they already have, they can benefit from some economies of scale in developed country markets where they have been acquiring, in order to compete more fiercely in the markets of their rivals.

- In order to achieve top market share positions in new markets, global food companies are undertaking selective acquisitions of local top quality ("premium") brands within the range of their of product categories. For instance, Nestlé and Unilever are competing in ice cream in many markets, and are trying to obtain larger global market shares by acquiring the most successful existing ice cream brands, e.g. Häägen Dazs by Nestlé and Ben and Jerry's ice cream by Unilever.
- Expansion into new products, including organic products, through mergers and acquisitions prevents companies having to make huge investments when bringing a new product to the market, for example the acquisition of Quaker Oats (snack bars) by PepsiCo.[131]
- Buying up products which are parts of existing companies that are divesting.

An example of how large multinational semi-processed and processed food and drink companies are able to use their financial strength to take over a new segment in the market through mergers and acquisitions is the organic market. Mainstream food multinationals were able to ignore organic farming and products in the past, but the increasing demand for healthy products has made the organic market a profitable one. Mergers and acquisitions have enabled them to quickly enter the market and acquire the most profitable organic producers, without having taken the risk to introduce these organic products. Figure 10: Organic Industry StructureFigure 10 indicates that this trend is being used by many large companies in the industry. The trend is continuing, for instance with the purchase by Hershey (US), one of leading chocolate product companies in the world, of Dagoba in October 2006 because of the "dramatic growth" in consumer demand for healthy, high-quality organic chocolate products.[132]

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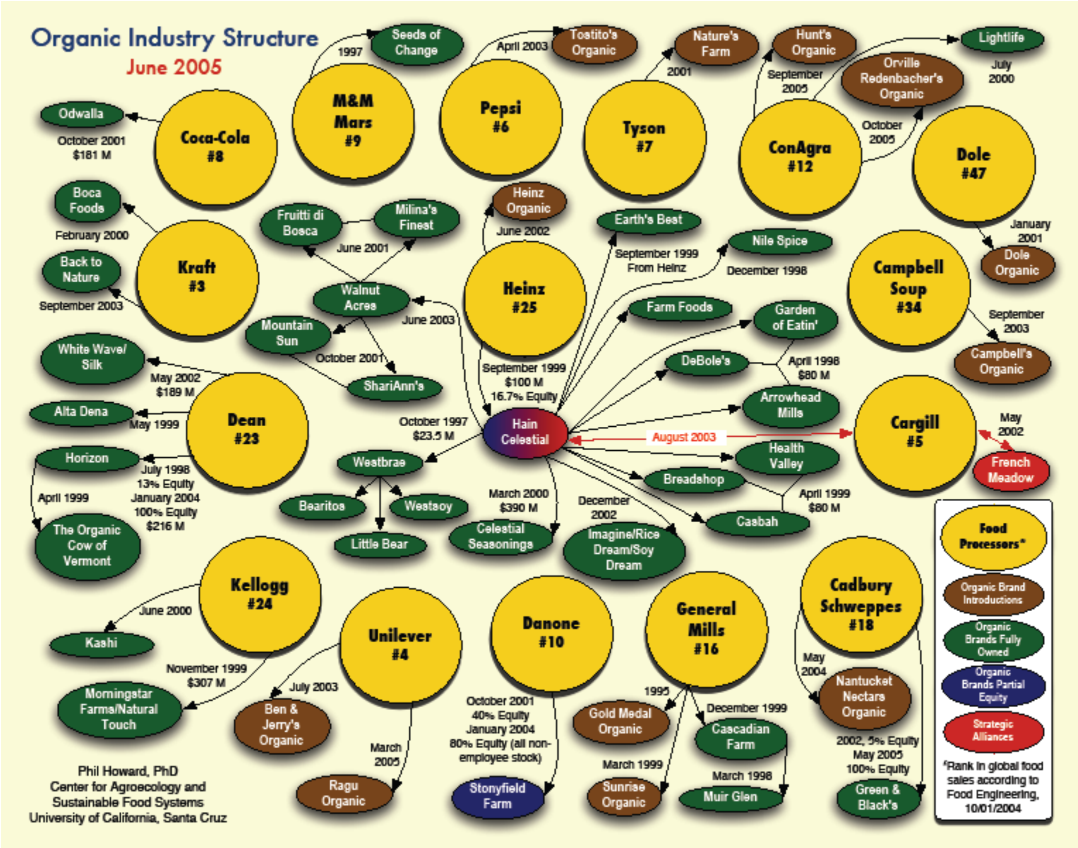
[130] This analysis is based on [130] A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 64.
[131] Euromonitor International, The World Market for Packaged Food, June 2006, p. 8.
[132] "Leading Manufacturer of Organic Chocolate Builds On Chocolate Leadership Position By Entering Rapidly Expanding Organic Segment", press release by Hershey, 19 October 2006, < http://www.thehersheycompany.com/news/release.asp?releaseID=918471> (viewed 10 November)

Figure 10: Organic Industry Structure



Source: P. Howard, University of California, quoted in [booklet with results from Paris workshop; used by Bill]

→ Critical issue

As soon as a developing country becomes a profitable market, existing food multinationals can quickly draw on the necessary financial resources and skills to acquire and merge, rapidly gaining larger market shares in a new country. This reduces the number of opportunities for the many smaller or local producers to grow on the basis of the improved market possibilities, and many underdeveloped processing companies could have difficulty surviving the rapidly increased competition. More research is needed to have exact figures of ownership of processed food companies in developing countries, the impact of foreign processed food companies and how far increased value added through increased processed food sales is also beneficial to domestic economies.

Mergers and acquisitions have allowed the food industry, and certain sectors in particular, to become more global at a high speed, despite the fact that food multinationals respond to consumer preferences at a local level and the global market still does not have high levels of concentration.

Divestment

Large food companies are selling off their brands (manufacturing, brand, marketing) to others, sometimes formal rivals in that product sector, usually when they are implementing a strategy of focussing on a smaller range of top brands in which they have leading positions and are most profitable. Examples include Unilever and Heinz,[133] who have been selling off most of their frozen food business since 2005. Apart from those two companies, Kraft Foods and Sara Lee are also implementing this strategy, following an era in which Western companies tried to expand through a variety of mergers and acquisitions of products and brands which are now no longer seen as belonging to the core business, or which are contributing to excessive levels of company debt.[134] Often, the product group ends up in the hands of another large food processing multinational which does see that sector as its core business. For instance, Cargill sold off its seed business to Monsanto, which is now the biggest seed company in the world and is estimated to control 41% of the global commercialised maize seed market.[135] By becoming leading companies with large market shares of a selective range of certain products, manufactured food and drink companies have more bargaining power with large retailer chains.[136]

Divestment transactions can involve exchanging company shares, whereby the selling company becomes part-owner of the buying company, leading to **cross-ownership**. One example of this is Heinz selling 8 factories and several brands, worth US$ 1.1 bn in sales, to Del Monte Foods in early 2003.[137]

2.3.2. Strategic alliances, joint ventures, Co-branding, etc.

An interesting strategy by some leading semi-processed and processed food and drink companies is the use of strategic alliances, co-branding and joint ventures. Rather than compete or acquire, which can be a costly business, some companies are using cooperative agreements with one of their rivals or with another interesting company to increase sales for some of their products and achieve rapid growth. Food Engineering[138], a food business magazine, identified Nestlé as the company which most often deploys the strategy of avoiding mergers and acquisitions and of using alliance strategies. These strategies are used in different ways[139]:

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[133] "Heinz wil af van Europese diepvriestak – groente van Hak staat al te koop", Het financieele Dagblad, 21 September 2005.wer000000

[134] Euromonitor, p 8, 16

[135] S. Murphy, Concentrated Market Power and Agricultural Trade, Ecofair Trade Dialogue Discussion Papers, No. 1, August 2006, <http://www.tradeobservatory.org/library.cfm?refid=89014> (viewed October, November 2006), p. 10.

[136] Standard and Poor's, Industry Surveys – Foods & nonalcoholic beverages, 8 June 2006, p. 1; see also: A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 67.

[137] K. Higgins, The World's Top 100 Food & Beverage Companies, published by Food Engineering, (BNP Media), 5 November 2003 < http://www.foodengineeringmag.com/CDA/Archives/b8cdd4f4472f8010VgnVCM100000f932a8c0_> (viewed 30 October 2006)

[138] Ibid.

[139] For some experiences already undertaking in the 1990s, see: D. Toma, Agri-food alliances which work:

Large food companies seek **strategic alliances** or, contractual arrangements, with local producers and distributors or retailers for the purpose of entering, or increasing sales in, a certain country by catering to local demands and making use of the experience of existing distribution channels and marketing. This strategy is used by multinational food manufacturers, such as Nestlé, Unilever and Kraft Foods.[140] Strategic alliances are also used to reduce the costs (such as those for research and development, and training) of creating new products and to meet stringent food safety and security requirements. Some companies are using strategic alliances to improve the sourcing of ingredients and inputs which can lead to vertical integration.

A more intense form of strategic alliance and cooperation are **joint ventures,** which are used when both parties think they can benefit from each other in terms of increasing their business. Some of these joint ventures are taking place between global leading food and drink companies in certain product areas. For instance, Beverage Partners Worldwide (BPW) is a fifty-fifty joint venture between Nestlé and Coca-Cola created in 2001 after Nestlé and Coca-Cola Company had cooperated for 10 years in a joint venture called Coca-Cola and Nestlé Refreshments.[141] Interestingly, in order to compete with Nestlé's successful growth in bottled water in the US market, Coca-Cola had formed a joint-venture with Danone and in 2002 created CCDA Waters LLC to increase the distribution bottled water.[142] In April 2005, howeer, Danone sold its interest in the joint venture to Coca-Cola.[143] It is not unusual for a large food company to acquire its smaller joint venture partner after a successful period. Joint ventures can also be undertaken with companies outside the food sector, such as Nestlé's joint venture with L'Oreal (in which Nestlé already has a 26% share) to develop nutritional products with a cosmetic effect (developing its "well-being" food sector). [144] In some developing countries, foreign companies have been forced to form joint ventures in order to enter a market/country, because of laws forbidding foreign companies from totally taking over the local food industry.

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cooperating to compete -executive brief", presented to BeefNet Conference Meat & Livestock Australia, Sydney, June 1999, < http://www.ccaa.bz/papers/toma_alliancebrief.pdf> (viewed 12 November 2006)

140 Euromonitor International, The World Market for Packaged Food, June 2006, p. 3, 8.

141 Beverage Partners Worldwide (BPW) joint venture to refocus on black tea, press release, 2 November 2006, <http://www.ir.Nestlé.com/News_Events/Press_Releases/Press/Press_Template/News.htm?PressGUID={54914ABA-E614-4273-B712-C6E357250451}> (viewed on 11 November 2006): "Nestlé and The Coca-Cola Company today an-nounced both companies have agreed to refocus the activities of their Beverage Partners Worldwide (BPW) joint venture on ready-to-drink black tea beverages. The transaction, which is subject to certain regulatory approvals, is expected to close early 2007"

142 K. Higgings, , The World's Top 100 Food & Beverage Companies, published by Food Engineering, (BNP Media), 5 November 2003

143 Standard and Poor's, Industry Surveys – Foods & nonalcoholic beverages, 8 June 2006, p .11.

144 A. Benady, "Nestlé's market wars: the food giant is drawing on local expertise to put marketing at the heart of its global growth strategy", The Chief Executive, April 2005, < http://www.findarticles.com/p/articles/mi_m4070/is_207/ai_n13787808/print> (viewed on 11 November 2006)

2.3.3. *Co-branding or cross-branding*[145]

Co-branding or cross-branding is using the strength of one brand to stimulate consumer demand for another brand. One way is to get a license for a brand to be used on the packaged food products of another company, such as the agreement under which Mars permits Bravo! to market vitamin-enhanced milk drinks using the names Milky Way and 3 Musketeers. Co-branding can be realised with brands from other product categories, for example dairy products with bakery products in the cross-branding agreement between Danone and Kellogg in the US, under which Kellogg offers coupons for free Dannon Light n' Fit yoghurts on packs of Special K. But also brands from totally different product categories outside the food sector are used to promote sales or justify higher prices, for instance Walt Disney cartoon characters to promote products for children, and characters from popular films or television programmes.

Other types of alliances and joint ventures are also being established between different parts of the supply chain,[146] such as between growers and processing companies, or between a food company and a retailer to introduce a certain product into the market. This allows different parties in the value chains to coordinate their activities between them, use one another's strengths, but also to guarantee better products, supply, etc. Other ways of cooperation could include the use of third-party certification or a company-based tracking system which allows a certain quality (such as organic, a genetically modified seed) at the start of the production chain to be tracked throughout the chain up to the consumer, who is then willing to pay more for the better quality ingredients used in the processed food.

Through a wide range of alliances, joint ventures and contractual agreements, some companies are **vertically integrating** large parts of the value chain from seed to higher-value products. A key example of this is Cargill[147] which has a very wide range of alliances and agreements which, in addition to its mergers and acquisitions, has made it a very vertical integrated company worldwide. It has integrated the inputs (seed, pesticides) and production services to farmers[148], transportation (ship ownership, trucks, storage facilities), packaging (owning an alternative plastic packaging ingredient[149]) in its primary food processing activities. In addition, Cargill is offering a range of financial, asset management and risk management services, and even power and gas products and services.[150] Through its joint ventures and alliances, Cargill is partnering with companies that include those with large global market shares in their product segment, such as seed

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[145] Most of the examples are taken from : Euromonitor International, The World Market for Packaged Food, June 2006, p. 8.
[146] Information based on: A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 18-31.
[147] Information mainly based on: www.cargil.com, and S. Murphy, Concentrated Market Power and Agricultural Trade, Ecofair Trade Dialogue Discussion Papers, No. 1, August 2006, p. 9-15, <http://www.tradeobservatory.org/library.cfm?refid=89014> (viewed October, November 2006)
[148] See for instance: http://www.cargill.com/products/crop/ps_harvesthealth.htm, http://www.cargill.com/products/crop/ps_crop.htm (viewed on 13 November 2006);
[149] For all the partnerships for producing and commercialising the packaging, see: <http://www.natureworksllc.com/corporate/partner_package.asp> (viewed on 103 November 2006)
[150] See: http://www.cargillpowerandgas.com/products.htm

companies Bayer CropScience[151] and Monsanto.[152] The latter bought a large part of Cargill's seed industry in 1998, and is now working together with Cargill to produce a new vegetable oil. Cargill is also signing strategic alliances with other companies to develop bio-fuel.[153]

→ Critical issues

Divestments and especially strategic alliances, joint-ventures, co-branding, cross-ownerships and other forms of cooperation and coordination are making it much more difficult to map out concentration and assess domination in the food processing sector. In practice, the distinction between international competitors might be blurred and production and sales units all over the world less separated as in the past.[154] This is a challenging situation for the authorities to be adequately equipped to avoid abuses of market power and disfunctioning of the market (see Chapter 5).

Box 8: Fonterra, a multinational cooperative

Fonterra is a New Zealand based dairy cooperative, with a total of 11,600 shareholding farmers who produce an estimated 13.5 billion litres of milk per year. A total of 95% of all New Zealand's dairy farmers are part of this cooperative and as a result, Fonterra generates 20% of all exports receipts for New Zealand. However, the number of shareholders has been steadily declining over the last 5 years. The farmer-owned company is run by a board of directors, most of whom are elected by the shareholders. There are three operating divisions within the company. The global trade and ingredients division is responsible for the entire cow-to-consumer chain, and includes the NZMP brand that markets ingredients to the international food industry. The Fonterra brands division produces and markets dairy-based consumer products both within New Zealand and internationally. Their brands include Anchor, Anlene and Mainland. The Fonterra enterprises division deals with the research and development of dairy ingredients and brands.

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[151] Cargill, Bayer CropScience Form Alliance to Provide Market With Specialty Canola Oil, Cargill press release, 31 Janaury 2005, http://www.cargillspecialtycanola.com/files/pdf/NR-Cargill_Bayer_Alliance.pdf (viewed on 13 November 2006): an alliance to produce a special oil seed (canola) which will result in oil that eliminate trans fat and reduce saturated fat content, an ingredient for which US packaged food companies have been under attack)

[152] Cargill Monsanto joint venture to build corn plant, Reuters, 20 January 2006, http://bioproducts.osu.edu/content/view/25/2/ , (viewed 12 November 2006)

[153] See for instance: "Cargill signs renewable energy agreement", Foodnavigator.com-USA, 245 October 2006, < http://www.foodnavigator-usa.com/news/printNewsBis.asp?id=71557> (viewed 12 November)

[154] K. Higgins, The World's Top 100 Food & Beverage Companies, published by Food Engineering, (BNP Media), 5 November 2003).

As New Zealand has one of the cheapest production costs for dairy, one of Fonterra's main focal points is export. Fonterra claims to be the largest exporter of dairy in the world and to control 30% of all dairy traded globally. The company is present in dairy sales in 140 countries worldwide.

One of the strategies Fonterra uses to establish its position abroad is by forming strategic alliances and joint ventures, both with local companies and with other multinationals. It has signed up to the Dairy Partners America alliance with Nestlé, in which Fonterra will be responsible for the raw materials, while Nestlé will sell the branded products. This alliance is in place in Colombia, Ecuador and Trinidad & Tobago, while Fonterra is also active in other Latin American countries, such as Brazil, Chile and Argentina. Fonterra also has joint ventures in Sri Lanka, India, Europe and the USA. While most of the ingredients used for their products are shipped from New Zealand, an estimated 22% come from third parties, including dairy from Australia and the United States. In the joint venture between Fonterra and Campina (NL) in the field of lactose ingredients for the pharmaceutical industry, Fonterra will produce its products in its home base in New Zealand, while they will be sold worldwide through various regional sales offices.

As a multinational cooperative, it has a very tight vertical and horizontal integration, enabling it to control the chain from primary production to consumer sales. It manages dairy herds, manufactures milk products, and distributes final products in retail markets. It also integrates packaging, transportation, shipping and quality control. In markets with strict requirements, such as the UK, Fonterra maintains tight control over the raw products. In other markets with less strict regulations, Fonterra often resorts to outsourcing within the supply chain.

During its 5-year existence as an integrated cooperative, Fonterra's revenues have been gradually growing to NZL$ 13 bn (€ 6.7 bn) in 2005/2006 . This is an increase of 6% in comparison with the previous year. Most of the revenue growth has come from the increase in ingredients sales. All its operating surplus is paid out to the shareholders as payment for the milk delivered. In other words, the surplus determines the price that the company pays to the farmers for every litre of milk supplied. In 2005, Fonterra's profit of NZL$578 million was pure profit which amounted to just under NZL$50,000 per farmer (€25,750).

Source: http://www.fonterra.com/default.jsp; http://www.fonterra.com/pdfs/05-06FonterraAnnualReportFinal.pdf; A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 71; http://www.foodnavigator.com/news/ng.asp?id=51490-nestle-expands-milk; http://www.prnewswire.co.uk/cgi/news/release?id=166870

2.3.4. Do cooperatives offer a good model?

In order to confront concentration and other hindrances to marketing their products, agricultural producers and primary processors have used cooperatives as a way to market the products of their members, who own and control the cooperative and share in the profits or benefits. Some production cooperatives in Western countries have expanded to include food processed from their products. Such a strategy is often difficult due to a lack of financial resources. In the US, some cooperatives who engaged in processing have had to file for banckrupcy, such as Tri Valley Growers – the largest fruit and vegetables cooperative in the US. Analysts A. Regmi and M. Ghehlhar attribute the failure of producer cooperatives to diversify into processing on a lack of response to consumer demand, oversupply that was not managed (leading to excessively low prices), an overly large range of diverse products and a failure to restructure to achieve the right size of competitive production. Other cooperatives, such as Fonterra Dairy Cooperative from New Zealand, have become very successful. Fonterra is now the world's leading dairy exporter and 12th largest dairy product manufacturer, competing with Nestlé, Danone and Parmalat (see Box 8). One of its strategies has been to engage in a strategic alliance with Nestlé in various countries in Latin America and Central America and the Caribbean, as Nestlé wants to move out of the less profitable market of raw milk processing.[155]

Even if it is not always clear why a cooperative fails or succeeds, some analysts[156] see some common characteristics shared by successful international cooperatives, namely:

- close vertical and horizontal coordination from primary production to final consumers, which can reduce transaction costs and improve product quality
- obtaining the right focus of products, the right range and number of products, and responding to changing product and quality demands by consumers, in order to be able to produce efficiently and with a competitive edge
- support from well-developed research and development (R&D), and technology
- education, training and communication with the members as growers and shareholders
- avoiding alienation and conflict between the cooperative company and the growers
- ensuring good management and leadership - membership is not always educated to run an international cooperative company

In some agricultural sectors, the cooperative structure might be an impediment, while some other sectors seem to be well-suited to processing cooperatives, such as meats, dairy, and horticultural products – these are sectors with a strong link to the producers.[157]

→ Critical issues

Southern producers who wish to use the **cooperative structure** to add value to their process by processing themselves need a complex and well-managed

[155] L. Partos, "Nestlé expands milk ingredient alliance in South America", Foodnavigator.com, 20 April 2004, <http://www.foodnavigator.com/news/ng.asp?id=51490-Nestlé-expands-milk> (viewed October - November 2006)

[156] A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p. 71; I. Donoso, N. Shadbolt, W. Bailey, The internationalisation of agricultural co-operatives – A source of conflict? Paper presented at the 2004 IAMA World Food & Agribusiness, 12-15 June 2004, < http://www.ifama.org/conferences/2004Conference/Papers/Shadbolt2002.pdf> (viewed October –November 2006)

[157] A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, nr. 794, February 2005, p . 71.

structure that integrates the different stages of the chain up to supply and marketing. This requires a lot of financial and human resources which are not easily obtained, and requires some time for training, adaptation, learning from experience, etc.

