

## Poultry likely to benefit from retail expansion in Central Europe

by CLIVE BEDDALL, leading food retail commentator and former editor of the UK magazine *The Grocer*



A significant new venue has joined the priority list of international exhibitions visited by UK food exporters - Budapest, the stylish and fast developing capital of Hungary.

For although Britain's top supermarket chain, Tesco, has long been convinced of the potential for growth in the Magyar state, and Bernard Matthews set up a production base there in 1993, it is only recently that ambitious British suppliers have also flown to the city by the Danube.

Yet that is a trend likely to hot up as Hungarian membership of the EU - expected in May 2004 - nears, and neighbouring states look east for more trade.

Add the fact that the central European retail sector is forecast to grow much more rapidly than western markets over the next four years, and you can see why so many enterprising retail and sales folk are heading for Heathrow.

According to IGD, the central research body for the grocery trade, levels of growth in Western Europe are expected to remain subdued, especially when compared to historical levels. Underlying factors such as reducing population growth, price deflation, the longer term trend of increased foodservice and the inability to expand hypermarket numbers in many European markets, are reducing the growth prospects for the big retailers.

But IGD statistics show that the picture is very different across the immature markets in Central Europe. Although currently the smallest grocery retail market in Europe, they predict that it will be the fastest expanding region over

the next four years growing by 26.4% - twice the level of any other in Europe.

The markets will increasingly resemble those of Western Europe, with a growth in the number of supermarkets, hypermarkets, discount stores and shopping centres. And the development of large formats and the process of internationalisation and concentration will continue.

As IGD emphasises, with many of the most powerful international retailers entering the region there will be a rapid development to structural maturity.

That was a point emphasised in Hungary, when the country's international food show, Foodapest, attracted more British executives than usual. True, UK

exhibits were thin on the ground, but the number of British sales folk trawling the aisles in search of new opportunities surprised and delighted the organisers.

For this was a fair that spectacularly mirrored much that is going on in eastern European manufacturing circles, with the important prospect of EU membership being swelled from 15 to 25, a point that is relished by the local business community.

There was an air of excitement among the stands as Hungarians, Bulgarians and Romanians alike eagerly grabbed the chance to talk to their western visitors about the days when EU levies disappear and a level trading playing field becomes more apparent.

Mind you, ask any Hungarian

food trader which western group has given most impetus to their ambitions and they'll quickly tell you - Tesco.

Since the group first went into Hungary, in 1994, it has skilfully built a chain of stores that, while taking western instore trends to the locals has also cemented successful trading links with many local suppliers.

Indeed, Hungary's food and drink providers believe their "homeland Tesco experience" will prove a trump card on the exporting front when they attain full EU membership next year.

As one food supplier put it to me: "Tesco has taught us a lot about quality, service and reliability. With 25 stores, it's our biggest local chain and one that we look up to."

But the Hungarians, like other suppliers in Eastern European states, know they face a tough fight for more UK business - even when their products attain full duty-free status.

Typical of the comments was one from Istvan Plesztowits, foreign trade director of the Kometa Meat Group, who told me: "A lot will depend upon the trading rules set by Brussels. Whatever we hope for, we are in the hands of the politicians."

And while it was clear that the fine foods/deli area was high on the agenda for the discussions at Foodapest, it was also obvious that the potential for trade in the mainstream poultry business ranked high among the priorities.



*Hungarian shoppers experiencing Western style food retailing. This edition looks at changes for the retail sector and the poultry industry likely to follow enlarged EU membership.*

Bernard Matthews set up a base over a decade ago, and while it has transformed its original production base to focus on turkeys, the locals predict that it will play an even greater role once Hungary attains full EU membership.

Although up-to-date statistics are often hard to come by in European states, figures being circulated in Budapest recently suggest Hungarian poultry consumption, at 22-23 kilos annually, is outstanding even by international comparison, and is higher than the EU average of 18.8 kilos per capita.

International poultry traders indicate that Hungarian product has compared well against EU product, although, traditionally they have been less successful in entering the frozen market in the EU as they have faced high competition from Brazil which has enjoyed lower cost benefits.

Having said that, one local producer I met in Budapest was hopeful that Brazil's traditional advantages in world markets would dissipate if they were forced to meet more stringent EU standards on items like the use of meat and bone meal in feed.

The local production scene, as presented by the executives of AMC, the country's Agricultural Marketing Centre, has some notable achievements to its credit. Since 1990 it has increasingly set its sights on the EU.