2.4. Summary and conclusions

The food-processing industry can largely be divided in two main groups of companies with different ranges of products, different production strategies, and different trade and sales channels. Firstly, there is the market of the primary processing of commodities, or semi-processing of food that is produced and traded around the world and constitutes the ingredients for the fully processed food manufacturing. This market is highly concentrated at the national, regional or global level for some products, such as soy oil and cocoa, with a very few companies producing or sourcing, primary processing, trading and selling. The same agribusiness multinational can be dominant in different commodity processing and trading, such as Cargill, Bunge, Archer Daniels Midland (ADM). Most global leading companies in this sector have US headquarters. This domination by a few agribusinesses has a great influence on how much developing countries can benefit from primary processing, and makes their food processing more dependent on these foreign companies even for ingredients grown in their own countries. It can also negatively affect government regulations and influence trade negotiations.

The other market is that of manufactured food and drinks, or packaged processed food and beverages, ready to eat or drink, and for direct sale to the consumer. This market is diverse, with new trends of ready-to-eat meals, healthy or functional food, especially in the saturated developed country markets, and more basic food such as bakery and dairy products being sold in developing countries. This market shows little concentration at the global level, with the number one food multinational, Nestlé (Swiss), only having 3.3% of the world market (2004). However, the top 10 companies that are leading at the global and many regional levels, show much larger market shares at the national or regional level, particularly for some packaged food and drink products whose production formulas they own and whose sales are heavily influenced by marketing. This makes it more difficult for small and developing country processors to enter the market, at home or abroad.

Global brands and companies, as well as small food manufacturers, are being seriously challenged by supermarket strategies. Firstly, by the increasing sales by supermarket chains of their own private labels - also called house brands - which now have a market share of more than 12% of the global packaged food retail sales. Private labels are now ranging from cheap low quality goods to higher quality products or exclusive products of a supermarket chain that sometimes uses different kinds of private labels. They are also introduced by supermarkets in developing countries where they can challenge local brands. Still more research needs to be done into the conditions in which private labels are produced – by small, medium or brand product manufacturers – in terms of workers’

conditions and income, profits and retailer buyer power, environmental impact, impact on the supply chain, benefits for developing country processing industry, etc.
Secondly, supermarkets, hypermarkets and discounters are increasingly becoming concentrated into a small number of players, and as a result of buyer power, and sometimes abusive practices, are able to squeeze the prices of food companies, even the largest food multinationals. The rapid expansion of the same small number of supermarket chains in developing countries affects the food and drink companies in these countries, especially the smaller ones, as supermarkets require large volumes at high quality and low prices, and source from outside the country if this is more profitable.

Packaged food companies have reacted with a wide range of strategies to compete against their rivals and increase their profits by cutting costs, including shedding many jobs, increasing efficiency and making supply chains more integrated, enabling inputs to be globally sourced (see also Chapter 3 for the negative impacts of these strategies). Where possible, manufacturing is also concentrated into one or a few units per continent. Food and drink companies are trying to rapidly respond to consumer demands for healthier, higher quality, environmentally friendly and new products, and increasing or innovating their marketing, some of which has been criticised for being irresponsible (see Chapter 3) or illegal (see Chapter 5). One of the strategies developed by food multinationals in the South is creating smaller packaging sizes, in order to increase sales to the poor . As it is important in the processed food sector that food and drinks cater to local tastes and consumer demands, the food and drink industry of the North has expanded in developed countries and especially developing countries with profitable markets by means of mergers and acquisitions, divestments of non-core or non-profitable operations, strategic alliances, joint ventures with experienced local companies, co-branding and cross trading. This has led to concentrations which are opaque and difficult to investigate.

As a result of these strategies of multinationals and developments in Western markets, developing countries who want to diversify away from primary commodity production therefore face difficulties in building up their processed food and drink sector sector or expanding it in the home market, even when consumer demand is rapidly increasing. The growing complexities and sophistication of Western food products and markets, where fresh processed food sales are increasing, make it increasingly technologically and financially demanding for Southern food and drink enterprises to access and export to Northern markets, even if tariffs and other trade barriers would be removed. Some cooperatives have successfully been able to overcome these difficulties, while others have failed.

Solutions for enabling developing countries to build up a sustainable and equitable primary and fully processing food and drink industry include providing domestic support to the private sector and governments, for training, infrastructure etc., as well as through changes in: trade and investment policies (see chapter 4), (international) standards setting and enforcement (see Chapter 4), competition policy and purchasing practices to enable better prices (see Chapter 5) and corporate social responsibility initiatives (see Chapter 3).

Chapter 3
Critical issues and CSR in the processed food industry

The processed food industry, obviously, greatly contributes to society in terms of aspects such as services and employment. Yet some of the issues in the sector regarding the industry's negative environmental, social and economical impact and its relationship with poverty eradication are much less apparent. Below (section 3.1 to 3.4) is an outline of some of the issues in the processed food industry from a sustainable development and CSR perspective in the media. The last section (3.5) of this chapter provides an overview of the various CSR initiatives that companies in this sector have joined or formed to address some of issues discussed.

This chapter focuses on food processing for the retail sector. It will not generally be looking at CSR issues in food services and primary processing. However, statistics often make no distinction between subsectors in food processing, so some of the trends (gender, for instance) outlined reflect the industry as a whole (including food service). Additionally, we will be looking at the sector's key players in terms of market share, and ignoring their activities outside the food sector - both Nestlé and Unilever for instance have important non-food activities. Moreover, we will focus on critical issues in food processing and the marketing of food itself only, not on issues in sectors that supply the food sector, such as the agricultural and energy sector. The agricultural sector, for example, is well-known for its lack of respect of workers rights and adverse environmental impact. This means that many critical issues, *arguably the most important from a poverty eradication and sustainable development perspective,* are left out or will remain underexposed in this section. However many of these issues have already been discussed in SOMO's report "Who reaps the fruit" (June, 2006) on the fresh fruit and vegetable (FFV) sector.

3.1. Social (labour) issues

Worldwide, and excluding the large informal food sector, the food and drink industry employs 66 million people. But while production is growing, employment declined marginally in the industrialised countries and grew marginally in developing countries during the nineties[158]. In general, jobs are under pressure, among other things by increased mechanisation and productivity that has led to restructuring and mergers and acquisitions in the sector. Unilever, for example, has progressively reduced its global workforce in order to remain competitive. Total employment declined from 308,000 in

[158] ILO website, "Employment, technology, research and training", March 2006, <http://www.ilo.org/public/english/dialogue/sector/sectors/food/emp.htm> (28-11-06).

1995 to 206,000 in 2005. One way of cutting jobs has been to close production plants in different countries, sometimes without previous notice and in breach of the OECD guidelines[159].

And while the multinationals in the sector are very successful at making large profits, according to the IUF, the perpetual quest to maximize profits and lower production costs of these companies leads "to a worsening of employment and working conditions, plant closures, production transfers and restrictions on trade union rights[160]." This section will be outlining some of these issues. It should be mentioned however that mass layoffs and many of the other critical issues below are certainly not unique to this sector but can be found in many other important sectors.

3.1.1. Freedom of association

Many large multinational food companies have operations in countries where union freedom is restricted, such as Colombia, Philippines, Kenya and Brazil, or in countries where independent unions are forbidden, such as China. In these countries, unionized workers have to be prepared to face intimidation, violence and - in extreme cases such as in Colombia - even death. In such countries, it is difficult or impossible for companies to guarantee their employees this core labour right.

In addition, leading food processing companies such as Nestlé[161], Coca-cola[162], PepsiCo[163], Unilever[164], Dole[165], InBev[166] and Campbell Soup Co[167] have been accused by NGO's and trade unions of undermining (independent) union activities in some of their overseas operations. Problems include undermining of genuine free union activities by pro-forma unions, casualisation (replacing steady jobs for temporary workers thereby

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159 IUF website, "Outlaw Conduct by Unilever Indian Subsidiary Prompts International Union Action at OECD" October 2006, < http://www.iufdocuments.org/cgi-bin/dbman/db.cgi?db=default&uid=default&ID=3745&view_records=1&ww=1&en=1> (7-12-2006)

160 Peter Rossmann, Bern, "30 October, Seminar on Worker and Trade Union Rights in Nestlé", IUF, October, 2006, <http://www.multiwatch.ch/fileadmin/BeitraegePresseAnhoerung/WorkshGewRechte_Rossmann.pdf> (28-11-06).

161 Corporate Watch website, "Union Busting", no date, <http://www.corporatewatch.org/?lid=240#union> (14 aug 2006).

162 Corporate Campaign website, Campaign to stop killer coke, "Coke can't hide its crimes in Colombia", no date, <http://www.corporatecampaign.org/killer-coke/crimes-isidro.htm> (28-11-06).

163 ICFTU website, Annual Survey of Violations of Trade Union Rights, "Trade union rights in law" <http://www.icftu.org/displaydocument.asp?Index=991223945&Language=EN> & <http://www.icftu.org/displaydocument.asp?Index=991219413&Language=EN> (28-11-06).

164 ICFTU website, Chile: Annual Survey of Violations of Trade Union Rights, "Trade union rights in law" http://www.icftu.org/displaydocument.asp?Index=991223864&Language=EN (28-11-06).

165 World Socialist website, Worker's Struggles Around the World, "Worker's struggles: Asia, Australia and the Pacific," September 2003, <http://www.wsws.org/articles/2003/sep2003/lab-s13.shtml> (28-11-06).

166 IUF website, "World's Largest Brewer Inbev Leaves a Bitter Taste of Lies and Layoffs," March 2006, <http://www.iufdocuments.org/cgi-bin/dbman/db.cgi?db=default&uid=default&ID=3225&view_records=1&ww=1&en=1> (28-11-06).

167 ICFTU website, "USA: Annual Survey of Violations of Trade Union Rights," 2002, <http://www.icftu.org/displaydocument.asp?Index=991215646&Language=EN> (28-11-06).

undermining workers rights), threats to close plants if worker demands are considered too high by the company management and refusal to acknowledge unions and/or to inform, or negotiate with, them on important matters. Large commodity processors such as Bunge[168] and Cargill[169] have also received criticism in this respect.

Box 9: CSR issues in tea processing in Indonesia

To prevent loss of quality, tea needs to be processed (dried, withered, cut) within hours of picking the leaves. Other processing activities in this industry include blending, packing, brewing and bottling (ice tea) of tea. Wages in tea processing are higher than in tea picking, and range from below to above regional minimum wage levels. Minimum wage levels in Indonesia often do not provide a worker and family with a decent standard of living. While permanent workers regularly have additional benefits, such as free housing and free primary education, the majority of factory workers are hired on a temporary basis, and are entitled to fewer or no benefits.

Union tradition is still very weak in the Indonesian tea sector. While some companies might support union activity, companies normally intervene to ensure that union leaders are loyal to company management. Sometimes unions are dissolved by companies if they are considered to be a threat, and in some cases there is no collective bargaining. In general, CSR is underdeveloped in this country’s tea sector, and actors that are familiar with the concept often refer to philanthropic activities instead of, for example, supply chain responsibility. The latter is mostly absent in the purchasing practices of buyers that are only interested in quality and price. The upstream market is heavily concentrated. Unilever buys 70% of all tea sold at the Jakarta auction through which the tea of government estates (see also Box 2 in Chapter 1) is sold.

Source: V.R. Kustanti, Business Watch Indonesia, Tea Sector in Indonesia (2006) (unpublished report)

3.1.2. Gender issues, discrimination and migrant workers and other labour issues

Up to a quarter of the total number of people employed as food processing workers in the US are women[170]. In the UK, women occupy a third of the jobs in this country’s food processing[171].Other countries for which data were available show wide discrepancy in this ratio from around 55% in countries such as Japan, Lithuania and Vietnam to (well) below

[168] SOMO, Quick Scan Bunge, 2005.
[169] ICFTU website, Brazil: Annual Survey of Violations of Trade Union Rights, “Trade union rights in law,” 2006, <http://www.icftu.org/displaydocument.asp?Index=991223949&Language=EN> (28-11-06).
[170] ILO website, Food; Drink; Tobacco, “Gender discrimination,” March 2006, <http://www.ilo.org/public/english/dialogue/sector/sectors/food/gender.htm> (28-11-06)
[171] DEFRA, Draft Food Industry Sustainability Strategy (ISS), April 2005, <http://www.defra.gov.uk/corporate/consult/fiss/draft-fiss.pdf#search=%22A%20draft%20Food%20Industry%20Sustainability%20Strategy%20%22> (28-11-06), p.56.

10 % in Islamic countries such as Quatar, Oman and Jordan[172]. Women account for a large proportion of low-skilled and low-paid jobs in this sector worldwide and there has been little improvement in their position over the years in many countries. Partly this has to do with technological changes in processing in the sector over the years, that require new skills[173]. Other factors include job segregation: male-dominated tasks (such as handling machines and tasks that involve heavy work) are better compensated than the typically female-dominated work[174], and fewer opportunities for promotion to senior jobs or for employment as managers (`glass ceiling`). In the UK, for instance, women are under-represented in senior jobs, as are ethnic minorities and disabled people. In the UK, women in food processing are paid 22% less than men (regardless of their position)[175]. Three top US food companies, PepsiCo, Kraft and Sara Lee, however, have female CEOs. Strategies to diversify (top) management tasks are more common in the US than in the EU, for instance.[176]

In some US states, migrant workers or refugees constitute a significant part of the workforce in the food processing industry[177]. Many of these are women. In the UK, for instance, it is acknowledged that meat and fish processors are increasingly relying on temporary (illegal) migrant workers through "gangmasters". Some of these workers are especially vulnerable to abuse because they are dependent on people traffickers[178]. Several cases of (alleged) maltreatment of temporary workers and discrimination at leading food processors including PepsiCo, Coca-cola, Sara Lee and Del Monte have been reported in the media. Cases include charges (and sometimes convictions) of racial[179] and sexual[180] discrimination, illegal dismissal, not allowing temporary workers to take time off[181] and sexual harassment[182].

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[172] UNIDO, The International Yearbook of Industrial Statistics 2006 (Abingdon: Marston Book Services Ltd., 2006), p.71-75.

[173] ILO website, Food; Drink; Tobacco, "Gender discrimination," March 2006, <http://www.ilo.org/public/english/dialogue/sector/sectors/food/gender.htm> (28-11-06)

[174] Regeringskansliet, Women's and Men's Wages in the Food Industry, 2003, <http://www.nrckvinnor.org/documents/dok/doc/AAAAJGBG.pdf#search=%22eu%20wages%20food%20industry%22> (28-11-06)

[175] DEFRA, The Economic Position of the Agri-Food Sector: Quarterly Analysis, December 2003, <http://statistics.defra.gov.uk/esg/reports/afq/afqbrief_dec.pdf#search=%22full-time%20gender%20pay%20gap%20UK%20food%20sector%22> (28-11-06), p.15

[176] P. Couwenberh and J. Strop, "De nieuwe rolmodellen van Unilever", Het Financieel Dagblad, 27 September 2006.

[177] ILO website, Food; Drink; Tobacco, "Gender discrimination," March 2006, <http://www.ilo.org/public/english/dialogue/sector/sectors/food/gender.htm> (28-11-06)

[23] DEFRA, Draft Food Industry Sustainability Strategy (ISS), April 2005, <http://www.defra.gov.uk/corporate/consult/fiss/draft-fiss.pdf#search=%22A%20draft%20Food%20Industry%20Sustainability%20Strategy%20%22> (28-11-06), p.60.

[179] ICFTU website, "Trade Unions Say No to Racism and Xenophobia," <http://www.icftu.org/displaydocument.asp?Index=991213215&Language=EN> & K. Ashton, "Man sues Coca-Cola, alleges bias," Daily Hampshire Gazette, May 2005, p.1.

[180] B. Louis, "Dallas Woman Sues Sara Lee Corp. over Alleged Job Discrimination," Knight Ridder Tribune Business Review (September 2004), p.1.

[181] B. Hunsberger, "Del Monte Forced Firings, Temp-Firm Owner Says," The Oregonian, August 2006, p.1.

[182] IUF website, Women Workers Network, "PepsoCo Poland- Latest News", February 2005,

3.1.3. Wages

In the US, production workers in food processing -who constitute more than half of the jobs in this country's industry- work longer and get paid less than workers in other industries[183]. According to the ILO, food processing workers in the US, and many other countries, rarely earn a "living wage". While thirty-four percent of all food manufacturing workers are employed in plants that slaughter and process animals in the US[184], gross annual incomes from meatpacking and poultry processing jobs are usually around federal poverty levels. Earnings in US fish processing can even fall to half of the established poverty levels[185]. However, while in the UK hourly wages in the processed food sector are about 15% lower than the national average across all sectors186, they are on average well above national minimum wage levels.

3.1.4. Health and safety

Relative to other industries, the food processing industry has one of the highest incidences of injury and illness. This can be explained by the nature of the work. Many jobs in this industry are production jobs, for which little training or education is necessary. Production workers account for 53% of all food processing jobs in the USA, for example. Production-related work in this industry, such as slaughtering, baking and operating machines for packing and canning, is often repetitious and physically demanding. This is because of factors such as noisy working environments with (sometimes) uncomfortable temperature (too hot, too cold), working odd hours, heavy lifting and using potentially dangerous tools and machines. Animal slaughtering plants have the highest incidence of injury in the sector[187].

3.1.5. Irresponsible marketing

The CSR issue that has received most attention in the media recently is the food industry's role in the obesity epidemic that has hit developed countries, in particular. More specifically the food industry has been criticized for, among other things, "super sizing" (serving/selling large portions of high-fat, high-calorie foods), targeting children with high-fat, high-calorie foods through media and toy promotions and saturating distribution channels such as schools, with high-fat, high-calorie foods.

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http://www.iuf.org/women/2005/02/pepsico_poland_latest_news.html#more (29-11-06) & "IFU Raises Serious Concerns about Pepsico," February 2005, http://www.iuf.org/women/2005/02/iuf_raises_serious_concerns_ab.html#more (29-11-06).

183 US Department of Labor website, Bureau of Labor Statistics, "Food Manufacturing," December 2005, <http://www.bls.gov/oco/cg/cgs011.htm> (29-11-06)

184 Idem.

185 http ILO website, "Employment, technology, research and training", March 2006, <http://www.ilo.org/public/english/dialogue/sector/sectors/food/emp.htm> (28-11-06).

186 DEFRA, The Economic Position of the Agri/Food Sector Quarterly Analysis, December 2003, p.16.

187 US Department of Labor website, Bureau of Labor Statistics, "Food Manufacturing," December 2005, <http://www.bls.gov/oco/cg/cgs011.htm> (29-11-06); U.S. Department of Labor website, Bureau of Labor Statistics, *Occupational Outlook Handbook, 2006-07 Edition*, "Food Processing Occupations," <http://www.bls.gov/oco/ocos219.htm> (*15-08-06)*

The debate over the role of food companies in the epidemic is certainly not over yet. In the United States the first law suits against food companies started in 2003 (against Kraft Foods)[188] and in 2002 against fast food firms (McDonalds, Burger King, etc)[189]. In addition, some leading packaged food companies have been accused of irresponsible marketing. Claims include irresponsible marketing of foods that contain mostly fat and sugar as healthy (for instance Kellogg's[190], Nestlé[191]) and (other) false health claims (for instance Unilever[192], Nestlé[193]) and marketing targeted at children (Nestlé[194], Coca-cola[195], Pepsi[196]). Another controversial issue with respect to advertising is the promotion of breast milk substitutes by some of the leading food companies (for instance Nestle and Heinz[197]).

3.1.6. GMO's and food safety

Similarly, the industry has been at the centre of a heated debate concerning GMOs in Europe, which started with the introduction of GMO in the EU at the end of the nineties. The leading companies in the sector have in the past endorsed (and some still endorse) the use of certain ingredients derived from GMO in food and acted accordingly (processing of GMOs in food, related research, lobbying) while most EU consumers claim to not want GMO-derived products in their food. The industry has also received criticism over marketing products the safety of which is disputed. For instance, both Pepsi and Coca-Cola have been accused several times of selling products in India that contain unacceptably high levels of pesticides,[198] leading to a state ban on their products in three Indian states[199]. Needless to say, with the industry being so large and the quantities of foods processed being enormous, there are bound to be food safety incidents. In the

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[188] C. Watkins, "Can Obese People Sue the Food Industry - and Win?, Inform, August 2005, <http://www.wrf.com/docs/news/2044.pdf> (29-11-06).

[189] "Fat Americans Sue Fast Food Firms," BBC News World Edition, July 25th 2002, <http://news.bbc.co.uk/2/hi/americas/2151754.stm> (29-11-06).

[190] The Ecologist, "Behind the Label KELLOGG'S NUTRI-GRAIN - SOFT BAKE BARS", March 2006 <http://www.theecologist.org/archive_detail.asp?content_id=588>..

[191] "Children Encouraged to Advertise to Themselves," Food Magazine, April/June 2005, <http://www.foodcomm.org.uk/PDF%20files/children.pdf> (12-12-06).

[192] Food Magazine, Press Release, ASA Slams Health Claims on Salty Soups, July 2003, <http://www.foodcomm.org.uk/press_knorr_july03.htm> (12-12-06) & "Do We Need to Be Buying Plant Sterols?," Food Magazine, October 2004, <http://www.foodcomm.org.uk/17.pdf> (12-12-06).

[193] Corporate Accountability International website, What's at Stake?, "Expose the Realtiy Behind Bottled Water," no date, <http://www.stopcorporateabusenow.org/campaign/exposebottledwater/explanation> (12-12-06).

[194] "Children Encouraged to Advertise to Themselves," Food Magazine, April/June 2005, <http://www.foodcomm.org.uk/PDF%20files/children.pdf> (12-12-06).

[195] M. Simon, "Junk Food's Health Crusade," Multinational Monitor, March/April 2005, <http://www.multinationalmonitor.org/mm2005/032005/simon.html> (12-12-06).

[196] Ibid.

[197] See for instance the baby milk action website: www.babymilkaction.org, for Heinz reference, Corporate Critic website, http://www.corporatecritic.org/abstracts.aspx?IDs=245481 (10 august 2006).

[198] J. Vidal, "Things Grow Better with Coke," The Guardian, November 2nd 2004 <http://www.guardian.co.uk/india/story/0,12559,1341454,00.html#article_continue> (29-11-06); R. Devraj, "Indian Coke, Pepsi Laced with Pesticides, Says NGO," India Resource, August 5th 2003, <http://www.indiaresource.org/news/2003/4725.html> (29-11-06).

[199] R. Ramesh & S. Jha, "India Bans Soft Drinks in Pesticides Row," The Guardian, August 7th 2006, <http://www.guardian.co.uk/india/story/0,,1839137,00.html> (29-11-06).

United States for example there have recently been a few high profile incidents in which food sold and/or processed by leading food companies such as Sara Lee and Conagra was accidentally contaminated with e-coli and listeria, and many millions of pounds of meat products had to be recalled. These incidents led to many people getting sick, and for a few of the affected consumers these accidental contaminations proofed fatal[200].

3.2. Corporate lobbying

There is a strong and influential lobby from the food and drink industry in both the EU and the US. Most relevant to sustainable development and poverty eradication is the lobby for free trade through trade negotiations, such as the WTO. Fewer trade barriers mean cheaper exports and imports of both processed and unprocessed foods, and therefore potentially greater profits for food companies. It also means more access to developing country markets. On the other hand, lobby groups clearly have a double agenda. Only on condition of unrestricted international free trade are they willing to give up the free-trade-distorting subsidies they receive both directly[201] and indirectly via cheap inputs for the foods they process from subsidised farming and export subsidies[202]. Developing countries can and do profit from (free) trade. Unrestricted free trade can however also be detrimental to their economies, and therefore to the livelihoods of the people within them, if (least) developed country governments are not allowed to protect their countries' sensitive sectors (see for a more detailed discussion of industry lobby chapter 5). Lobby activities by industries are controversial because they are considered undemocratic (no public scrutiny nor public debate), not transparent (especially in Europe but less so in the US, it is not clear how lobbyists work, for whom and how much influence they have on government policies) and potentially over-represent industry interests (an industry lobby has much more resources than a lobby of developing country governments or civil society bodies, for example).

3.3. Environmental issues

Food processing is not without environmental impact: externalities of food manufacturing include energy use for processing and transportation (resources, emissions of CO_2, NO_2, SO_2), processing and transport emissions (greenhouse gases, heavy metals,

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[200] See for instance: L. Heller, "Listeria Concerns Result in ConAgra Product Recall," Food Quality News, Februyary 12th 2005, <http://www.foodqualitynews.com/news/ng.asp?n=64305-conagra-listeria-recall> (29-11-06); "ConAgra's Meat Recall Conduct Faulted by Industry Analysts as Aloof, Fairly Emotionless and Unfeeling," The Agribusiness Examiner, October 8th 2002, <http://www.electricarrow.com/CARP/agbiz/196.htm> (29-11-06); "Allegations Made About Tainted Meat," The New York Times, August 31st 2001, <http://query.nytimes.com/gst/fullpage.html?sec=health&res=9902E2DD1330F932A0575BC0A9679C8B63&n=Top%2fReference%2fTimes%20Topics%2fSubjects%2fM%2fMeat> (29-11-06).

[201] Oxfam website, Oxfam Press Release, "Lid Comes Off French Farm Subsidies," November 7th 2005, <http://www.oxfam.org/en/news/pressreleases2005/pr051107_france_eu> (29-11-06).

[202] War on want, The EU Corporate Trade Agenda, The role and the interests of corporations and their lobby groups in Trade Policy-Making in the European Union *(*S2bnetwork, Brussels, November 2005*).*

particulates), water extraction and discharges (resource use, biodiversity, contamination, transformation), waste, odour and noise of operations, waste of packing materials and land take (soil, biodiversity).

The processed food sector is a major consumer of energy and likewise contributor to carbon emissions. In the UK, for example, this industry (including food service/catering) accounted for 11% of all industrial energy consumption and exhausted 7.9 million tons of carbon in 2002. Waste is a major issue in this sector, with packaging and food waste probably the most significant aspects. In the UK, the food industry generated approximately 8.6 million tonnes of solid waste in 1998/99, or 19% of total UK industrial waste. Of this waste, 44% is recycled and 37% is sent to landfill. Sales of packaging material to the UK food and drink industry amounted to 11 billion US dollars in 1997. While there is no direct correspondence in volume terms, the amount of packaging handled by the UK food industry increased by 41% between 2000 and 2003[203].

Actions damaging to the environment of which leading food processors have recently been accused and sometimes convicted include exhaustion of water resources near plants (for instance Danone[204] and Nestlé[205]), pollution via dumping of all kinds of untreated waste and chemicals (for instance Coca-cola[206], Kraft[207] and Cadbury[208]), failure to take mandatory steps to prevent emissions of ozone depleting refrigerant

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[203] DEFRA, Draft Food Industry Sustainability Strategy (ISS), April 2005, <http://www.defra.gov.uk/corporate/consult/fiss/draft-fiss.pdf#search=%22A%20draft%20Food%20Industry%20Sustainability%20Strategy%20%22> (28-11-06) p.78-79.

[204] Corporate Watch website, "Hydrating the G8," no date, <http://www.corporatewatch.org.uk/?lid=1510> (12-12-06).

[205] Baby Milk Action website, Press Release, "BBc Reports Damaging Environmental Impact of Nestle's Bottle Water Business," July 22nd 2005, http://www.babymilkaction.org/press/press22july05.html (29-11-06).

[206] See for instance: D. Teather, "Has Coke Become the New McDonald's?," The Guardian, August 18th 2006, http://business.guardian.co.uk/story/0,,1852635,00.html (29-11-06).

[207] US Environmental Protection Agency website, Region 1 New England, "Kraft Foods Resolves Two Environmental Cases by Agreeing to Pay Penalties and Perform Environmental Project At Woburn Mass. Facility," July 13th 2006, <http://yosemite.epa.gov/opa/admpress.nsf/1367c4195702d16a85257018004c771c/cbdd4628a16bff45852571aa006a790e!OpenDocument> (29-11-06).

[208] "Seven-up Taken Down: Bottler Pleads Guilty to 12 Counts of Water Pollution," Corporate Crime Reporter 44(4) (November 2005) <http://www.corporatecrimereporter.com/sevenup111005.htm> (29-11-06).

(Kraft[209]) and volatile organic compounds (Campbell[210]) and selling solid waste as fertilizer (Coca-cola)[211].

3.4. Economic and trade issues

There is little literature on purchasing practices in the food industry. The food industry, in particular coffee, chocolate and tea producing firms, have however been accused by NGOs of paying prices that are below the costs of production to producers while reaping great profits[212]. For instance, only about 10% of the retail price of ground coffee goes to cover the production costs, and for tea this is only about 8%[213]. The rest is captured downstream of the supply chain, and to a large extent by food processors.

Another important economic issue is **tax avoidance**. In order to attract foreign investment, (poor) countries compete with one another in offering the lowest taxes, tax breaks and special economic zones while for instance at the same time benefiting from taxpayer money in this country. Also a number of multinational food companies, such as PepsiCo, Bunge and Cadbury Schweppes PLC[214], are either incorporated in tax havens or have a large number of subsidiaries there. This means that they need not pay taxes or pay less tax in the countries in which their operations are concentrated. As an example for both of these tax avoidance issues, leading US food corporations paid only about 24% tax on their profits between 1996-98, while the effective corporate tax rate at that time was 35%[215].

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209 US Environmental Protection Agency website, Region 1 New England, "Kraft Foods Resolves Two Environmental Cases by Agreeing to Pay Penalties and Perform Environmental Project At Woburn Mass. Facility," July 13th 2006, <http://yosemite.epa.gov/opa/admpress.nsf/1367c4195702d16a85257018004c771c/cbdd4628a16bff45852571aa006a790e!OpenDocument> (29-11-06).

210 US Environmental Protection Agency website Region 9 News Releases, Campbell Soup to Pay $1,215,000 to Settle Environmental Violations," October 29th 1998, <http://yosemite.epa.gov/opa/admpress.nsf/016bcfb1deb9fecd85256aca005d74df/91bd3dcc0d7232a6852570d8005e12fa!OpenDocument> (29-11-06).

211 India Resource Centre website, Campaigns, Coca Cola, "Campaign to Hold Coca Cola Accountable," no date, <http://www.indiaresource.org/campaigns/coke/index.html> (29-11-06).

212 For instance: Make Trade Fair website, <http://www.maketradefair.com/en/index.php?file=13092002173102.htm> (01-08-06).

213 Somo, Profound, India Committee of the Netherlands, "Sustainabilitea", March 2006, p19.

214 Flex News website, Food Industry News, EU Courts Rule Cadbury Schweppes Tax Havens Mayu Be Legal," September 12th 2006, <http://www.flexnews.com/console/PageViewer.aspx?page=4722&str=Cadbury%20Schweppes> (29-11-06).

215 Institute on Taxation and Economic Policy website, "Study Finds Resurgence in Corporate Tax Avoidance", no date, <http://www.ctj.org/itep/corp00pr.htm> (29-11-06).

Box 10: How 5 companies operated a global price cartel on citric acid[216]

"In the period 1991-1995, US companies Archer Daniels Midland (ADM) and Haarmann & Reimer (H&R), Dutch company Cerestar Bioproducts B.V., and Swiss companies Hoffmann-La Roche and Jungbunzlauer (JBL), participated in a worldwide cartel through which they fixed the price and shared out the market for citric acid one of the most used additives in processed food.

The cartel pursued four main objectives: allocating sales quotas, fixing 'target' and 'floor' prices, exchanging specific customer information and eliminating or limiting price discounts. The companies met at technical level within the "Sherpa" meetings and at high or strategic level within the "Masters" meetings. A monitoring system to ensure compliance with the quotas was established, as well as a compensation scheme obliging any member that over-sold its allocated quota to provide compensation to the others. Concerted action was also taken against Chinese imports to regain some of the customers lost to the Chinese suppliers (the "Serbia list") through a concerted and targeted price war."

Obviously it is important that a company is managed properly - if not, this has a potentially negative effect on the livelihoods of its employees, their families and sometimes entire regions. Nevertheless, several leading food processing companies, such as Cirio[217], Parmalat[218], ConAgra[219] and Sara Lee[220] have been accused of fraud[221]. Another important issue is **price fixing**[222]. Leading processed food companies have been accused of all kinds of activities to keep prices for food items artificially high. Recent examples include price fixing schemes in the sales of citric acid[223] (see Box 10), corn syrup[224]

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[216] Source: European Commission, "European Court upholds fines for citric acid cartel", 28 September 2006, Press release 06/351, 27 September 2006, <http://www.foodnavigator-usa.com/news-by-product/news.asp?id=70889&idCat=72&k=european-court-upholds> (viewed 4 December 2006)

[217] "Update 1- Italian Magistrates Seek Mass Trial over Cirio," Reuters, December 12th 2005, <http://today.reuters.com/news/articlebusiness.aspx?type=consumerProducts&storyID=nL12159908&from=business> (29-11-06).

[218] M. Tran & A. Jay, "Parmalat: All You Need to Know About the Collapse of the Italian Dairy Giant," The Guardian, October 6th 2005, <http://business.guardian.co.uk/qandas/story/0,,1677296,00.html> (29-11-06).

[219] Corporate Predators website, "Top 100 Corporate Criminals of the Century," no date, <http://www.corporatepredators.org/top100.html> (29-11-06).

[220] "Sara Lee Exec's Implicated in Ahold Scandal," Food and Drink Europe, April 8th 2003, <http://www.foodanddrinkeurope.com/news/ng.asp?n=29637-sara-lee-exec> (29-11-06).

[221] "OECD Economic Surveys – Italy," Corporate Governance and Market Liberalisation: The Scope for Improvement, (November 2005) p.105(38).

[222] For instance see: "Cargill Settles Price-Fixing Lawsuit," Confectionary News, May 21st 2004, <http://confectionerynews.com/news/ng.asp?id=52270&n=wh22&ec=%23emailcode> (29-11-06) & P. Stiff, "Wrigley Fined for Price Fixing," 20th December 2005, <http://www.confectionerynews.com/news/ng.asp?id=64726-wrigley-fined-romania> (29-11-06).

[223] "EU Fines Price-Fixing Citric Acid Cartel," Food Navigator Europe, December 6th 2001, <http://www.foodnavigator.com/news/ng.asp?id=42459-eu-fines-price> (29-11-06).

(artificial sweetener companies involved included Cargill, Archer Daniels Midland) and very recently accusations of price-fixing cartels for beer in the EU[225] (among others Heineken, Inbev and Grolsch are accused). Interestingly in the corn syrup case the accusations were made by eighteen manufacturers of soft drinks, canned and baked goods, confectionary and dairy products, including Coca-Cola and Pepsi-Cola[226] (see also Chapter 5 for more information on these price fixing cartels and other controversial business tactics such as "predatory pricing").

3.5. CSR in the processed food sector

Many leading companies in the sector publish at least some information on how their practices affect the environment and society. In addition, many of these companies have implemented business principles, codes of conduct (COC) and other guidance documents that along with business integrity include principles on CSR. Some of the leading companies have schemes to monitor compliance with these principles in their branches and at suppliers. In this section we will not be focusing on the CSR policies of individual companies. Instead we will provide an overview of some of most well-known CSR initiatives and standards in the sector (sa8000, organic, fair trade, BSCI, ETI). We will also be focusing on - sometimes less well-known - CSR initiatives in which one or more of the major processed food companies is involved, or has at least signed up to. In this way we aim to provide some insight into how these companies are dealing with some of the CSR issues discussed above. For more information on some of these initiatives and a critical discussion of such CSR initiatives, see "Who reaps the fruit: Critical issues in the fresh fruit and vegetable chain" SOMO, June 2006, www.somo.nl.

3.5.1. Social (multi-sector) CSR initiatives

SA8000

SA 8000 is a worldwide multi-sector standard for monitoring and certifying labour standards. SA 8000 stands for 'Social Accountability 8000'. The standard was developed by Social Accountability International (SAI). It is intended primarily for producers and suppliers. Most SA8000 certified companies can be found in the textile and apparel sector. However in total, 44 facilities in the food industry are also SA8000 certified. Most of these facilities are based in Italy.

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224 "Cargill Settles Price-Fixing Lawsuit," Confectionary News, May 21st 2004, <http://confectionerynews.com/news/ng.asp?id=52270&n=wh22&ec=%23emailcode> (29-11-06).

225 "Heineken, Inbev Face EU Price-Fixing Charge," Food Production Daily Europe, September 9th 2005, <http://www.foodproductiondaily.com/news/ng.asp?n=62297-heineken-inbev-european-commission> (29-11-06).

226 Agribusiness Center, 'ADM reaches court settlement in high fructose corn syrup suit', 18 June 2004: <http://www.agribusinesscenter.org/interior.cfm?content=headlines&id=590> (viewed 4 December 2006); Archer Daniels Midland Company. 2005 Annual Report. p. 50: Note 15; K. Arasu, "Court OKs Cargill Price-Fixing Settlement", Reuters, 19 May 2004, <http://www.agobservatory.org/showFile.php?RefID=60073> (viewed 4 December 2006)

The SA 8000 is based on the Universal Declaration of Human Rights (UDHR) and fundamental labour conditions, augmented by a number of important ILO conventions regarding safety and health, working hours and a living wage. The SA 8000 system is arranged according to the ISO 9000 system that companies use for quality control. SAI trains and accredits audit agencies, which can then be hired by producers and suppliers to obtain SA 8000 certification. The audit costs are borne by the suppliers, as well as the costs for improvements to be made for certification. This is seen as a fundamental problem with the system, as the SA 8000 system does not require the company at the 'top' of the chain to enable their suppliers to make the additional changes, so the burden is placed on the suppliers and subcontractors. There is no mechanism within the system to guarantee contracts or prices that take into account sustainable production costs.

The normative framework of the SA 8000 is increasingly viewed as a basic standard in CSR initiatives when it comes to social standards, and very similar standards can be seen in other initiatives and model codes of conduct. It contains the fundamental ILO labour standards, augmented by stipulations on working hours, living wages, health and safety working conditions and job security.

The Ethical Trading Initiative (ETI)

The Ethical Trading Initiative (ETI) is an alliance of companies, NGOs and trade union organisations, at the objective of which is the identification and promotion of 'best practices' in the area of implementation of corporate codes of practice which cover supply chain labour conditions.

The goal of the ETI is to ensure that the labour conditions of employees producing goods for the UK market comply with international labour standards. The ETI mainly focuses on the implementation of labour standards in the supply chains of the participatory companies. Participatory companies commit themselves to the ETI's Base Code and the implementation of that code by their suppliers. This code is similar to the model code of the International Confederation of Free Trade Unions (ICFTU) and shows a strong resemblance to the SA 8000 standard. The ETI has pilot projects in various sectors including the food industry. ETI members include leading retailers in the UK such as Asda, Tesco, Sainsbury's and Marks and Spencer. Members from the food processing industry include Premier Foods and Associated British Foods. ETI also has developed guidelines on how to include smallholders in supply-chains.

BSCI

The Business Social Compliance Initiative (BSCI) is a European platform of retailers, industry and importing companies for monitoring and improving social standards in all supplier countries and for all consumer goods. Its membership is mostly made up of EU retailers, and some apparel companies. BSCI was designed for the textile industry, but retailers have adapted it so it can be implemented in the food sector (production). Roll out of this system has started in 2006. The current status of the initiative as regards implementation in the food sector is unknown[227]. The credibility of the initiative has been seriously challenged by NGOs, however, among other things for being business dominated, not having meaningful stakeholder involvement, not having independent verification of implementation and for not being transparent as regards audit results and suppliers[228].

EU Platform on Diet, Physical Activity and Health

The Platform was launched on March 15, 2005 and brings together a broad range of stakeholders, including the Confederation of Food and Drink Industries of the EU (CIAA), industry organisation of the large food processing companies that operate in Europe, the European Consumers Organisation (BEUC) and the European Commission[229]. The aim of the Platform is to reverse the current trend of increasing overweight and obesity in Europe, especially among children and adolescents. Its purpose is to provide a platform from which all interested actors can present and discuss their plans for action, and where the outcomes of performance are reviewed in order to be able to determine Best Practices. The Platform defines a number of points of action, including 1) consumer information, 2) education, 3) support for physical activity, 4) marketing and advertising and 5) the composition of foods, including the availability of healthy food options and smaller size portions.