Typically, one of the largest producers, Hadju-Bet, has usually exported about 50% of its sales. Of its domestic business, 47% of sales have been further processed rather than raw whole chicken or parts.

This suggests that the market is fairly well developed compared to a lot of developing countries where further processed sales make up a much smaller percentage.

This group has invested in a brand programme that has helped it gain good market share and this suggests that consumers are affected by branding, again something that industry executives point out is not expected from a low-end market.

Traditionally, most of the product in the Hungarian further processed sector of the domestic market has been chopped and formed, although some whole muscle product is sold.

According to recent figures, about 50% of Hungarian domestic production is accounted for by producers Hadju-Bet and Babolna - handling some 25 million birds per year.

So what is the potential for producers in the EU to compete profitably in Hungary? One international trader told me: "The big challenge comes because Hungary has much cheaper labour and property costs. In addition, their grain costs are lower.

"Having said that, EU producers have a plus in that they are probably more sophisticated in further processing. But they will find it difficult to compete with local prices and the production knowledge will migrate.

## *"Suppliers look for chance to 'piggyback' Western European chains into the east"*

"In addition, the political picture across poultry will also be affected in the years ahead. As more product comes into western Europe from the new EU members, there will be more pressure on the EU to find ways to keep out Brazilian and Thai product."

But one possibility for Western, and British suppliers in particular, loomed large in Budapest - the chance to "piggyback" Western European chains into the east. In addition to Hungary, Tesco is also in Slovakia, Poland and the Czech Republic. Judging by the noises coming out of the chain's UK headquarters, its Eastern European ambitions have yet to be fully realised.

Recent statistics have suggested that the total number of hypermarkets in operation across the region will increase to over 418 from around 260 two years ago. Slovakia, according to IGD, will see the greatest percentage growth and Tesco will lead the development programme.

Hypermarket expansion in the Czech Republic will be led by Dutch giant Ahold, and Spar is also expected to consolidate its already strong position.

Significantly, in an obvious pointer for UK suppliers with sales ambitions, IGD says that the retailers who have performed best in the region are those that have

demonstrated sensitivity towards local traditions in their ranging, merchandising and pricing strategies. Echoing the words of many of the local pundits that I met in Budapest, the organisation says the winners will be those retailers who have the best core competencies; skill and scale in local markets will be the main criteria for success.

Meanwhile, another country that is increasingly being seen as an area for development among UK retailers is Bulgaria. It suffered a shattering economic collapse in 1996 and 1997 and inflation reached four figures. However, the situation has since stabilised.

With the prospect of future entry into the EU and a population that is only slightly below that in Hungary, many

significant big players in Western European retailing are not ruling out entry into the market.

In the past, grey economy, crime and the burden of tax and bureaucracy has held back the development of Bulgaria's retail sector. Few foreign retailers have entered the country and several have been deterred by the difficulty of finding an appropriate local partner.

However, international traders point out that Bulgaria offers the potential to act as a stepping stone into Turkey with its larger population and the important Istanbul market.

Meanwhile, all eyes remain on Tesco as it builds critical mass in Central Europe. IGD predicts that it will continue to improve the efficiency of its supply chain and capitalise on global sourcing - probably one of the most important features to watch for potential suppliers.

And, waiting in the wings is Wal-Mart - the Arkansas-based chain with ambitions to rule the world. It had a tough time when it entered Germany, but with Asda under its belt in the UK, it is believed to be looking hard at Eastern Europe.

Boasting one of the most efficient sourcing operations in world retailing, it is clearly not deterred from entering developing markets, as it

showed in China and South America.

Wall Street analysts say that although it was a late entrant into the food retailing business, there is nowhere on the global map that Wal-Mart would not enter.

It could be, of course, that Wal-Mart will follow recent trends and buy its way into Eastern Europe, perhaps by taking over an existing Western European chain which has a foothold in the area.

French group Auchan is rumoured to have turned down an offer from Wal-Mart in 1998, but in these days of mega deals anything is possible.

In the longer term, IGD says there should be room for four types of retailer in Central Europe - hypermarkets, in-fill supermarkets, discounters and convenience stores.

Significantly, more and more international traders are moving down the discount route, specialising in the lowest possible prices rather than the widest possible range. And while it's difficult to see scope for traditional poultry products in this sector, new lines with an accent on convenience could be attractive to Eastern European consumers. It all depends upon the production economics.

Hungarian government officials touring the Foodapest show were realists. They know that, given EU qualification more Western European companies will be looking to the region as an expansion area, given its low production costs.