The Commission has decided to highlight some of the outcomes of the EU platform by means of the following commitments:

- The 9 soft drinks companies in UNESDA who have committed not to advertise to children under 12 and have set up a system of independent consultants to monitor the implementation of this commitment;
- McDonald's for their commitment to providing nutritional information on packaging throughout Europe;
- Unilever for their commitment to reformulate products;
- Kraft for their commitment not to market certain products directly to children unless they meet a certain nutritional profile.

Declaration of Ethical Trading Values

The Food and Drink Federation (FDF), representing the food and drink manufacturing industry in the UK, has drafted a Declaration of Ethical Trading Values, as part of its Statement of Principles. All FDF members that support the Statement of Principles commit themselves to 1) comply with all environmental, social and economic legislation in the

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[227] Ahold website, Responsibility, "Ahold Sustainable Trade Development," no date, http://www.ahold.com/page/4213.aspx (29-11-06).

[228] See for instance: Clean Clothes Campaign, The Business Social Compliance Initiative (BSCI) A Critical Perspective, June 2005, http://www.cleanclothes.org/ftp/05-050bsci_paper.pdf#search=%22critique%20bsci%22 (29-11-06).

[229] EUROPA website, Rapid, Press Releases, "Questions and Answers on the EU Platform on Diet , Physical Activity and Health, and Its Commitments," November 9th 2006, http://europa.eu.int/rapid/pressReleasesAction.do?reference=MEMO/06/418&format=HTML&aged=0&language=EN&guiLanguage=en (29-11-06).

countries in which they operate, 2) work with customers, suppliers and other business partners in the food supply chain to encourage ethical trading standards and to seek continuous improvement, and 3) integrate ethical trading considerations, where practicable, into all aspects of their business. The Ethical Trading Value declaration includes statements on labour rights, health issues and fair remuneration. All the major food processing companies that are active in the UK are members of the FDF and have signed up to the Statement of Principles. Some of the commitments are not very specific or ambitious, for instance the commitment on fair remuneration reads “fair remuneration and benefits be provided, comparable to that offered by similar companies in the same region or country.”[230]

Fairtrade

The primary aim of fair trade is to improve the livelihood of marginalised producers in developing countries by developing more direct, equitable and long term trading relationships. Central to the fair trade concept is the notion of empowerment: smallholders and workers are required to organise and cooperate to strengthen their position in the trade chain. An important aspect of the fair trade system is the premise that fair trading practices are the key to improving the situation of producers. Therefore, buyers must pay a price that covers the costs of socially and ecologically sustainable production; pay a premium specifically for the social and economic development of the workers or small farmers; pre-finance the trade if necessary and aim for long-term contracts.

The Fairtrade Labelling Organisations International (FLO) is the international umbrella organisation for national Fairtrade initiatives. FLO sets the Fair Trade Standard and has certified over 800,000 producers in more than 40 countries. These certified producers are permitted to carry the ‘Fairtrade’ label. As is the case with organic products, the fair trade concept applies primarily to producers and not to processors. However FT premiums and FT minimum prices apply to some (semi-)processed products such as fruit juices. FLO is also currently developing a generic standard for Processed Products that deals with issues concerning the processing of basic FT agricultural commodities. According to FLO “the aim of this Standard for Processed Products (PP) is to explain how processing can be carried out in a way that is consistent with the aims of FLO and meets the expectations of all players in the supply chain, including the end consumer[231].” Estimated retail sales of Fairtrade products worldwide amounted to 1,5 billion US dollars in 2005, an 37% increase from 2004[232].

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[230] Food and Drink Federation website, “Declaration of Ethical Trading Values,” no date, http://www.fdf.org.uk/manifesto_7.aspx (29-11-06).
[231] Fair Trade, News Bulletin October 2006, http://www.fairtrade.net/uploads/media/News_Bulletin_October_2006_01.pdf (29-11-06).
[232] Fairtrade labelling Organizations International, Annual report 2005, p4

3.5.2. Environmental social (multi-sector) CSR initiatives

Organic

Organic production is a holistic management of the agro-ecosystem, emphasising biological processes and minimising the use of non-renewable resources. Its implications from a sustainability perspective apply primarily to agricultural production and its environmental impact. There are some requirements for food processors, however. These include preservation of the identity of organic ingredients through handling in the foods, a ban on food irradiation and restriction on the kinds of non-organic ingredients used, such as additives in the final product[233].

In organic farming, the use of chemical fertiliser and pesticides is prohibited. Other key elements of organic production include creating nutrient-rich, healthy soil that contains abundant organic matter, which helps to prevent erosion, retain water and control the release of nutrients to plants.

Although organic is still a niche sector, the organic foods industry has been growing at a rate of 20% to 24% annually worldwide and is outpacing the conventional food industry in terms of growth. Worldwide sales of $32 billion are projected by the year 2009[234].
The International Federation of Organic Agriculture Movements (IFOAM) has established private voluntary basic standards for organic production, while the FAO/WHO Codex Alimentarius Committee has adopted guidelines for the production, processing, marketing and labelling of organic foods. In the EU standards for organic production, products and inspection systems are laid down in regulations.

Sustainable Agriculture Initiative Platform

The Sustainable Agriculture Initiative Platform (SAI Platform) was created by the food industry to communicate worldwide about sustainable agriculture and support its development. Danone, Nestle and Unilever are its founding members, while Kraft, Sara Lee and Coca Cola are among the other members[235]. The SAI Platform's work consists of facilitating working groups composed of active member companies, and is aimed at developing sustainable agricultural practices. The SAI Platform's working groups' activities revolve around three main themes: 1) Development of documents: Mission Statement, Principles and Practices, and Indicators for sustainability 2) Stakeholder consultation and 3) Pilot testing and roll-out under the responsibility of companies. Each working group focuses on a different product category, such as palm-oil, coffee and cereals.

Case studies by various leading food companies have mainly focused on agricultural production and, to some extent, primary processing. Most of these case studies have

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233 FAIA website, Additives and Ingredients for Healthy Eating, "Organic Food," no date, http://www.faia.org.uk/organic.php (29-11-06).
234 RCNOS, World Organic Foods And Beverages Report (2006), Description, June 2006, http://www.rncos.com/Report/IM042.htm (29-11-06).
235 Sai website, "Members," no date, http://www.saiplatform.org/about-us/members/default.htm (29-11-06).

focused more on improving production from a product quality perspective (training in Good Agricultural Practices, GAP) and less on social and trade related issues. However, training of this kind can increase income for producers, because it improves their chances of inclusion in international trade and/or in the supply chains of these companies. Nevertheless, GAP is not about *minimising* environmental impact, as is the case in organic production, which can be considered more sustainable from an environmental perspective.

ISO14001 and EMAS

ISO 14001 is a standard aimed at creating and certifying environmental management systems (EMS). An EMS enables companies to control and decrease the environmental effects and risks of their activities. Among other things, this is cost reductive, as less water, energy and resources are used, and fines are avoided. In order to have their EMS certified by ISO, companies need to define an environmental policy in which they commit to a constant improvement of EMS, preventing pollution and abiding by local environmental laws. Also, environmental targets must be set and progress monitored in respect of them. Environmental organizations such as Greenpeace have criticized these norms because companies tend to use their ISO 14001 certification for their own publicity purposes, while they do not actually tackle the company's *environmental performance*. Being certified only means that a company has a functioning environmental management system. However, the environmental targets are set by the companies rather than by ISO, and can potentially be very unambitious. Even abiding by local environmental laws is no prerequisite for certification. Kraft, Danone, Unilever and Cadbury Schweppes are among the many companies which have ISO certified EMS.

The 'Eco Management and Audit Scheme'(EMAS) is an EU initiative that resembles the ISO 14001, but has the additional demand that companies publish a publicly available environmental report in order to be EMAS certified. It also demands an independent audit of the company's monitoring.

3.5.3. Social and environmental initiatives

UN Global Compact

The UN Global Compact is a CSR initiative applicable to all business sectors, expressed in 10 voluntary principles on human rights, labour rights, environment and anti-corruption. The initiative was initiated by Kofi Annan, UN's Secretary General in 1999, in an attempt to integrate social and environmental issues in business practices. It contains ten principles, rooted in key international instruments, such as the Universal Declaration of Human Rights, the ILO Declaration on Fundamental Principles and Rights at Work and the Rio Principles of Environment and Development. Food processing companies that are participating in the initiative include Nestle, Kraft, Danone, Unilever and Cadbury Schweppes. The initiative has been heavily criticized by civil society organisations because there is no screening of the companies joining the initiative, nor of the implementation of the principles by the companies that have joined.

World Business Council of Sustainable Development

The World Business Council for Sustainable Development (WBCSD) is a business initiative aimed at commitment to "sustainable development through economic growth, ecological balance and social progress[236]." Its 180 members are from more than 30 countries and 20 major industrial sectors. Leading food company members include PepsiCo, Coca Cola and Unilever. The Council also comprises a Regional Network of 54 national and regional partner organizations – called Business Councils for Sustainable Development (BCSDs) – mostly located in developing countries.
Goals of the council include being "a leading business advocate on sustainable development", "to develop and promote the business case for sustainable development" and "to demonstrate the business contribution to sustainable development and share best practices among members".

International Business Leaders Forum

The International Business Leaders Forum is an international not-for-profit organisation initiated by the Prince of Wales and a group of chief executives of international companies in 1990, in response to the emerging challenges of economic growth and change in the global economy. The forum's mission is to promote responsible business leadership and partnerships for social, economic and environmentally sustainable international development, particularly in new and emerging market economies. Food industry participants include Coca Cola, Inbev, Cadbury Schweppes, Kraft, Nestle, Pepsico and Unilever. Its activities include the HEAL Global Partnership to tackle lifestyle-caused illnesses and Human Rights and Conflicts.

3.5.4. Other initiatives

It is beyond of the scope of this report to provide an exhaustive list of CSR initiatives in the food industry. The programmes referred to above are some of the best known international multi-sectoral initiatives. However on a national sector level there are numerous initiatives that address issues such as obesity (for example, code of conduct on overweight of the Dutch Drink Industry Association (NFI)) and packing waste (for example the Sustainable Packaging Coalition in the US). There are also numerous initiatives at a subsectoral level, which mainly address CSR issues for commodities sectors such as palm oil (Roundtable on Sustainable Palm Oil), soy (Roundtable on Sustainable Soy), tea (Ethical Tea Partnership), cocoa (World Cocoa Foundation and International Cocoa Initiative) and coffee (Common Codes for the Coffee Community, Utz Kapeh, Rainforest Alliance).

[236] World Business Council for Sustainable Development, "About the WBCSD," no date, http://www.wbcsd.org/templates/TemplateWBCSD5/layout.asp?type=p&MenuId=NjA&doOpen=1&ClickMenu=LeftMenu (29-11-06).

3.6. Summary and conclusions

The above overview of CSR issues in the food processing industry shows that there are still are many problems that need to be addressed by the industry. Some of the most critical issues as regards the food processing industry include union freedom in countries that have a bad reputation regarding labour rights, equal opportunity and pay, increasing numbers of temporary (migrant) workers, the role of the industry in the obesity epidemic and its legal and illegal negative environmental impact. In the critical issue section, we focussed on the issues in which leading food companies are/were (allegedly) involved. It is therefore important to note that these issues involve the world's leading food companies, and are not simply problems that are caused by anonymous "bad guys", "laggards" among the industry population, or only SMEs. However in a number of cases these companies denied allegations.

In the section on CSR initiatives, we took a closer look at how industry leaders are dealing with some of these critical issues. The focus was on some of the major initiatives involving many companies, and sometimes other stakeholders, such as governments and CSOs. It is beyond the scope of this research to look at actual implementation or the effects of these initiatives on sustainable development and poverty eradication. However some trends can be identified in the ways the industry is dealing with CSR issues.

There are many CSR initiatives in this industry. And while we have not looked at CSR in individual companies, from researchers' experience it is known that many leading companies address issues raised actively and passively by means of communications through the media, CSR reports, websites and of course various codes of conduct and business principles. In this respect, the food industry is certainly one of the leading sectors when it comes to CSR. A likely explanation is that because food is a necessity, and therefore everybody is to some extent interested in food. This concern could increase the likelihood that people will also be interested in production conditions. In addition the industry is relatively close to consumers in the sense that is often only one link away (retailer) from consumers, and that ready-to-eat processed foods are often branded products. These factors make brands, products and companies vulnerable to reputation damage. And leading companies are therefore eager to "manage" CSR issues, as these might directly affect sales. These same factors are true, to a large extent, for another leading sector - the clothing industry.

One trend that can be identified on the basis of the overview in this chapter is the fact that there are a number of leading companies in the food industry, such as Unilever, Danone and Coca Cola, which are active in various initiatives at the same time. On the other hand, the same companies are involved much less - or not at all - in initiatives that are viewed as more credible by CSOs such as organic, FairTrade and to a lesser extend SA8000 and ETI, generally preferring more mainstream initiatives such as Global Compact, SAI platform, World Business Council of Sustainable Development. The former initiatives might be still too marginal or ill-adapted to the scale of leading processors in this industry. Another reason for this non-involvement could be the fact that it is more strategic to address critical issues in a less strict and binding fashion, such as through Global compact commitments and/or working on case studies that serve as pilots but are not (yet) scaled up to encompass the whole of their production (SAI platform). It should be noted, however, that by virtue of acquisitions, some leading companies such as Unilever (Ben and Jerry's organic) and Cadbury's (Green & Black's, organic (Fair Trade) chocolate) have tapped into these niche markets (for a critical discussion, see chapter 2). Another interesting finding is that most initiatives in the overview focus on CSR issues in *production* and not on (*higher) processing* in the supply chain. This finding is not very remarkable, however; as mentioned in the introduction there are many issues in the agricultural sector, the industry's supplier, that need to be addressed properly. "Downstream issues" that *are* addressed specifically in multi-company initiatives are most notably obesity and packing issues.

Chapter 4
Selected items on regulations, trade and investment

This chapter deals with some trade and investment related governmental measures that affect the processed food sector of developing countries. The items are selected on the basis of being considered major trade obstacles for developing countries, such as tariff escalation and standards, or because they receive (too) little attention in the literature, policy making and public debates, such as the lobbying by the processed food industry. Some relevant issues have been dealt with extensively in the SOMO report on critical issues in the fresh fruit and vegetable sector, to which we refer.[237] By raising critical issues in the trade and investment regimes and by assessing the possibilities, or lack of them, offered by governmental measures to solve the problems identified in previous chapters, this chapter exposes the challenges of an export orientation in the current competitive trade and investment climate.

This chapter will not be examining in detail the problems faced by many developing countries, and particularly the least developed countries, which prevent their companies from taking advantage of the trading opportunities in processed agricultural products. Such problems relate to a lack of financial resources and internal production and supply constraints, such as insufficient storage and transportation facilities, lack of technology, lack of entrepreneurship and business experience, an inadequate legal and regulatory framework, economic policies that are biased against agriculture, structural adjustment programmes pushed by the IMF and World Bank to move from import substitution to trade and investment liberalisation and export orientation.

4.1. Trade rules and negotiations influence export capacities of developing countries

Traditionally, high tariffs have been criticised for forming major impediments to processed food exports by developing countries because they make these imports more expensive and less competitive in the importing country. However, there are also other measures and regulations that make such exporting difficult and that are dealt with by the international trade regime, namely safeguard mechanisms against imports as well as food safety and technical standards, as is explained below.

[237] M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 125-127.

4.1.1. WTO and prohibitive tariffs on processed food

In 1995, the World Trade Organisation (WTO) replaced the General Agreement on Tariffs and Trade (GATT), which had only weak rules on agricultural trade[238], and the WTO Agreement on Agriculture came into effect. The new Agreement on Agriculture was painstakingly negotiated in the Uruguay Round of negotiations (1986-1994) and reduced tariffs on primary and processed agricultural products, but not as much as for industrial products. Developed countries agreed to reduce their agricultural tariffs in 6 year by a total of 36% with a minimum of 15% for each product while developing countries needed to reduce their tariffs by a total of 24%, with a minimum of 10% per product, over a longer period (10 years). Least developed countries did not have to make reduction commitments.[239] However, the formula left many opportunities for developed countries to limit tariff reductions on all kind of agricultural products which they considered sensitive, i.e. which would affect their agriculture or agriculture-based industries. Major problems for developing countries' exports and imports resulting from the Agreement on Agriculture have been explained in SOMO's report on fresh fruit and vegetables[240]; they include complex tariffs, tariff-rate quotas and variable levies, which also seem to affect processed food products.[241] The particular problems of high tariffs and tariff escalation for processed food exported from developing countries are discussed below.

Tariff peaks on processed food

Not only do tariffs vary considerably according to the product and between countries, there are still many high tariffs applied to primary processed and fully processed agricultural products. When tariffs are higher than 12% or 15% they are called tariff peaks (or tariff spikes) because they are above three times the average tariff level in industrial countries. Some high tariffs are difficult to calculate, because of additional complex tariff systems[242] applied by developed countries in particular (see also below: safeguard measures).

Tariff peaks are being applied by developing countries as well as developed countries, even taking into account the special lower tariffs developed countries apply to developing countries (see below: GSP). The (semi-) processed food and drink products on which EU, US, Japan have applied tariff peaks (including tariffs in excess of 100%) cover milk

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[238] WTO, Market access: unfinished business – Post Uruguay Round inventory and issues, WTO Special Studies, no. 6, [2000], <http://www.wto.org/English/res_e/booksp_e/special_study_6_e.pdf> (viewed on 18 November 2006)

[239] The reduction was calculated from the already bound rates, for unbound tariffs those applied in the year 1986, for over-quota duties introduced after tariffication, the base was the level of protection provided by the non-tariff barriers during 1986-88: see A. Regmi, M. Gehlhar, J. Waino, T. Vollrath, P. Johnston, and N. Kathuria, Market Access for High-Value Foods, USDA Agricultural Economic Report, no. 840, February 2005, p. 4.

[240] M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, chapter 6, p 129-139.

[241] More research about these complex tariffs related to processed food was beyond the scope of this report.

[242] Non-advalorem tariffs, tariff quota rates, etc.

products, cereal and sugar-based products, fruit preparations and (canned) fruit juices, other preserved fruit and vegetables, peanut butter, margarine, coffee, chocolate and sugar confectionary.[243]

Tariff escalation prevents more exports of processed food and drinks

A particular negative effect on developing countries' attempts to move from exports of raw agricultural products to exports of processed commodities and food or drinks comes from the rise of tariffs as the level of processing increases, called tariff escalation. A typical example is that, in many developed countries, the tariffs are higher on cocoa butter and even higher on chocolate than on cocoa beans (see Table 13).

Tariff escalation for developing countries' processed products is not as easy to calculate[244] as many studies seem to show, because of widely different terms of country and commodity coverage, methods of calculating tariffs, definition of processed food, etc. For example, the tariffs applied in practice by the developed countries are often lower than the maximum "bound" tariffs to which they agreed in the WTO Agreement on Agriculture, especially when the provide trade preferences.
Nevertheless, the many varied studies[245] that have assessed the level of tariff escalation after the Uruguay Round negotiations concluded that tariff escalation is persisting in a large number of commodity chains in both developed and developing countries. All OECD countries have cut their (bound) tariffs less for fully processed products than for semi-processed or bulk commodities.[246] In developing countries, tariff escalation is lower, and sometimes much lower when looking at the rates actually applied rather than the bound rates.[247]

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243 UNCTAD/WTO, "The post-Uruguay Round tariff environment for developing country exports: tariff peaks and tariff escalation", 28 January 2000 (UNCTAD document: TD/B/COM.1/14/Rev.1), < http://www.unctad.org/en/docs/c1d14r1.en.pdf>, (viewed on 18 November 2006), p. 6.

244 Many processed products include different commodity ingredients, which makes it difficult to calculate the tariff escalation; these are not included in the research studies (for example, cake that contains processed soybeans and wheat, sugar, fats and oils.) Many studies have been undertaken while the tariff reduction commitment under the Uruguay Round Agreement on Agriculture - 2000 for developed countries and 2004 for developing countries – had not yet been fully implemented. Studies for 2005 were not yet readily available.

245 N. Elamin, H. Khaira, "Tariff escalation in agricultural commodity markets", Commodity market review 2003-2004, FAO, 2003, <http://www.fao.org/docrep/006/Y5117E/y5117e0e.htm> (viewed 17 November 2006); A. Regmi, M. Gehlhar, J. Waino, T. Vollrath, P. Johnston, and N. Kathuria, Market Access for High-Value Foods, USDA Agricultural Economic Report, no. 840, February 2005, < http://www.ers.usda.gov/publications/aer840/> (viewed 19 November 2006); UNCTAD/WTO, "The post-Uruguay Round tariff environment for developing country exports: tariff peaks and tariff escalation", 28 January 2000 (UNCTAD document: TD/B/COM.1/14/Rev.1), < http://www.unctad.org/en/docs/c1d14r1.en.pdf>, (viewed 18 November 2006); WTO, Market access: unfinished business – Post Uruguay Round inventory and issues, WTO Special Studies, no. 6, [2000], p. 51-< http://www.wto.org/English/res_e/booksp_e/special_study_6_e.pdf> (viewed on 18 November 2006)

246 A. Regmi, M. Gehlhar, J. Waino, T. Vollrath, P. Johnston, and N. Kathuria, Market Access for High-Value Foods, USDA Agricultural Economic Report, no. 840, February 2005, p. 4, , < http://www.ers.usda.gov/publications/aer840/> (viewed 19 November 2006)

247 See for instance: WTO, Market access: unfinished business – Post Uruguay Round inventory and

Tariff escalation has been found[248] in processed food products such as vegetable oils, meat products, sugar products, fruit and cereal products, and tea. Tariff escalation in developed countries is particularly high for processed tropical commodities, coffee and cocoa (average chocolate tariffs can increase up to 57%: see Table 13). In parallel, the participation of developing countries in world trade (2000-2002) in cocoa beans was 96%, while in chocolate this was 8%; similarly for coffee, developing countries traded 96% in non-roasted coffee beans, 9% in roasted coffee and 41% in coffee mixtures and extracts.

Table 13: Tariff escalation in selected countries

Processing chain	Average tariffs (%)				
Cocoa	**Australia**	**Canada**	**EU**	**Japan**	**U.S.**
Cocoa beans	1	0	0	0	0
Cocoa paste	0	0	10	8	0
Cocoa butter	0	0	8	0	0
Cocoa powder	9	6	27	19	16
Chocolate and products	17	57	18	21	15

Source: amber waves [see also: A. Regmi, M. Gehlhar, J. Waino, T. Vollrath, P. Johnston, and N. Kathuria, Market Access for High-Value Foods, USDA Agricultural Economic Report, no 840, February 2005, p. 8 : add percentages of trade ; add coffee and sugar]

→ Critical issues

All studies identify tariff escalation as an important factor contributing to impediments for these countries to move up the processing scale and add value to their exports, including on commodities that they can grow in their countries. As many countries struggle with basic commodity dependence with low prices, environmental destruction from monoculture and over-exploitation, it is seen as important that hindrances to developing countries diversifying their exports are removed so that they can take their share of world trade in higher value-added food products as much as developed countries do. However, as this report explains, it is important that such an increase in processed food and drinks exports is achieved by companies who apply sustainable and equitable principles and by domestic enterprises so that value added remains in the country and contributes to poverty eradication, without destroying the environment.
Developing countries often use tariff peaks and tariff escalation to protect their processed food industry that is not yet ready for competition from cheap imports, to promote the development of a processed industry or for revenue-raising reasons. Article XVIII of GATT 1947 recognizes the need of developing countries

issues, WTO Special Studies, no. 6, [2000], p. 51-< http://www.wto.org/English/res_e/booksp_e/special_study_6_e.pdf> (viewed on 18 November 2006)

[248] Amongst others by N. Elamin, H. Khaira, “Tariff escalation in agricultural commodity markets”, Commodity market review 2003-2004, FAO, 2003, <http://www.fao.org/docrep/006/Y5117E/y5117e0e.htm> (viewed on 17 November 2006); A. Regmi, M. Gehlhar, J. Waino, T. Vollrath, P. Johnston, and N. Kathuria, Market Access for High-Value Foods, USDA Agricultural Economic Report, no. 840, February 2005, < http://www.ers.usda.gov/publications/aer840/> (viewed 19 November 2006)

to grant tariff protection required for the support of their infant industries.[249] While some argue that protection leads to inefficient and more expensive products, others point to the de-industrialisation which has occurred since the World Bank and IMF structural Adjustment programme of rapid tariff reductions. Given the increasing trend whereby food multinationals use mergers and acquisitions to enter developing country markets and export to neighbouring countries with low tariffs, more ‘efficiency’ might result in fewer local and small or medium-sized enterprises that can enter or remain in the domestic and neighbouring markets.

Preferential access for developing countries’ products

Many developed countries apply lower tariffs to developing countries because there are several policy instruments lowering tariffs for the latter.

The general system of preferences (GSP)

Under the general system of preferences (GSP), developed countries grant lower tariff access to the developing countries, and even better access for the least developed countries. Contrary to the WTO principle of reciprocity, the WTO allows developing countries not to grant similar increased market openings to rich countries (non-reciprocity). However, the improved access offered under the GSP is much less in the agricultural sector than for industrial goods. As a consequence, a relatively large number of tariff peaks and tariff escalation have long existed in major developed countries, even for the least developed countries, on processed food products such as fruit juices and sugar products.[250]

Better access to the EU for some developing countries: ACP, Cotonou, EPAs and EBAs

The EU has been giving special improved (‘preferential’) access to imports from 78 Sub-Saharan African, Caribbean and Pacific (ACP) developing countries under the Lomé Conventions. While all ACP imports were duty free in principle, some agricultural products remained restricted (by quotas, for example) and some processed food and drink products retained higher tariffs.[251] The EU assigned better prices for ACP imports of sugar, while the EU subsidised its own exports of sugar, an important ingredient for exports of processed foods.

However, preferences given to the ACP and not to other developing countries are incompatible with WTO rules, and this EU trade regime has been attacked by WTO

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[249] Footnote by N. Elamin, H. Khaira, “Tariff escalation in agricultural commodity markets”, Commodity market review 2003-2004, FAO, 2003, <http://www.fao.org/docrep/006/Y5117E/y5117e0e.htm> (viewed on 17 November 2006)

[250] UNCTAD/WTO, “The post-Uruguay Round tariff environment for developing country exports: tariff peaks and tariff escalation”, 28 January 2000 (UNCTAD document: TD/B/COM.1/14/Rev.1), p. 8, < http://www.unctad.org/en/docs/c1d14r1.en.pdf>, (viewed on 18 November 2006): some of the higher tariffs start to apply when imports raise above a certain level (tariff quota’s).

[251] UNCTAD/WTO, “The post-Uruguay Round tariff environment for developing country exports: tariff peaks and tariff escalation”, 28 January 2000 (UNCTAD document: TD/B/COM.1/14/Rev.1), p. 8, < http://www.unctad.org/en/docs/c1d14r1.en.pdf>, (viewed on 18 November 2006)

members under the dispute settlement system. The EU and the ACP have therefore received – at a high price - a WTO waiver that allows the Lomé preferential trade regime to exist until 2008. After the new Cotonou agreement[252] on aid, trade and politics replaced the Lomé Convention, the ACP and the EU have since 2002 started to negotiate free trade agreements (FTAs) called Economic Partnership Agreements between the EU and 6 ACP regions (4 EPAs in Africa, 1 in the Caribbean and 1 in the Pacific). The WTO Art. XX requires far-reaching liberalisation of trade on a reciprocal basis in FTAs[253], which means that the ACP also have to reduce their tariffs substantially over time – which could leave their processed food and drink sector more exposed to European imports, without much progress being made on cutting distorting EU subsidies. The highly commodity-dependent ACP fear that they will lose export opportunities for their processed goods after other - more competitive - developing countries receive equal access to the EU. Given the growing resistance by ACP governments and societies to such 'preference erosion' and a full free-trade regime that would allow EU goods to flood their markets, it remains to be seen whether a new trade regime will be in place by 2008 as planned.

At the same time, the EU has been granting all least developed countries the same preferential access as the ACP countries (the "Everything But Arms" measure or EBA). Least developed ACP countries will receive such treatment after 2007. Since new WTO negotiations started in 2000, the EU has been pushing other developed, and major developing, countries to also offer EBA concessions to all least developed countries, but so far without success.

→ Critical issues

Notwithstanding the privileged trade access, many ACP countries did not diversify much into more processed forms of exports; least developed countries exports in processed food even decreased (see Chapter 1). While a few export opportunities might have been taken, the poorest countries were not always given generous preferential access schemes for (processed) products that are of most interest to them. Also, preferences' were mitigated by often complex non-transparent rules, e.g. rules of origin for mixed processed or industrial products, and various exemptions whereby preferences stop when exports reach a certain threshold level.[254]

The lack of progress by least developed countries in exporting more processed food indicates that simply granting improved market access will not lead to much success in this very competitive business climate (see Chapter 2). Other policies and support are needed, along with technical assistance, financing of infrastructure, etc. This questions to what extent global free trade agreements are

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[252] Was signed in 2000 and came officially into force in April 2003

[253] Liberalisation of up to 90% of trade, for which the ACP might have a longer period (up to 15 or perhaps 20 years) than the EU: for further explanation, see for instance: http://www.epawatch.net/general/start.php

[254] IMF/World Bank. Market Access for Developing Countries' Exports, April 27, 2001, <http://www.wSorldbank.org/economics/marketaccess.pdf> (viewed 17 November 2006)

sufficiently supportive of least developed countries even if they receive special and differential treatment.

Regional trade blocs

The formation of trade blocs among countries in the same region has in the last decade increasingly involved developing countries on all continents, between one another or with richer countries. According to basic WTO rules (Art. XX of GATT 1947) these regional and bilateral FTAs need to liberalise "substantially" all trade, mostly interpreted as 90% of trade, without having to reduce subsidies. This means that developed and developing countries which have signed FTAs get better tariff cuts than those who have only signed WTO agreements. There is currently a race under way to sign more and more bilateral or regional free trade agreements, especially by the US and the EU, but also amongst the more advanced developing countries. Trade agreements among developing countries, however, have some leeway and do not need to open up markets as much.

While these FTAs can challenge local processed manufacturing enterprises with cheaper imports from the region or further away, they also provide opportunities for foreign food companies to invest in production in one country and trade its products around the region. Such considerations of regional markets are claimed[255] to be an important consideration by foreign investors and match the strategies of food companies such as Unilever (see Box 6 in Chapter 2).

Safeguard measures or "trade remedy measures": protection measures against harmful imports

Apart from trade liberalization, the WTO and other trade agreements include numerous instruments other than tariff measures that allow countries to protect their domestic industries or agriculture. These special mechanisms are also applied to processed food products. They are hindering the exports of processed food by developing countries, but such impediments are harder to quantify than tariff protection. However, most of these safeguard measures can also be used by developing countries to protect their own food and drink processing industry or farming community. In short they can be explained as follows.

Anti-dumping duties: a country is allowed to impose higher duties to restrict imports that enter at unfair prices, i.e. when the prices of the imported goods are esteemed to be under the production price or to be below the price of consumption in the exporting country.

Countervailing duties: a country can impose higher duties to restrict imports of products whose production or exports have been subsidized by government.

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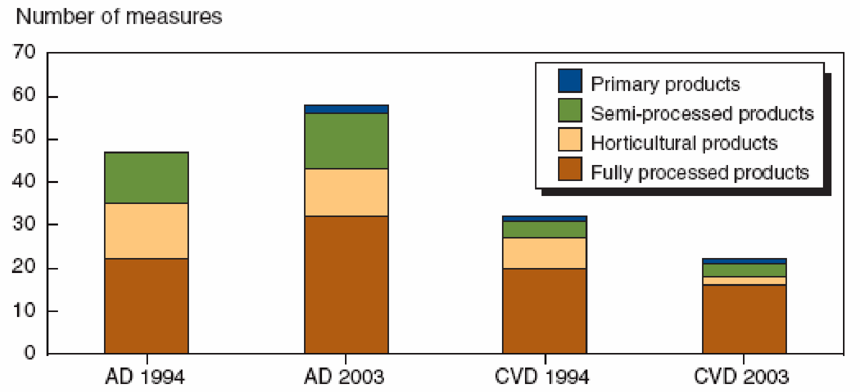
[255] For instance by the chief EU negotiator on EPAs: see M. Vander Stichele, EPA negotiations do not promote the right investment policies in Africa, SOMO Briefing paper, September 2006 <www.somo.nl>; see also: Wilkinson, The food processing industry, globalization and developing countries, electronic Journal of Agricultural and Development Economics, Vol. 1, No. 2, 2004, p. 192-193.

Available data[256] for 1994, 2002 and 2003 show that most of the anti-dumping and countervailing duties in agriculture have been taken on fully processed food and beverages, namely 55% of the agricultural antidumping measures in 2003 and 73% of the total countervailing duties on agriculture in 2003.[257] The products affected by these measures since 1994 have been: cheeses, meats (including canned ham and luncheon meats), refined sugar, canned fruits (e.g. pineapples and peaches), bottled olive oil, brandy, pasta, concentrated apple and pineapple juice, and prepared baby foods.[258]

In a –still incomplete- attempt to minimize protectionist abuses, the WTO has laid down procedures how to calculate the duties can be imposed, when the duties can be imposed, and for how long duties can be imposed, namely for no longer than 5 years. The WTO disciplines can be found, amongst other places, in the WTO Agreement on Implementation of Article VI of GATT 1994, and the WTO Agreement on Subsidies and Countervailing measures.

Figure 11: Unfair trade measures in place on Dec. 31, 1994 and 2003



Source: A. Regmi, M. Gehlhar, J. Waino, T. Vollrath, P. Johnston, and N. Kathuria, Market Access for High-Value Foods, USDA Agricultural Economic Report, no 840, February 2005, p. 13, < http://www.ers.usda.gov/publications/aer840/> (viewed 19 November 2006)

Emergency safeguard measures: A WTO member country can suspend its WTO liberalization commitments in trade in goods when a product is imported in "such increased quantities or in such conditions as to cause or threaten serious injury to domestic producers". Art. XIX of GATT 1947 and the WTO Agreement on Safeguards stipulate how such trade restrictions can be taken, and sets the total duration of such provisional measures at 8 years.

256 A. Regmi, M. Gehlhar, "Processed food trade pressured by evolving global supply chains", Amber waves (Economic research service USDA), Volume 3, issue 1, February 2006, p. 19; A. Regmi, M. Gehlhar, J. Waino, T. Vollrath, P. Johnston, and N. Kathuria, Market Access for High-Value Foods, USDA Agricultural Economic Report, no. 840, February 2005, < http://www.ers.usda.gov/publications/aer840/> (viewed 19 November 2006)

257 A. Regmi, M. Gehlhar, J. Waino, T. Vollrath, P. Johnston, and N. Kathuria, Market Access for High-Value Foods, USDA Agricultural Economic Report, no. 840, February 2005, p. 13-15, < http://www.ers.usda.gov/publications/aer840/> (viewed 19 November 2006)

258 Ibid.

Emergency safeguard measures have been predominantly used on processed food products while bulk commodities were hardly affected by the measure between 1995 and end of 2003.[259] (Semi-) processed products that were subject to safeguard measures were wheat flour, vegetable oils, liquid or powdered milk and fructose or glucose.

→ Critical issues

Developing countries have been suffering a lot from dumping and other unfair trade practices in their markets by some processed products, resulting from the (export) subsidies of developed countries.
For the developing countries and their domestic producers, the WTO procedures for applying the WTO measures to protect themselves against unfair imports are often too cumbersome and costly, and not all producers are aware of them. Moreover, when countries restrict trade according to these WTO rules, they can be challenged by the exporting country, which again is also a costly and cumbersome procedure for some developing countries.
Moreover, during the Uruguay Round negotiations on agriculture, from which developing countries were partly excluded in practice, the developed countries managed to impose a "peace clause" by which WTO members were not allowed to impose, countervailing duties on domestic support subsidies and some export subsidies that were in conformity with the Agreement of Agriculture until after end of 2003, even if they caused harm. This was stipulated in Art. XIII of the WTO Agreement on Agriculture, and also applies to processed food.

The WTO rules do not allow anti-dumping or safeguard mechanisms to be used to restrict trade on products which have been produced in way that breaches social and labour laws or damages the environment, also called social or environmental dumping.

Special Safeguard Measures: The WTO Agreement on Agriculture has introduced a "special safeguard" measure for countries which might be harmed by too many or excessively cheap imports after they converted all non-tariff measures into tariffs (" tariffication"). Art. V of the Agreement on Agriculture defines how this complex special safeguard can be used.

Until October 2004, almost two-thirds of these measures were taken on processed foods and beverages such as cocoa preparations and chocolate, dairy products and sugar & confectionary.[260]

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[259] A. Regmi, M. Gehlhar, "Processed food trade pressured by evolving global supply chains", Amber waves (Economic research service USDA), Volume 3, issue 1, February 2006, p. 19.

[260] Regmi, M. Gehlhar, J. Waino, T. Vollrath, P. Johnston, and N. Kathuria, Market Access for High-Value Foods, USDA Agricultural Economic Report, no. 840, February 2005, p. 16, < http://www.ers.usda.gov/publications/aer840/> (viewed 19 November 2006); see also WTO, Market access: unfinished business – Post Uruguay Round inventory and issues, WTO Special Studies, no. 6, [2000], < http://www.wto.org/English/res_e/booksp_e/special_study_6_e.pdf> (viewed on 18 November 2006), p.82,83: Appendix Table III.11. A. and B.

→ Critical issue

This special safeguard measure can only be applied by those who have undertaken the tariffication and who have indicated that they wanted to use this special measure. Many developing countries failed to reserve the right to use this safeguard measure or have chosen a formula other than tariffication. This gives developed countries, and in particular the US and the EU, an unbalanced advantage in using safeguard measures, which are useful for protecting their processed food and drink industry.

WTO rules have permitted some agricultural subsidies on processed food

Export subsidies

Although Art. XVI of GATT 1947 (paragr. 4) has since 1958 prohibited any export subsidies on any processed product which would result in dumping, subsidies on processed exports are being used. So while export subsidies were allowed to a certain extent on primary agricultural products, export subsidies were also given to processed products which incorporated primary agriculture inputs, for example for sugar, cereals and eggs incorporated in exported biscuits, chocolate and spirits. The Uruguay Round has legalized this practice for some major developed countries, but after the expiry of the Peace Clause from 2004 onwards, the legality may be challenged.[261]

The EU has been a main user[262] of export subsidies to its processed food and drink industry (that calls them export 'refunds') for the sugar, cereals, egg and milk products contained in the exported processed[263]. Apart from the high tariffs that protect the European food and drink industry, the latter considers these export refunds as compensation for the higher costs they incur in sourcing agricultural products (more than 70% of EU output of agricultural raw materials[264]) in the EU where prices are higher because of the EU's Common Agricultural Policy (CAP) which would make them uncompetitive on world markets. Between 1995-96 and 2000-2003, the EU spent 12% of its overall export subsidies on incorporated agricultural products, i.e. paid them to food and drink processors. Notwithstanding the many reforms of the CAP up to 2006, including on sugar, to reduce subsidies and unfair trade practices, some level of export subsidies on processed food with incorporated primary agricultural products remains, especially for sugar and dairy ingredients.

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[261] A. Swinbank, "The EU's export refunds on processed foods: legitimate in the WTO?", The Estey Centre Journal of International Law and Trade Policy, Vol. 7, No. 2, 2006, p. 152-167.

[262] Idem, p. 152-160.

[263] "EU to cut processed farm product export subsidies", Food & Drink Weekly, 2 August 1999, http://www.findarticles.com/p/articles/mi_m0EUY/is_30_5/ai_55361196 (viewed on 12 November 2006); for more details on which companies receive export subsidies see amongst others: M. Wiggerthale, What's wrong with EU agricultural subsidies?, paper, July 2005, <http://www.attac.de/agrarnetz/dokumente/marita_eusubsidies.pdf> (viewed on 22 November 2006)

[264] CIAA's main concerns as regards the launch of the next WTO round and negotiations on agriculture, document TCO 044/01 E-Final, <http://www.federalimentare.it/documenti/TCO-044.htm> (viewed on 22 November 2006)

The US subsidisation of export credits and food aid also covers some processed food. Some of the leading agribusinesses such as ADM have also received US subsidies that account for an important part of their income.[265]

→ Critical issues

Not all WTO members have received the right under the Agreement on Agriculture to subsidize processed products. This leads to unequal competition between processed products from the EU and other developed countries, and those of developing countries, on world markets, and also on the domestic markets of developing countries which import the subsidized foods and drinks.

Domestic support subsidies

While most of the domestic support subsidies in the developed countries go to farmers, and mostly to the very large farmers,[266] some of these subsidies have been going to the processing business. In the EU, food and drink companies, including large food multinationals that were processing agricultural products such as sugar, dairy and cereals have received subsidies as compensation for sourcing ingredients from the EU. The CAP reforms have reduced a fair number of these subsidies, but the complexity of the matter and the lack of transparency about who receives the subsidies does not allow a very clear picture to be formed of how much of this domestic support for 'conversion' is still provided.[267]

An overview in the Netherlands[268] makes clear that some large food companies such as Mars, Heineken, Bavaria, Philip Morris (now part of Altria) and Shell Chemie have received millions of Euro's of both export subsidies and some domestic support subsidies.[269] However, the lack of clear public data makes it difficult to quantify how much exactly each multinational receives.