But as the giants of western retailing head east, perhaps there will be a spin-off for local producers to piggyback the new players sourcing systems and sell in the opposite direction.

Yet, in a recent report IGD warned that retailers operating in Central Europe face the risk of a slowdown in consumer spending, caused by a tightening of economic policy in order to fulfil the criteria for EU membership. In fact, the region is likely to experience rising inflation as a result of joining the EU.

Nevertheless, at the moment, the region has high priority in the future sales strategies of a wide range of food suppliers, not just poultry producers. But for domestic traders in potential new EU member states, even though they know that adapting to the new rules will be a challenge, May 2004 cannot come fast enough.

# EU poultry industry faces biggest expansion to date

POULTRY meat production in the EU is set to rise by 17 per cent next year when 10 more states formally accede to membership.

The historic agreement reached at the Copenhagen Summit in December takes effect on 1 May 2004, and will see the largest expansion of the EU in terms of individual states since its original formation. Table 1 lists all 10, with poultry production figures for 2001.

Total output by the new 10 stood at just under 1.6m tonnes in 2001, and will take total EU poultry production past 10m tonnes for the first time.

The majority of the new members are relatively small in terms of both human and poultry populations, but there are two which could have a significant impact on EU poultry markets - Poland and Hungary. A third, the Czech Republic, will make a contribution of around 2% to total production in the expanded EU (fig 1).

The other seven combined will only account for 2% of the EU total after May next year.

These new members have great potential for expansion, with the advantage of low production costs to help them compete against established EU industries. Both Poland and Hungary have been expanding production in recent years and are involved in exports.

Poland in particular has already been increasing its exports to the EU after the recent introduction of the zero import tariff as a prelude to membership. These exports have been taking the place of those to the FSU (former Soviet Union) where demand has declined.

However, with total exports of 37,000 tonnes in 2001, the Polish industry is still a relatively small player within the EU. Total exports by all EU countries, to destinations both within and outside the EU, came to 2.5m tonnes in 2001.

Domestically Poland is likely to run into problems with a slackening in demand for poultry meat. Recent rises in domestic consumption have been fuelled by worries over BSE in beef and competitive pricing against other meats. However, a weakening in the price of pork - highly popular in Poland - should arrest its substitution by poultry. Output of poultry in Poland had increased by 50% over the five years to 2001.

Hungary increased its output of poultry by almost a quarter last year but the industry claims that there is no real cause for concern. Consumption is steadily rising and is expected to keep pace with supply in the longer term.

Exports have always featured strongly for the Hungarian

Table 1

## Output of poultry meat ('000 tonnes)

	10 new EU members from May 2004	
	2000	2001
Poland	626	620
Hungary	414	512
Czech Rep.	215	219
Slovakia	90	92
Slovenia	68	68
Cyprus	35	35
Lithuania	25	28
Latvia	7	9
Estonia	7	7
Malta	6	6
<b>Total-10</b>	<b>1493</b>	<b>1596</b>
<i>Current EU-15</i>	<i>8793</i>	<i>9121</i>
<b>After 2004:</b>		
Romania (2007)	261	295
Bulgaria (2007)	100	100
Turkey*	595	618

\*not yet agreed

poultry sector and account for about a fifth of production, but total exports have changed little over the last five years.

The EU will have three years to assimilate these new arrivals before another two states, Romania and Bulgaria, become members in 2007.

Romanian poultry output is around 300,000 tonnes a year, and that of Bulgaria about 100,000 tonnes. Yet to be offered a firm date for accession is Turkey, with a poultry industry of similar size to Poland.

## Russia puts the squeeze on poultry trade

PROBLEMS could lie ahead for world export markets for poultry with the news that Russia has drawn up plans to impose a tough new quota system to restrict imports of meat.

Under the scheme, beef and pork would be subject to swingeing import tariffs (of up to 80%) for imports above the quota limits, while poultry imports would be restricted to the amount of the quota and no more. Even those poultry imports within quota would be subject to a 25% tariff.

At present the proposed quota for poultry meat stands at 1.05m tonnes, compared with total poultry imports in 2001 of 1.4m tonnes, so someone stands to lose 350,000 tonnes of annual export trade.

At present the US dominates the market with exports to Russia of 1.07m tonnes in 2001 - virtually the same as the amount of quota that is planned to be offered.