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[265] http://en.wikipedia.org/wiki/Archer_Daniels_Midland

[266] For more details in the UK and the US, see for instance: http://www.oxfam.org.uk/what_we_do/issues/trade/downloads/bp55_subsidies.pdf; and < http://www.ewg.org/farm/> (viewed 22 November 2006)

[267] See for instance for a detailed analysis about the multinationals receiving EU subsidies in the Netherlands: "landbouwsubsidies in Nederland", analytical paper by the Evert Vermeer Stichting, November 2005, <http://www.evertvermeer.nl/renderer.do/menuId/237907/clearState/true/sf/237966/returnPage/237966/itemId/75109/realItemId/75109/pageId/237965/instanceId/238046/>

[268] Multinationals, smaller companies and big farmers who received EU domestic support and export subsidies can be viewed at : http://www.ewg.org/sites/netherlandsfarmsubsidies/index.php, and http://www.evertvermeerstichting.nl/download.do/id/100226248/cd/true/; http://www.evertvermeer.nl/renderer.do/menuId/237907/clearState/true/sf/237966/returnPage/237966/itemId/75109/realItemId/75109/pageId/237965/instanceId/238046/

[269] Evert Vermeer stichting, "Landbouwsubsidies op internet snel te doorzoeken", press communiqué, Amsterdam, 28 September 2005.

4.1.2. Neglected aspects of WTO negotiations in agriculture

Since 2000, WTO members have been negotiating to further liberalise trade in all agricultural products. A great deal of attention has been paid to reducing all access barriers, and cutting export and domestic support subsidies.[270] The very difficult negotiations, that are part of the Doha Round, stalled in July 2006 because of the lack of progress made. The US, in particular, was put in the spotlight for not sufficiently reducing its subsidies, but the EU has also been slow in offering market openings as requested by many WTO members. Developing countries had to resist pressure to make severe cuts in their tariffs and eliminate measures that would protect the development role of their vulnerable agricultural sectors.

The developed countries such as the EU, US and Japan are not only basing their negotiation positions on the interests of their farmers, but also on the interests of their (primary) food and drink processing industry. The EU, for instance, has fewer primary processing agribusinesses dominating export markets than the US where Cargill, Bunge and ADM are headquartered (see chapter 2). A close analysis[271] shows that the EU negotiators have been keen to listen to the position of the lobby of its food and drink industry, represented amongst others by the Confederation of the Food and Drink Industries in the EU (CIAA) which represents 25 national federations, 32 EU food and drink sector associations and 22 major food and drink companies grouped in a Liaison Committee that is made up of a majority of US food companies such as Cargill, Kelloggs and Coca Cola operating in the EU.[272]
The interests of the food and drink industry have been taken into account in the EU's position, and consequently been the subject of negotiations in the Doha Round, as follows:

(a) "*Real improvements in market access opportunities for EU food and drink industry products*"[273]*:* Since the food and drink market is saturated in Europe, the industry's production in Europe can only stay and grow by having more access to foreign markets, especially in the emerging market countries where more profits can be made (see chapter 2). This strategy has been reflected in the EU's position and consequently in the Doha Round negotiations as follows:

- - A **formula that cuts all tariffs** has been the basis of the latest negotiations, as proposed by the EU but contrary to tariff cuts on specific products as first requested by developing countries to allow protection of their sensitive products

[270] For a more detailed explanation of the issues that have been negotiated, see for instance: <www.iatp.org> or a short overview in M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 139-143 .

[271] For a detailed analysis of how the EU has taken up the lobby points from the CIAA, see M. Vander Stichele, K. Bizarri, L. Plank, Corporate power over EU trade policy: good for business bad for the world, Seattle to Brussels Network, Brussels, October 2006, < http://www.foeeurope.org/publications/2006/Corporate_power_over_EU_Trade_policy_Sept_2006.pdf>

[272] See for more information: http://www.ciaa.be

[273] CIAA (2006), WTO negotiations following the Hong Kong Ministerial Conference: restoring balance in the agriculture agreement, position paper, Brussels, 28 February 2006 (See www.ciaa.be).

or industries. This formula leaves no product of interest to the EU industry unaffected. This reflects the CIAA interest that *"no tariff lines should be exempted from reduction commitments"*[274].

- - A **tiered tariff-cutting formula** has been pushed by the EU and other developed countries that would apply the biggest cuts in the highest tariffs and reduce tariff peaks and tariff escalation. This would be particularly effective in reducing tariffs on processed food, also in developing countries: the CIAA does not want emerging markets "*to escape cuts of high agricultural tariffs*".[275]

- - Developing countries have asked for fewer tariff cuts ("flexibilities") to be applied for "**special products**" that are important for food security and rural development, and for "**special safeguard measures**" in case import surges lead to price falls that destroy a country's agriculture or farmers' livelihoods. The EU has been reluctant to fully support this demand, and the negotiations still need to define how developing countries can use them. This reflects the CIAA position that "*developing countries will certainly have a safeguard and we will have to formulate the boundaries of the safeguard*"[276].

(b) Parallelism: the EU has resisted pressure to reduce its **export and domestic support subsidies** if other support schemes such as export credits and food aid schemes – used as market-opening tools - by other WTO members, especially the US, are not reduced at the same time. The EU has attached this condition to its concession in December 2005 to stop export subsidies by 2013. This reflects the CIAA's request for parallelism to ensure the industry's direct and indirect subsidies are not cut while that would not be the case for its foreign competitors, thereby making the EU food and drink industry less competitive.

(c) Limiting market access: Within the negotiated tariff instruments, the EU has been trying to protect Europe's market for primary and processed food as long as possible or as long as the others protect their markets. This would keep foreign competitors out of the European processed food and drinks market, certainly as long as the CAP reform has not led to agricultural ingredient prices for the European processing industry that are as low as on the world market. As the CIAA states "*ultimately, it must be possible to keep specific duties for agricultural and processed products*."[277] Under pressure from the EU, negotiators agreed to have fewer tariff cuts on "**sensitive products**" in developed

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[274] CIAA (2005), Press Release: European Food and Drink Industry favours clearer trade rules and a balanced agriculture agreement at the WTO Hong Kong Ministerial Meeting to be held from 13-18 December 2005, Brussels, 14 October 2005.

[275] The CIAA states that it "would be concerned if emerging economies were able to escape cuts of high agricultural tariffs": CIAA (2005). Press release: CIAA concerned about lack of progress in negotiations. Brussels. Brussels, 8 September 2005.

[276] M. Vander Stichele, K. Bizarri, L. Plank, Corporate power over EU trade policy: good for business bad for the world, Seattle to Brussels Network, Brussels, October 2006, footnote 77.

[277] M. Vander Stichele, K. Bizarri, L. Plank, Corporate power over EU trade policy: good for business bad for the world, Seattle to Brussels Network, Brussels, October 2006, footnote 75.

countries but it was not yet decided which (processed) agricultural products would be covered.

(d) Access to cheap inputs and raw materials: WTO rules and further reforms in the Common Agricultural Policy (CAP) pushed in the Doha Round negotiations will lower the market price for agricultural commodities produced within Europe and compensate farmers for the difference between the market price and production costs via decoupled payments. This provides the food processing industry with much cheaper inputs, also making it competitive in export markets.

Box 11: Lobbying through different channels: the case of Unilever

Unilever appears to be carrying out its lobbying activities in a particularly strategic and systematic manner. Representatives of the company occupy leading positions within important European business branch organisations such as UNICE, CIAA and the TABD. Depending on the case, Unilever may team up with other TNCs in a variety of coalitions and associations. “We know where to find each other” stated a Unilever representative. However, on WTO issues, Unilever claims to take the lead within the associations of which it is a member, both at national and European level. A Unilever representative chairs the Dutch trade policy committee of the Dutch employers' federation, is a member of the CIAA Trade and Competitiveness Committee, is a “rapporteur” on agriculture for UNICE, and Unilever’s Jean Martin is also President of the CIAA. As a rapporteur for UNICE, Unilever meets in private meetings with the European Commission. Similarly, the European Commission also participates in some of UNICE’s working groups. Peter Carl, former Director General of DG Trade, had a standing invitation to such working groups – meetings were indeed organised according to Mr. Carl’s agenda and, in the opinion of the Unilever representative, it was thanks to the massive business lobbying at all levels of government, following the failure of Cancun, that brought the negotiations back on track. Unilever participates in many political and public debates and has strong connections with many high-ranking politicians, which extends to its non-executive director, Lord Brittan of Spennithorne, former EU Trade Commissioner.

Source: M. Vander Stichele, K. Bizarri, L. Plank, Corporate power over EU trade policy: good for business bad for the world, Seattle to Brussels Network, October 2006, < http://www.foeeurope.org/publications/2006/Corporate_power_over_EU_Trade_policy_Sept_2006.pdf>

→ Critical issues

The push to open up developing countries’ agricultural markets and the targeting of high tariffs might leave their domestic processed-food industry unfairly exposed to foreign competitors that have gained much more competitiveness over the years from subsidies and by operating in large or multiple markets. By protecting its own processed industry as much as possible through complex schemes at the same time, the EU does not provide developing countries with similar market openings. The proposed tariff cuts also benefit the supply chain of food and drink multinationals that are increasingly established in developing countries or are operating regional production and supply strategies, based on the cheapest possible sourcing in a region.

The CAP reforms of decoupled payments are increasingly being recognized as a trade distorting subsidy for Europe's exporting food and drink industry because it does not have to pay the full production costs of its supplies.[278]

The lobby of the food and drink industry in Europe, through the CIAA and otherwise, is not a unique phenomenon for Europe and such lobbying can also be observed in other developed countries. However, there is little attention being paid to the undemocratic and privileged access lobbyists have to the (EU) negotiators. By the end of 2006, the EU still had not fully developed meaningful lobby transparency rules. The undue impact of the food industry's interests on developing countries' agricultural and food processing industries has so far remained unchallenged.

Box 12

"Most policy advice given to poor countries over the last several decades – including that by the World Bank – has emphasized the advantages of participating in the global economy. But global markets are far from equitable, and the rules governing their functioning have a disproportionately negative effect on developing countries. These rules are the outcome of complex negotiating processes in which developing countries have less voice. Moreover, even if markets worked equitably, unequal endowments would limit the ability of poor countries to benefit from global opportunities. Leveling the global economic and political playing fields thus requires more equitable rules for the functioning of global markets, more effective participation of poor countries in global rule-setting processes".

Source: World Bank, World Development Report 2006

4.2. Trade and standards

Apart from tariffs, developing countries are meeting many other hindrances to export their processed food and beverages, such as the food standards of importing countries, complex and inefficient customs procedures, licensing arrangements, registration requirements, and intellectual property rights.

For processed food exports, the food safety and health requirements and other technical standards are considered to be very significant impediments, although they are hard to

[278] In other words: While EU subsidies for domestic support are being reduced and changed towards more direct payment to farmers to be compatible with the WTO and stop the high prices above world prices in the EU, these subsidies are still indirectly trade distorting because they allow the food industry to acquire cheaper ingredients and therefore enable it to bring products on the domestic and world markets at a lower price than when they would have to pay European farmers their full price.

quantify. The capacity of companies to meet the increasingly stringent standards required by developed countries, in particular, is increasingly influencing the international competitiveness of food and beverage exports from developing countries and their domestic enterprises. Some companies from developing countries manage to meet the high costs associated with these standards and increase their export capacity, while many others fail to meet the standards and see their produce banned or rejected at the borders of the importing country.

4.2.1. What standards for processed food and drinks?

Governments have established different regulations and standards on processed food, primarily to guarantee their safety for consumers and to prevent long-term damage from production or trade. The private sector has also established requirements that function as standards. The WTO makes a distinction between technical regulations which are required by governments and which need to be implemented in order to sell a product, and standards with which compliance is voluntary.[279] These measures are:

- **Sanitary and phyto-sanitary regulations and standards**: food health and safety requirements and other measures to be taken in order to make food and beverages safe and healthy for consumption and in order to avoid diseases and other health problems for animals and plants. Examples are maximum levels of pesticide residues or (natural) toxins, traceability requirements, restrictions on certain processing techniques, limits of veterinary medicines use, etc.
- **Technical regulations and standards:** requirements how food and beverages need to be produced, traded, packaged and marketed e.g. labeling requirements.
- **Private standards**: standards set individually or collectively by food and drink processing companies towards suppliers of their ingredients, and by retailers towards their private label suppliers and other processed food and drinks suppliers.
- **Certification and labeling on social and environmental impacts regarding processing and production methods (PPMs)**: measures undertaken during the production and processing to respect the required social and labour standards and to minimize negative environmental effects are being assured through private or governmental certification institutes and labeling. Indeed, these methods do not differentiate the appearance of these products ('non-product related PPMs') from other products
- The growing safety and health demands by consumers in developed countries (see Chapter 2) and some of the health scares (e.g. avian flu) have led to the introduction of many new and more stringent regulations and private standards on (primary) processed and unprocessed food.

[279] http://www.wto.org/english/tratop_e/tbt_e/tbt_info_e.htm: technical information on technical barriers to trade

4.2.2. International standard setting bodies

In order to promote standards that protect public health against contaminated food and prevent trade barriers due to abuses or unscientific arguments in setting or food standards, the following international bodies deal with the process of setting international standards and promoting their worldwide implementation by national governments; their standards are directly or indirectly (through ingredients) applied to processed food and drink products:

- The Codex Alimentarius Commission: for food safety
- The International Office of Epizootics: for animal health
- The FAO International Plant Protection Convention: for plant health.

The functioning of the Codex Alimentarius and problems facing developing countries in this body are described in SOMO's report on the fresh fruit and vegetable chain.[280]

4.2.3. The WTO's influence on regulations and standards

The WTO has established rules to prevent food standards and regulations becoming non-tariff barriers to trade as follows. **The WTO Agreement on the Application of Sanitary and Phytosanitary Measures (SPS agreement)** allows governments to introduce food safety and animal and plant health regulations, but they should preferably be based on those from the international standard-setting bodies, any other or higher regulations standards are to be based on scientific evidence. **WTO Agreement on Technical Barriers to Trade (TBT Agreement) describes how** to prepare, adopt and apply technical standards and regulations and does not want technical regulations to be more trade restrictive than necessary to achieve a given policy objective related to the protection of human, plant and animal life or health, the environment, national security and the prevention of deceptive practices.
Both agreements also try to avoid trade restrictions by imposing the following principles:

- no discrimination between domestic and foreign food products, or between foreign food products
- making national standard setting and risk assessments more transparent for other WTO members and their exporters, e.g. through notification at the WTO
- non-governmental standards, such as those set by retailers, also need to apply the provisions of the Agreement
- special and differential treatment for developing countries' application of the agreement
- encouragement of harmonization of standards through the usage of standards agreed at international standard bodies
- supporting 'equivalence' whereby one country recognizes the technical regulations and procedures to assess the risk of conformity of other countries, even if they are different (mutual recognition)

[280] M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 122-125.

- complaints about undue rejections or bans of food produce and other non-applications of the Agreements by other countries must be settled through the WTO dispute settlement procedure

Notwithstanding these WTO rules, developing countries still complain that food safety standards and regulations are too prohibitive for their exporters and are disguised protectionist tools of the developed countries. The WTO's SPS and TBT agreements do not seem to have solved the problem that some imported foods face more stringent controls and standards than local processors.[281]

Standards still not adapted to developing countries

The current agreements have helped developing countries to be informed about standard setting and new regulations introduced by other WTO members, and even to complain about such new regulations. However, many smaller developing countries lack the human resources to fully exploit these possibilities or to defend their interests in negotiations. The rapidly changing Northern food standards, regulations and risk assessments still do not take sufficient account of Southern circumstances, climate and marketing structures, and thereby the ability of Southern countries to meet the required safety levels. In addition, the WTO has not achieved a rapid move towards harmonization and mutual recognition of standards and inspections among countries (equivalence). Developing countries also lack the capacity to effectively participate in international standard setting bodies, which in any case are too slow to deal with the many new processed products.[282] As a consequence, developing country exporters must still comply with a complex set of a standards and regulations that vary considerably per developed country, or face rejection. This results in production and transaction costs which can be difficult to meet. Many food and drink producers in developing countries have therefore had difficulty continuing to export, or even to continue their business if alternative markets were not found. There has not been enough research to quantify how much (smaller) food and drink companies have suffered or disappeared due to food standards and regulations, as indicated by many case studies and anecdotal evidence.[283]

Such marginalization of many food processing companies in developing countries is attributed to a lack of financial, human, technical and scientific resources to implement the requirements, especially by smaller companies whose costs are relatively higher.[284] Some governments of developing countries also lack the regulatory, administrative and training capacity, as well as the infrastructure to support their producers and test the products before exporting, as required by some importing countries. Moreover, developing countries claim that concrete assistance from donors is insufficient or inadequate, and

[281] S. Jaffee, S. Henson, Agro-food exports from developing countries: the challenges posed by standards, p. 94.

[282] See for instance: M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 123-124; see also chapter 2 about the new products the Western processed food industry introduces.

[283] S. Jaffee, S. Henson, Agro-food exports from developing countries: the challenges posed by standards, p. 98-100.

[284] See amonst others: S. Jaffee, S. Henson, Agro-food exports from developing countries: the challenges posed by standards, p. 111

fails to meet the promises of technical assistance laid down in the SPS and TBT agreements and international standard-setting bodies. [285]

→ Critical issues

While lowering food and drink standards is mostly not a good option, it is important to note that WTO does not oblige or guarantee that the price paid to processed food manufacturers incorporates all the costs of compliance with the standards.

By not being able to sufficiently meet the food standards and regulations, processors in developing countries could lose their comparative advantage in processed food based on natural resources grown in their countries or cheap labour. This can also encourage take-overs by foreign companies, which is a growing phenomenon (see chapter 2).

Meeting standards improves competitiveness

Developing country exporters of processed food and drinks which are sufficiently well-informed and linked with their customers, pro-active and well resourced to invest in meeting the changing official and private standard demands, and/or who receive sufficient governmental support, see their export potential increase because they can easily supply to many supply chains and have become more competitive and sometimes more efficient. The standards are also improving food safety and consumer confidence in the domestic market.

The WTO's negative effects on food safety standards

The WTO's SPS and TBT agreements and their reference to Codex Alimentarius standards have negatively affected the quality of the standards and the decision-making process at that body (see the SOMO report "Who reaps the fruit?"[286]). These agreements are not clear about what social and environmental labelling, or which retailer standards at higher than governmental levels, are acceptable. Moreover, Western food companies that see food regulations as barriers to their trade, can ask their home governments to resort to the WTO dispute settlement system or lobby the host governments for removal of such standards.

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[285] Quoted in : J. Wilkinson, The food processing industry, globalization and developing countries, electronic Journal of Agricultural and Development Economics, Vol. 1, No. 2, 2004, p. 189 , < http://www.fao.org/es/esa/ejade/vol_1/vol_1_2/cover_en.htm> (July-November 2006);

[286] M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 125-127.

4.3. Investment rules that allow rapid internationalisation of the food processing industry

Current investment policies are an important element, as they have enabled the food processing sector to become more international and to expand enormously in size and influence. They have enabled food multinationals to undertake investments, mergers and acquisitions, disinvestments and strategic alliances so that they could be present and adapt to new and profitable consumer markets, while also overcoming difficult trade barriers. Investment policies, supported by trade liberalisation policies, have also contributed to more domestic and foreign (primary) processing industries being part of the global supply chain or regional strategies of food multinationals.

4.3.1. Changes in investment policy orientation

Over the last decades, the World Bank, the IMF, donors and various trade and investment agreements have totally reversed many investment policies which developing countries had undertaken in their drive to become economically independent. Newly independent developing countries had been nationalising foreign investments or had introduced strict rules on foreign investments. They tried to capture the economic benefits and spill-offs of foreign investment, for instance by requiring that foreign investors cannot own more than 49% of a domestic company or need to engage in joint ventures. Such severe restrictions on equity participation in East Asia partly explain why Japanese (food) companies invested little, in value terms, in East Asia before 2000, and why Japanese investment was more in the form of ‘ affiliates’ rather than subsidiaries, as ‘affiliates’ involve less control by the company to which it is related.[287] Other rules by which developing countries attempted to benefit from foreign investors was to make the use of domestic natural resources and national labour or management compulsory (‘local content requirement’), or by limiting the use of foreign exchange by foreign investors.. Such policies are now virtually impossible to enforce, due to various investment agreements which are explained below.

After the lack of diversification in many developing countries, from basic agricultural commodities into more processing industries, for example, liberalisation of foreign investment is currently considered to be the solution for supplementing the lack of domestic capital, donor aid, know-how and infrastructure, while allowing investors to use their domestic human, labour and natural resources. This is seen as the way for them to integrate into the world economy and promote economic development. Many developing

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[287] J. Wilkinson, The food processing industry, globalization and developing countries, electronic Journal of Agricultural and Development Economics, Vol. 1, No. 2, 2004, p. 187 , < http://www.fao.org/es/esa/ejade/vol_1/vol_1_2/cover_en.htm> (July-November 2006);
N.B. : “A corporation may be referred to as an affiliate of another when it is related to it but not strictly controlled by it, as with a subsidiary relationship, or when it is desired to avoid the appearance of control. This is sometimes seen with multinational companies that need to avoid restrictive laws (or negative public opinion) on foreign ownership.”

countries have therefore focused on attracting foreign investment and opening up to foreign investment, by providing investors with protection against national regulation that could harm foreign investors' interests, and by providing a wide range of incentives. However, the means by which investment liberalization is being implemented at the national level, and at the international level through negotiated agreements, is increasingly the subject of debate, because the effects on developing countries' economies, social development and the environment are not always as desired or as planned. Chapter 3 has provided some examples of the negative effects associated with processed food investments within such investment policy frameworks.

4.3.2. Incentives at the national level

In order to attract foreign investors, developing countries have implemented the following policy measures and rules that would make it profitable for foreign investors, even though some of the circumstances and political instability do make it risky or not very profitable to invest. Such incentives include:

- tax exemptions or reductions on profits made, often for a period of 5 to 10 years,
- tariff exemptions on imports, e.g. of machinery
- a wide range of rules that guarantee investors that they can move their money and profits in and out of the country, without obligations to reinvest the profits made in the country
- building infrastructure only for the smoother operation of the investors
- establishment of export processing zones (EPZs) in which investors receive even more benefits, such as removal of import restrictions, and often formal or informal exemptions from the application of labour and environmental laws.

→ Critical issues

Food multinationals sometimes make use of these incentives, while the same ones may not be available to domestic investors, resulting in unequal competition. And with all these incentives going to foreign (food and drink) companies, the question is what benefits are left for the host government?

4.3.3. Bilateral investment agreements

In order to guarantee that their investing companies are not being expropriated and disadvantaged vis-à-vis domestic companies and other foreign companies, Northern governments have bilaterally negotiated and signed "bilateral investment agreements" (BITs). Although these BITs were originally intended to encourage investment in developing countries[288], in the past decade these agreements have taken the approach that protection of investments and providing investors with predictability by restricting national regulations is the only way to attract investment.

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[288] See for instance: M. Filbri, I. Praagman, A Sustainable Balance?, SOMO, November 1999.

The number of BITs increased dramatically during the 1990s, from 385 in 1989 to a total of 2,265 in 2003. One reason for this increase is that many developing countries have started to sign BITs between one another. Note that developed countries did not sign BITs between one another because they are part of the OECD Code of Liberalisation of Capital Movements, which promotes very wide liberalisation of investment and capital movements but is less sanctionable than BITS.[289]

The most common rules covered by BITS which are of interest to foreign food processing companies, given their strategies described in chapter 2, are:

- **A broad definition of investment**: not only including foreign direct investment but also portfolio investment, shares and bonds, intellectual property rights, licences and concessions.
- **Non-discrimination principles**: once a foreign investor is operating in a country, governments cannot give that investor any treatment "less favourable" than that given to national/domestic investors ("**national treatment**" principle) and other foreign investors ("**Most favoured Nation"** clause or MFN).
- **Fair treatment**: host governments are required to give foreign investors fair and equitable treatment, as well as full protection and security
- **Freedom of capital movements**: investors are guaranteed that they can freely transfer payments related to, or in connection with, their investments. This includes repatriation of profits without conditions. Sometimes BITs include rules for an exception on a temporary basis in the case of balance-of-payment (BoP) problems.
- **Expropriation rules and compensation**: a state may not nationalise or expropriate the property of a foreign investor except for a public purpose, in a non-discriminatory manner, in accordance with due process of law and upon payment of compensation. Increasingly, measures considered equivalent to expropriation are explicitly or implicitly included so that new governmental laws that prohibit products or operations from which foreign investors intend to make profits, can be sued by foreign investors.
- **Investor-to-state dispute settlement and state-to-state dispute settlement**: disputes about non-compliance with BIT rules between a state and foreign investors, or between 2 states which have signed a BIT, can be resolved within a small number of agreed international dispute-settlement mechanisms. This includes the right for foreign investors to sue host governments outside the country, but not vice versa.

→ Critical issues

The most striking aspect of current BITs is the imbalance between the rights and guarantees for foreign investors on the one hand, and the lack of obligations, duties or corporate social responsibility mechanisms on the other hand. This allows foreign investors such as food companies to exploit insufficient regulations or nonenforcement of domestic social and environmental laws by the host

[289] For full text see: <http://www.oecd.org/dataoecd/10/62/4844455.pdf>

country. On the other hand, BITs establish obligations upon host governments regarding how they must treat foreign investors, thus restricting these goverments' room to manoeuvre.

The national treatment principle can have far reaching effects on economic development policies, as national companies cannot be favoured over foreign companies with regard to incentives, subsidies, etc. to promote their growth. Also, as foreign investors should receive a “no less favourable” treatment, this means that they can be treated more favourably than national investors. This can happen when governments are too keen to attract investors and boost export from their countries, at the expense of the local enterprises. The non-discrimination articles of BITs also prohibit governments to give more favourable treatment to foreign investors with a good record for corporate responsibility.[290]

4.3.4. The WTO agreement on investment restricts governments' treatment of foreign investment

Some regulations and measures by which (developing) countries have attempted to obtain economic benefits from foreign investors have been considered by Northern governments as restricting the imports and exports of foreign investors and their freedom of operation. These measures include:

- **Local content requirements**: obligation to purchase or use products of host country origin
- **Import restrictions**: limitation on the use of imported products according to the amount of local products that a foreign investing company exports
- **Foreign exchange limitations**: access by an investor to foreign exchange is limited to the amount of foreign exchange inflow generated by the investor
- **Export restrictions**: exports by an investor are limited in volume or in value, according to its domestic production or because they belong to a certain category

These “trade-related investment measures” were deemed to be violating the WTO's rule of non-discrimination and elimination of all quotas (Art. III and XI of GATT 1947), be economically inefficient and hindering the profit-making strategies of foreign companies. The developed countries managed in the WTO to get developing countries to agree to an Agreement on Trade Related Investment Measures (TRIMs), under which the forbidden measures would be eliminated, including in the food processing sector. Developed countries were given 2 years to do so, developing countries 5 years and least developed countries 7 years. Various developing countries found it difficult to eliminate the measures, and have asked for an extension of the elimination period.

[290] For a full analysis, see: S. van Bennekom, M.Vander Stichele, Investment agreements and corporate social responsibility (CSR): contradictions, incentives and policy options, SOMO Discussion paper 1, November 2005.

→ Critical issues

The TRIMs agreement further limits the room to manoeuvre of developing countries. The usefulness of local content requirements remains an issue of discussion, but in the food processing industry, which typically could rely on food products grown in the host country, it would be useful to grant countries the possibility to see whether local content requirements are useful. At the moment, when locally produced products can be imported more cheaply, food companies are importing them and leaving local producers without (new) outlets, for example powdered milk for dairy products or herbs for soup.

4.4. Gats: trade and investment rules for supermarkets

Chapter 2 of this report has described the worldwide expansion of a few supermarkets, their private-label processed food products, and the resulting growing influence and power of supermarkets over the whole supply chain.
The expansion of some internationally operating supermarkets has been made possible by liberalisation policies, with governments granting market access to foreign supermarkets to operate in their countries. This was carried out on the basis of unilateral governmental decisions, or through negotiations of international agreements such as the General Agreement on Trade in Services (GATS) under the WTO or bilateral/regional trade agreements. The GATS agreement came into force in 1995 and often serves as a model for bilateral or regional trade agreements in which supermarkets and other retail services are liberalised. However, GATS article 5 states that regional or bilateral trade in services agreements need to be liberalised substantially, although developing countries have more leeway when they liberalise among themselves. This is in contrast to the GATS agreement that allows countries to only liberalise those sectors they deem of importance to their development or economy, or for which they give in under pressure of the negotiations. Under the current GATS agreement, fifty-five (55)[291] countries including the EU member state countries, had made commitments to open up their retail services. New members of the WTO after 1995 have tended to open up more of their retail services than WTO members did during the negotiations that shaped the GATS agreement (Uruguay Round negotiations, 1986-1994).

Countries that liberalise under GATS have to abide by GATS rules, which protect foreign retailers against governmental regulations that could harm their interests. As "trade in services" in practice often means that foreign service providers, such as supermarkets, need to establish themselves in the country in which they want to offer their services, some of the GATS rules resemble the investment liberalisation agreements described above. Key GATS rules that apply to countries which have liberalised various supermarket services, under the heading retail services include:

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[291] M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 147: calculated for countries being member of the WTO by the end of 2004.

- **non-discrimination principle** under which foreign supermarkets cannot be treated less equally than national supermarkets (national treatment) and or in a discriminatory way between various foreign supermarkets (MFN)
- **no "unnecessary barriers to trade"** and no restriction on the supply of the supermarket services when governments apply licensing procedures, qualification requirements and technical standards for supermarkets
- **prohibition of several "market access" restrictions** imposed by governments, such as limits on the number or value of supermarket operations and their assets, limitations to foreign ownership of supermarkets, and requirements on the legal form under which the supermarkets may operate
- **freedom of current capital transactions** such as profit repatriation

GATS members which liberalise retail services under GATS can make exemptions to national treatment and in applying market access restrictions. Negotiators of developing countries have to be aware of this technical possibility, or forego these regulatory rights. For full details of the GATS rules and their relation to supermarkets or retail services, see the SOMO report "Who reaps the fruit?"[292]

4.4.1. Concerns about the liberalisation of supermarkets and its impact on the processed food sector

After developing country governments have liberalised supermarket services unilaterally or through trade in services agreements, usually one or some of the small number of internationally operating supermarkets (see Chapter 2) establish themselves in the country. As explained in Chapter 2, these supermarket chains have longstanding supply relationships with big food multinationals (which often have production units in developing countries), which can make it cheaper for supermarkets to purchase the food and drinks they sell. Small processed food and drink manufacturers have much less chance to supply large supermarket chains who want large quantities at a high quality but a low price. Supermarkets selling private labels might use local food and drink manufacturers, but the question remains as to how profitable that is for the local processed food and drink industry.

Because of their experience, worldwide supply lines, capital and technical resources, supermarkets sell processed food and drinks at low prices. As a result, small shops can rapidly disappear, leaving some villages and small towns as "food deserts".[293] Informal and small shopkeepers in developing countries, often women, selling processed food lose their source of income. It also means that many consumers need to go to supermarkets, hypermarkets or discounters to buy processed food. Even when convenience shops remain or return, they are often in the hands of the same large supermarket chains. This leads to concentration of processed food sales in the hands of large foreign supermarkets, resulting in buyer power and abuses (see Chapter 2).

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[292] M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 145-148, and Annex 1

[293] Idem: see example of Thailand (p. 148-149).

The problem is that GATS and other trade in services agreements do not have instruments that help governments to solve the problems associated with supermarket liberalisation. Some GATS rules undermine the measures which governments wish to take in order to deal with new problems. The new GATS negotiations that have started since 2000 and which are part of the WTO Doha Round include further liberalisation of services and limiting of governmental regulations, which raises the following concerns for supermarket services:

- Developed countries have asked many developing countries to open up their retail or distribution services markets and have focused on the largest and most profitable developing countries through a special negotiation instrument ("plurilateral" or "collective" requests).[294] Although impact assessments and sectoral studies indicate the need for accompanying regulations, the negotiations do not guarantee that the necessary accompanying measures are in place.[295]
- The negotiations should lead to the removal of many restrictions governments still have in place against full **foreign ownership** of supermarkets and other distribution services.[296] This means that foreign supermarket chains should be more able to fully take over local supermarkets and other retailers, which can greatly affect the domestic suppliers of fresh, primary processed and processed food and drinks.
- The right of governments to apply **economic needs tests** should be substantially reduced.[297] This means that (developing) countries will no longer make an assessment of the economic, employment, social and environmental impact before they give permission to build a new supermarket, hypermarket or discounter.
- **Domestic regulation** further curtailed: Negotiations to further define what kind of technical standards, licensing and other qualification requirements "constitute unnecessary barriers to trade" and could lead to governments being further restricted in regulating what they see as necessary for social, developmental and environmental purposes in their country. In particular, the debate about the need to prove that the measures taken are economically necessary, "reasonable" and not trade-restrictive has been controversial. In the case of retail services, many developing countries have had little experience with the impact of large supermarkets and might not have other means for restricting trade to enable them to quickly deal with problematic situations in their country. Moreover, developed countries are extremely reluctant to negotiate **safeguard measures** which WTO members can use when liberalisation is too destructive to their economies or social development.
- Developed countries are requesting that managers and other **skilled personnel** can easily enter other WTO member countries, for instance to manage newly established supermarkets and swiftly increase the competitiveness vis-à-vis local supermarkets. At the same time, developed countries are extremely reluctant to

[294] Idem, p. 150-151.
[295] Idem, p. 148-149.
[296] WTO Ministerial Conference Declaration, Hong Kong, December 2005, Annex C
[297] Ibid.

allow movement of low-skilled personnel, which is of interest to developing countries.

→ Critical issues

The GATS agreement and other free trade agreements do not have stringent measures to deal with concentration of supermarkets at the global level, nor to deal with buyer power problems following the opening up of markets. Art. IX of the GATS recognises that any service provider can engage in anti-competitive behaviour but provides for only voluntary consultation and exchange of information as a - weak - remedy. Rapid international concentration of supermarket chains and their impact on processed food is currently not being tackled in agreements that promote such concentration (see also Chapter 5 on competition policy).

The European retail services industry is lobbying hard to ensure that they get more permanent market access and investment protection in profitable developing countries, through bilateral negotiations and through the WTO. They try to use negotiations for such agreements to get countries to eliminate laws that limit their operations and profitability, such as laws that restrict the size of supermarkets or prohibit supermarkets being situated near to town centres. As few impact assessments are being made beforehand – or if they are made, hardly taken into account by the negotiators - and as many parliamentarians, local entrepreneurs and citizens of the countries under pressure to open up are hardly aware of the free trade talks, their interests are not taken into account. Subsequently, measures to avoid potential negative impacts, such as on local processed and other food suppliers, might not be put into place. Worse, some lobbyists try to have the right to comment before new legislation is put into place being incorporated in the new GATS or free trade agreements.

GATS negotiations were suspended in July 2006, along with the entire Doha Round . At the end of 2006, there were new attempts to kick-start the negotiations, including by resuming work on the GATS negotiations. It was not clear whether more prudent non-business concerns would be taken into account in the renewed talks.

4.5. Summary and conclusions

Although the WTO Agreement in Agriculture, other WTO rules and other agreements have liberalised trade, this report has shown evidence that exports from developing countries in all (primary) processed food and drinks still face many obstacles, mainly:

- High tariffs, i.e. much higher than the average industrial tariffs in developed countries
- Tariff escalation that makes processed products more expensive than primary agricultural commodities

Both tariff escalation and high tariffs are reduced, but not fully eliminated, for processed food exports from developing countries receiving preferential access by developed countries.

- Unequal access compared to member countries of a trade bloc
- Anti-dumping rules against excessively low prices
- Countervailing duties against allegedly subsidised products
- Emergency safeguard measures that reverse market opening commitments
- Special safeguard measures under the WTO Agreement on Agriculture, which many developing countries cannot use, however
- Food standards set by national, regional or international governmental bodies and by private enterprises, and certification and labelling, including on processing and production methods related to social and environmental impacts
- Export subsidies which especially the EU gives to its processed food and drink industry
- Domestic support subsidies which are also given to the processed industry in the EU and other developed countries

Most of the above mentioned measures can also be applied by developing countries to protect their (primary) processed industry but some are too costly or cumbersome to be used by governments or small producers who have to provide the proofs harm.

By allowing most of the above measures, WTO agreements lead to unfair competition for exports by food processors from developing countries. This marginalises or eliminates small food and drink producers, and disadvantages the food-export orientation policies implemented by many developing countries wishing to participate in the global economy. There are no WTO rules or other rules that guarantee that developed countries' exporters are getting a price that covers the (increasing) cost of applying the standards and providing the necessary proofs for it. Lack of mutual recognition agreements and lack of support for developing countries to develop or meet standards as promised under WTO agreements and Codex Alimentarius have not allowed many producers in developing countries to adapt to the rapidly growing standards that partly result from the changing demands of developed country consumers (see chapter 2). Private standards that are higher than governmental standards and seen as barriers to trade by developing countries are still not tackled on the basis of WTO rules, but WTO discussions are starting for the fresh fruit and vegetable sector. The WTO has so far been unclear regarding whether to allow governmental and some private labelling and certification based on processing and production methods. This undermines some labelling and certification schemes that could be part of the solution for preventing social and environmental exploitative relationships in the production and supply chain as described in Chapter 3.

Whether new WTO negotiations will improve the situation of companies in the processed food sector in developing countries remains to be seen. The lobby of the processed food and drinks industry has an important influence for instance on the negotiation position of the EU, which is in line with protecting the interests of the processed food industry in the EU (which also includes US and other food and drink companies) and getting much more access to processed food markets in developing countries for their exports or production chains. Unfair competition from indirect subsides might also continue if WTO talks restart based on the same proposals as are currently on the table.

Food and drink processors in developing countries also face competition in their domestic markets from food and drink multinationals and supermarkets investing and taking over local industries, rather than trading, in order to meet local consumer demands (see Chapter 2). Such investments are supported by many measures taken by developing countries to attract foreign investment which is increasingly seen as the way to development and integration into the world economy. Foreign food and drink investors are receiving advantages by unilateral measures such as exemption of tax payments, of import or export restrictions or even labour laws. Through bilateral investment agreements (BITs), the TRIMs and GATS agreements under the WTO, investors in processed commodity trade, food and drink processing, and supermarket or other retail services receive legal protection against governmental measures that could disadvantage or harm their profit making. These agreements undermine the governments' regulatory flexibility and can prevent some measures that would be needed to support local and small food, drink and commodity processing companies or even financial stability. As these agreements do not impose obligations on investors or home countries, they are imbalanced in favour of the latter and do not encourage solutions and legal mechanisms to solve problems of undue and unfair behaviour by foreign commodity, food or drink and retail investors.

Investment liberalisation measures taken by the governments of developing countries, which accept 100% ownership by foreign companies or remove other related restrictions, allow food multinationals to establish or take over local food and drink processing industries as soon as they see that a developing country market is becoming profitable for them. The GATS agreement promotes 100% ownership and removal of other restrictions on foreign operators, which allows foreign supermarkets to rapidly expand in the newly profitable markets of developing countries.

As a consequence, deregulation and liberalisation of trade and investment without adequate competition policy rules (see Chapter 6) have allowed the trans-nationalisation of the food processing sector and its value chain. Some large food companies and multinationals, and a select group of supermarket chains have expanded enormously and have captured profit making opportunities in developing countries. The economic and political influence and power of these large companies are restructuring developing countries' agricultural systems and processing industries in a way that many poor and marginalised groups cannot benefit from. In addition, only a small minority of entreprises or workers in developing countries can share the income from the industry's growth.

In order to allow processed food and drinks sectors in developing countries to benefit more, the report makes the following recommendations:

- improve the effective participation of the governments of developing countries, and their food processors and consumer organisations, in international standard-setting bodies and the functioning and renegotiations of the SPS and TBT agreements
- standards should, where possible, minimise their incompatibility with the production and marketing systems applied in developing countries
- conceive and establish guarantees that the prices paid to processed food manufacturers incorporate the costs of compliance with standards
- governments of developing countries should, with external support where necessary, maintain or introduce the infrastructure and institutions to regulate, research and test, administer and manage exported (primary) processed food products (for example, through accredited laboratories, or internationally recognised systems of certification), and provide training and other support programmes for their processed food industry
- Northern governments have to stop requiring high levels of trade and investment liberalisation for the processed food and retail sectors in developing countries, and listening too much to their powerful and opaque business lobbies. Trade and investment agreements must guarantee benefits for the poor and the environment and the rights and obligations of these agreements need to be urgently rebalanced.

Chapter 5
Competition policy not sufficiently dealing with concentration, malpractices and buyer power

5.1. Dealing with concentration of processed food and supermarket chains

Free trade agreements under the WTO and bilateral or regional free trade agreements are removing so-called trade barriers and unfair competition created by governments in order to increase competition and create a "level playing field" in the trade in (processed) agricultural products and services around the world. However, trade liberalisation might not result in more companies having access to the world market if a particular sector is dominated by a few multinational traders, as is the case for cocoa or soy meal amongst other primary processed products (see Chapter 2), or if a large part of domestic markets are taken over by a few internationally operating supermarkets.
There are no competition policy rules at the international level that deal with such concentration at the international level.[298] The attempts made in the WTO since the WTO Ministerial conference in Hong Kong (1996) to negotiate rules on competition policy, were halted at the WTO Ministerial Conference in Cancun (2003) because the developed countries' proposals were aiming more at opening national markets of developing countries than dealing with international concentrations and market abuses by multinationals which are difficult to deal with under national or EU-level competition policy rules. Also, it was difficult for developing countries to negotiate competition policy issues in the WTO. Some developing countries have few or no laws governing competition policy at the national level, and they did not want competition policy rules to be imposed which were not adapted to the level of development and needs of their markets.

Fully processed food and drinks are not yet concentrated at the international level - the largest food multinational, Nestlé has less than 4% of the world market. Chapter 2 has indicated that at the national level, however, some products are produced by very few top multinationals or large national firms (Nestlé, for example, has a market share of 60% in Latin America and 91% in baby formula products in Brazil)[299]. Strategic alliances, co-branding, joint ventures and vertical integration might also lead to concentration of production and large market share of particular processed food and drink products or by supermarkets.

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[298] M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 160-164.
[299] A. Regmi, M. Gehlhar (Ed.), New directions in global food markets, Agriculture Information Bulletin, no. 794, February 2005, p. 68-69; see also chapter 2 for more examples.

National or EU-level competition authorities do not always tackle these concentrations, because competition policy is oriented towards avoiding excessively high prices and other damages to consumers resulting from market concentration, and supermarket chains currently seem to be offering lower prices to consumers, while they may be hiding their high profit margins. In the UK, where Tesco has been achieving in excess of 30% of UK supermarket sales and, together with 3 other supermarkets, is dominating the market (approx. 75%), the UK competition authorities called for a new investigation into the behaviour of supermarkets , mainly with regard to potential harm to consumers resulting from lack of choice, for example.[300]
Many developing countries do not have competition policy rules that are sophisticated enough to look into concentrations of rapidly growing supermarkets or particular products. As only around 100 countries around the world have competition laws, many smaller developing countries hardly even have any competition rules at all.

→ Critical issues

Current competition policy rules are not sufficiently developed to deal with the growing international concentration of primary processed food producers and traders, and international supermarket chains and their broader impacts on economies, international trade and processed food producers. Free trade and investment rules have no instruments to ensure fair competition in an international free market. This is one of the causes of unequal sharing of the benefits of free trade and globalisation, which leads to an increasing gap between rich and poor.

Strategic alliances, co-branding and vertical integration are particular forms of concentration in the processed food sector which many competition policy authorities might not be well equipped to tackle.

5.2. Dealing with market abusive practices in the processed food sector

In the processed drink and food sector, some companies engage in market abusive practices which are forbidden by competition policy laws such as:

Price-fixing cartels: Some food and agricultural companies agree among one another to fix the prices of the products they sell to others in a local market, or even the global market, at a higher level than would be the case if they would be competing against each other. Although companies make these agreements in secret, some of these cartels have been discovered by the competition authorities and the companies involved have been fined millions of euros (sometimes with the exception of the company that informed the authorities). Of the major cartels detected worldwide between 1990 and 2005, 7% were in the food, beverage and tobacco products sector, 22% were in the organic chemicals

[300] UK Office of Fair Trade, The grocery market – The OFT's reasons for making a reference to the Competition Commission, May 2006, <http://www.oft.gov.uk/NR/rdonlyres/1A2D7FA2-FEA3-4459-9B25-4A737A20023D/0/oft845.pdf> (viewed 5 December 2006)

sector (including amino acids and vitamins used by food companies) and 2% were in the agricultural and forestry raw materials sector.[301]

A major global price-fixing cartel for **corn fructose** (a sweetener used in the food and drink industries) was in operation between 1980 and 1995 (see Chapter 3). Ultimately, ADM had to settle for $400 million compensation in the US to food and drink companies, and Cargill settled for $24 million, still claiming it had not engaged in any illegal activity.[302] ADM had already been fined $100 million in the US for price-fixing worldwide in the **lysine** (a food and feed additive) market, and 3 of ADM's top officials were sentenced to prison in the US in 1999.[303] ADM has been fined for the same lysine cartel in the EU in May 2006[304] and in Mexico[305].

Market-sharing and price-fixing cartels: In the beginning of the 1990s, ADM was part of a worldwide secret cartel with 4 other companies (see Chapter 3), through which it fixed prices an shared the market for sales in **citric acid**, used in numerous food and drink products and the most widely used preservative in the world. The European Commission fined the five producers of citric acid a total of €135 in September 2006.[306] At the same time, ADM and 5 other companies were fined €57.53 million by the European Court of First Instance for a market-sharing and price-fixing cartel (1987-1995) for **sodium gluconate**, an additive in food and in various chemical applications.[307]

→ Critical issues

Developing countries' food processing industries which use food additives such as citric acid and corn fructose are faced with higher prices because of the price-

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301 J. Connor, C. Helmers, Statistics on modern private international cartels, 1990-2005, Purdue University, Dept. of Agricultural Economics, Working Paper no. 06-11, November 2006, p. 8

302 Agribusiness Center, 'ADM reaches court settlement in high fructose corn syrup suit', 18 June 2004: http://www.agribusinesscenter.org/interior.cfm?content=headlines&id=590 (viewed 4 December 2006); Archer Daniels Midland Company. 2005 Annual Report. p. 50: Note 15; K. Arasu, "Court OKs Cargill Price-Fixing Settlement", Reuters, 19 May 2004, <http://www.agobservatory.org/showFile.php?RefID=60073> (viewed 4 December 2006)

303 See amongst others: C. Hunter-Gault, Charlayne, "ADM: Who's Next?", October 15, 1996 quoted by < http://en.wikipedia.org/wiki/Archer_Daniels_Midland>

304 European Commission, Competition: Commission welcomes judgment of the Court of Justice in Archer Daniels Midland case (Amino Acids cartel), Press release 06/209, 18 May 2006, <http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/06/209&format=HTML&aged=0&language=EN&guiLanguage=en> (viewed on 4 December 2006)

305 M. Levenstein, V. Suslow, L. Oswald, Contemporary international cartels and developing countries economic effects and implications for competition policy", Working paper no, 03-10, University of Michigan Business School, December 2003, p. 41

306 "European Court upholds fines for citric acid cartel", 28 September 2006, http://www.foodnavigator-usa.com/news-by-product/news.asp?id=70889&idCat=72&k=european-court-upholds (viewed 4 December 32006) ; European Commission, "European Court upholds fines for citric acid cartel", 28 September 2006, Press release 06/351, 27 September 2006, <http://www.foodnavigator-usa.com/news-by-product/news.asp?id=70889&idCat=72&k=european-court-upholds> (viewed 4 December 2006)

307 A. Fletcher, "EU court throws out sodium gluconate cartel, 29 September 2006, < <http://www.foodnavigator.com/news/ng.asp?id=70925-adm-roquette-jungbunzlauer> (viewed 4 December 2006)

fixing and market-sharing cartels. [308] Many developing countries, however, are not aware of the higher costs they endure because they do not have well-developed competition policy authorities and investigation or enforcement capacity. Also, the EU and US competition authorities do not have a mandate to take into account the effects of the cartels in developing countries, nor are there effective cooperation instruments between developed and developing countries' competition authorities and their investigations; there are only a few information-sharing agreements. One solution could be that developing countries could seek remedies from the cartels under the home country jurisdiction of the TNCs involved in the cartel.[309] Existing forums such as the OECD Global forum on Competition and the International Competition Network are more engaged in sharing experience and ideas to promote competition policy.[310] They should also discuss new competition policy issues such as buyer power (see below) or establish cooperation agreements between competition authorities.

The greater the concentration of production of some food items, the easier it is for companies to engage in world wide cartels.

Primary and fully processed food companies as well as supermarkets can also engage in **other** "**restrictive business practices"** whereby they use their market power to sell some products under the production price to drive competitors out of business, for example ("**predatory pricing**").
The case of Coca Cola in Mexico and the EU provides some examples of other restrictive business practices. In Mexico, where Coca Cola has a market share of around 70%, Coca Cola and its distributors were fined US $15 million and $54 million for refusing to deliver Coke products to a shopkeeper who had been asked to stop selling a rival cheaper cola brand ("**refusal to deal**"), threatening to remove refrigerators and displays supplied by Coca Cola from shops that sold other brands, or removing products from competitors from prime locations in some shops.[311] In Europe, Coca Cola had to settle with the European competition authorities by committing to stop its previous practices such as

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[308] Action Aid International website, "Power hungry: six reasons to regulate global food corporations", [no date}, <http://www.actionaid.org.uk/wps/content/documents/power_hungry.pdf > (viewed 4 December 2006)

[309] M. Levenstein, V. Suslow, L. Oswald, Contemporary international cartels and develoing countries economic effects and implications for competition policy", Working paper no. 03-10, University of Michigan Business School, December 2003, p. 40, 43.

[310] See: M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 163-164.

[311] M. Stevenson, "Coca-Cola Slapped With $68 Million Anti-Monopoly Fine", Associated Press, 15 November 2005, <http://www.indiaresource.org/news/2005/2051.html> (viewed 4 December 2005); M. Stevenson, "Mexican court: Sodas not national interest", Associated Press, 18 November 2005, <http://www.indiaresource.org/news/2005/2051.html> (viewed 4 December 2005): Pepsi soft drink market share hovers around 20% – and together with Coke continues to steadily edge out Mexican brands. A local brand lost 10 % market shares over the last 20 years and was left with 3%: the high court decided not to protect that local brand.

exclusive selling whereby customers had to buy all their soft drinks only from Coca Cola, and requiring customers wishing to purchase the top-selling Coca Cola products to also buy less popular Coca Cola products.[312]

5.3. Dealing with buyer power and related competition policy

In the days that supermarkets did not yet have the power over the supply chain that they have today, some countries such as the Netherlands developed laws to ensure that food processors could not threaten not to supply shops and other retailers if their demands were not met. Ironically, today the Dutch food processors –including Unilever- are being forced by the largest supermarket chain Albert Heijn to supply them at very low prices, or lose that outlet, and a food company has even taken the supermarket to court for selling its products below production cost. The Dutch branch organisation of the food and drink industry has complained that their profit margins are too small to allow them to develop new products.[313] The Dutch competition authorities however have so far found no reason to intervene, even after the price war started by Albert Heijn has helped to bring about the collapse of the second largest supermarket chain, Laurus. They then allowed Albert Heijn to buy some of Laurus' shops.

Because guaranteeing low prices to the consumer is considered to be the task of competition policy and competition authorities, the buyer power of supermarkets and their related abusive practices towards their food and drink suppliers, there is still very little that has been legislated for. Chapter 2 above and SOMO's report "Who reaps the fruit?"[314] explain how the malpractices squeeze the prices of the food industry and throughout the chain while more of the profit margins go to the supermarkets. Also the wider impact of supermarket buyer power on job losses at food manufacturers and closures of food shops in villages or small town centres is not being addressed.

Some measures and legislation have however been established[315] in some countries regarding the following problems and abuses:

- **Buyer power and oligopsony** (buyer power concentrated in the hands of a few supermarkets) resulting in large supermarkets getting lower prices from their suppliers than other wholesalers and buying groups: The UK Competition

[312] European Commission, "Commission close to settle antitrust probe into Coca-Cola practices in Europe", press release 04/1247, 19 October 2004, < http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/04/1247&format=HTML&aged=0&language=EN&guiLanguage=en> (viewed on 4 December 2006)

[313] P. Couwenber, "Eerst moeten er slachtoffers vallen", Het Financieele Dagblad, 16 January 2006.

[314] M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 57-62, and p. 156-164.

[315] This information is based on: M. Vander Stichele, S. van der Wal, J. Oldenziel, Who reaps the fruit? Critical issues in the fresh fruit and vegetable chain, SOMO, June 2006, p. 57-62, and p. 156-164; AAI, "Call for action to limit the abuse of power by EU supermarkets", December 2006,

Commission has started a new investigation in June 2006 about the anti-competitive behaviour and buyer power of the large supermarkets in the UK after the voluntary Code of Practice on Supermarkets' Dealings with Suppliers did not solve the suppliers' problems (an investigation in 2000 found 52 kinds of abusive practices); consumers are seen to be potentially harmed by a lack of choice.

- **Below-cost selling:** France has retained a ban on below-cost selling[316] under the new Dutreil Law that came into force on January 2006. Spain, Ireland and Germany have also introduced or retained laws against below-cost selling. In the UK, the Competition Commission is not clear whether below-cost selling is harming the consumer, but it has included the issue in its investigation in 2006.

- **Price flexing:** The practice of supermarkets selling at higher prices in areas where there is less competition while charging low prices in competitive areas is also under investigation by the UK Competition Commission to see whether this is harming the consumer.

- **Market power abuses, including hidden discounts and compulsory extra payments** by suppliers: In order to redress the balance between supermarkets and suppliers and to prevent supermarkets demanding excessive payments from suppliers for shelf space, listing fees, sales promotion, etc. – which can be in the form of discounts applied by the supermarket to the invoices of a supplier ("rebates", "marges arrières"), the new Dutreil Law in France requires that the pricing terms between the retailer and the supplier must be clearly stated on the invoice, with no hidden discounts. Laws in Spain and Germany also prevent retailers from stretching the terms of payment to suppliers. In Indonesia, the Business Competition Supervisory Commission has sufficient powers to condemn the use of listing fees if that leads to bankruptcy, but not to condemn supermarkets that force suppliers not to sell (at lower prices) to other supermarkets. In Korea, the law allows the Korea Fair Trade Commission to fine supermarkets that unfairly reduce prices after goods are purchased, impose payments for advertisements, refuse to accept products or unfairly returned products. Competition regulations in Thailand also attempt to protect suppliers against buyer power and heavy price reductions.

- **Dominant locations:** Many countries such as Spain, the Netherlands have zoning laws restricting the construction of out-of-town supermarkets. In the UK, the Competition Commission is investigating deals made in relation to sites sold by large supermarkets, which restrict competitors from establishing new stores.

→ Critical issues

Many countries, and especially developing countries, still need to take measures and legislate to curb buyer power and protect processed food and other

316 "Reform of pricing laws in France", Planet Retail Daily news, 11 July 2005.

producers against abusive practices by supermarkets. This lack of legislation contrasts with the speed with which international supermarket chains establish themselves in developing countries and use the same practices as witnessed in France and the UK, for example.

The abusive relationship between supermarkets in the North and food or drink suppliers in the South is difficult to legislate. Perhaps the use and renewal of the United Nations Convention on Contracts for the International Sale of Goods (CISG) adopted in Vienna in 1980[317] and the UN Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices[318], which was adopted in 1980 (known as the UN "Set of Principles and Rules on Competition" since 2000) might provide a solution.

The reluctance of, or refusal, by many competition authorities to accept that not only consumer interests but also those of (processed food) suppliers should be protected, does not match the speed of supermarket expansion and concentration. Other legislators and policy makers should perhaps also get more involved in curbing negative impacts of buyer power, such as those dealing with loss of employment and labour conditions (at stores and at suppliers), desertion of towns and villages, excessively low prices for producers in developing countries (while trade is promoted as a development policy tool), increasing pollution problems from out-of-town supermarkets and packaging, concentration of profits from retailing in the hands of a few (Wal-Mart's owners are among the richest people in the World), the loss of specialty shops, etc.

At the EU level, it is not yet clear how the problems of buyer power for suppliers can be addressed while some of the European retailers are present in many of the 25 EU member states. The competition authorities of the European Commission have hardly looked into the matter recently.[319] Competition Commissioner Nelie Kroes has made it clear that she is not concerned about dominant companies as long as the consumer benefits.[320]

Rethinking and re-orienting competition policy is not an easy matter. For developing countries it needs to incorporate the specific needs of their (processed food) industries. New competition policy needs to be progressive to include the interests of suppliers and their workers, social policies such as "promotion of the ability of small businesses, or firms controlled or owned by historically disadvantaged persons, to become competitive" (South African Competition Act, Art. 10.3.(b).(ii)[321]) and to not undermine collective defence

[317] See: http://www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG.html
[318] See: http://r0.unctad.org/en/subsites/cpolicy/docs/CPSet/cpset.htm
[319] The EC looked into the matter by commissioning Dobson Consulting to produce the paper "Buyer power and its impact on competition in the food retail distribution sector of the EU", May 1999, DG IV (IV/98/ETD/078), <http://europa.eu.int/comm/competition/publications/studies/bpifrs/>
[320] "I like aggressive competition including by dominant companies. And I don't care if it may hurt competitors, as long as it ultimately benefits consumers." (New York, September 2005 quoted in: "EU proposals seek to set clear market-abuse rules", International Herald Tribune, 20 December 2005)
[321] Text and information can be downloaded at :

systems or corporate social responsibility initiatives based on cooperation between companies. Some competition lawyers and experts are increasing their research about buyer problems and solutions. A broader political and public debate, research and discussion is needed as has happened in the UK where Parliament issued a report on the loss of small shops, a public campaign prompted much public discussion and the competition authorities came under pressure to take more action.[322]

Existing and new legislation should take into account demands already made by groups[323] in the UK who have been searching, together with groups from outside the UK[324], for solutions. They propose:

- **Legally binding and clearly worded rules** to ensure the fair treatment of all suppliers, in the UK and abroad, supplying directly or through intermediaries;
- **An independent retail supervisor and regulator** who pro-actively monitors the breach of interests of farmers and small suppliers, protects complainants, ensures that the binding rules are followed (mediation and legal action), makes its findings public and recommends necessary changes to the rules;
- **Support for local shops** from local authorities and the government;
- **Measures that hold supermarkets accountable** for internationally recognised workers' rights throughout their supply chain.

<http://www.compcom.co.za/aboutus/aboutus_intro.asp?level=1&desc=7>; < http://www.compcom.co.za/thelaw/TheNewAct.doc>

322 See http://www.breakingthearmlock.com, http://www.tescopoly.org,

323 See website of a UK NGO coalition tackling the negative impacts of supermarkets expansion and buyer power: www.breakingthearmlock.com

324 See: www.agribusinessaccountability.org

5.4. Summary and conclusions

This chapter has shown that there are not enough competition policy instruments at the national, and regional level, and none at the international level to deal with national and international concentration in the primary processed food sector, national concentrations in the processed food sector and national and international concentration in the supermarket sector. There is also insufficient capacity to deal with less transparent forms of concentration that are used in the processed food sector, such as strategic alliances.

The processed food sector is affected by abusive practices such as secret cartels to fix prices and share markets among a few producers of food additives. Some processed food and drink companies engage in abusive “restrictive business practices” whereby customers, shops and retailers are forced to purchase at disadvantageous terms or face no supply. Where governments have enough investigative and regulatory capacity, such practices are punished under national and EU competition law, but many such practices are not discovered in developing countries, leading to higher prices.

The increasing market domination by a few supermarkets has led to buyer power and exploitative pressures on producers to supply at very low price levels or with additional payments or discounts. A few countries have legislated to rebalance the relationship between supermarkets and suppliers, and against abusive practices such as below-cost selling. However, many more countries need to take action and also deal with the wider problems resulting from buyer power.

A major obstacle to developing more and better competition policy and making competition authorities take action against concentrations and buyer power is that competition policy is aimed at protecting the interest of the consumer, especially against high prices and low choice. This leaves the protection of suppliers outside current competition policy in many countries, with the exception of certain countries, such as South Africa.

The lack of competition policy instruments in the context of free trade and investment agreements and rapidly expanding supermarkets results in many problems such as:

- free trade and investment rules, which are wrongly based on the assumption of large numbers of competitors and not on just a few corporations trading in a sector, and which are removing government barriers to trade while not sufficiently removing private barriers to market access, especially for developing country producers
- lack of sharing of the benefits of trade and growing consumption markets, and concentration of profit margins in the hands of a few
- growing buyer power that suppresses prices paid to food processors, which has negative consequences throughout the whole food sector (examples are indicated in Chapter 3).

A major problem is that it is difficult to legislate with regard to the abusive relationship between supermarkets, and for that matter food processors, in the North and food or drink suppliers from the South.

Recommendations that are being proposed are:

- Tackling the abusive relationship between supermarkets in the North and food or drink suppliers from the South by using the United Nations Convention on Contracts for the International Sale of Goods (CISG) and the UN Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices.
- Protecting the interests of suppliers and their staff should be integrated in competition policy at national and EU level rather than only the protection of consumers.
- Developing countries should be able to seek remedies from the cartels under the home country jurisdiction of the TNCs involved in the cartel.
- The OECD Global forum on Competition and the International Competition Network should discuss new competition policy issues, such as buyer power, and establish cooperation agreements between competition authorities of developing countries.
- New competition policy should take account of the reality of current (international) markets as well as the specific needs of developing countries' markets and economies.
- Social and economic objectives could be part of new competition policy in many countries such as South Africa has done to promote small and marginalized entrepreneurs. On the other hand, other policy makers should be involved to solve the problems resulting from buyer power and concentration such as in the areas of employment, development and poverty eradication, labour conditions, social policy, environment and spatial development, trade and investment, and corporate social responsibility.
- Competition policy or its enforcement should not undermine valuable and sustainable collective defence mechanisms of small suppliers and corporate social responsibility initiatives that require cooperation among companies (and not be considered as a cartel).