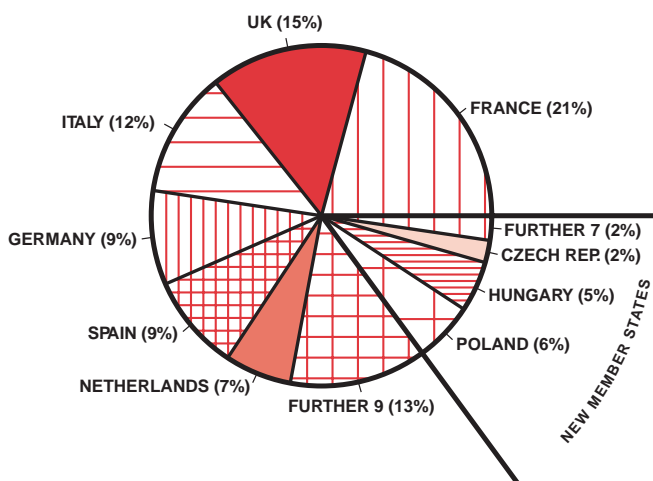
It is feared that the US, whose chicken legs are always competitively priced and favoured by the market, would mop up almost the entire allocation.

The main casualties could be Brazil and the EU, with exports to Russia of 94,000 and 193,000 tonnes respectively in 2001. France, Germany, Belgium, the Netherlands and the UK all send significant quantities to Russia.

Under the new regime as currently proposed, the EU may then not just have to find alternative destinations for its current exports to Russia, but may also find itself a target for the extra Brazilian product also looking for a new home.

Fig 1.

## Poultry meat output in the EU from May 2004



## Italian flu back on the rampage

THE renewed outbreak of avian influenza in Italy had claimed nearly a million birds (broilers plus layers) by the end of 2002.

The toll of birds culled had passed 900,000, and the disease was approaching epidemic proportions once more, raising concerns over the immediate prospects for the Italian industry.

Movement of poultry has been banned in Lombardy and Veneto, where more than two thirds of

the industry is located, and a mass vaccination programme was begun before Christmas.

Two years ago, in the last outbreak, the total number of birds slaughtered reached 14 million but this time the virus is believed to be more virulent and resistant to cold.

Italy is the third largest poultry meat producer in the EU (after France and the UK), with an output of 1.3m tonnes in 2001.

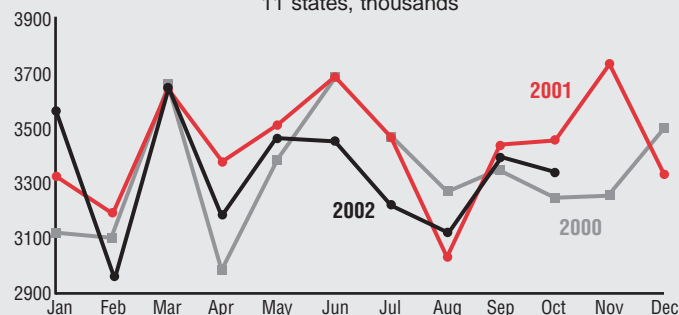
# MARKET TRENDS

## Feed ingredient prices

National currency/tonne	Current (Dec)	3 months ago (Sept)	6 months ago (June)	9 months ago (Mar)	Year ago (Dec)
<b>US wheat (\$)</b> soft red winter	149	153	118	114	116
<b>US maize (\$)</b> No 3 yellow corn	108	111	99	90	95
<b>US soya (\$)</b> No 2 yellowbeans	225	223	196	180	176
<b>EU feed wheat (£)</b> UK - national average	58	57	60	71	77
<b>EU feed wheat (€)</b> Rotterdam	117	111	115	124	131
<b>EU feed wheat (€)</b> Hamburg	105	102	108	119	119
<b>EU maize (€)</b> Bologna	138	130	149	137	130
<b>S American soya (\$)</b> Argentina/Brazil	223	250	207	157	192

## EU female parent chick placings

11 states, thousands



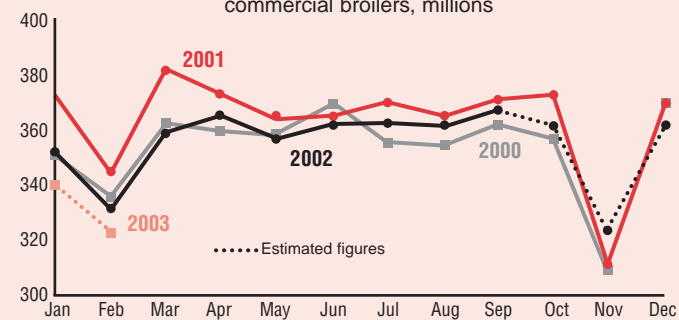
## EU broiler prices

€/kg liveweight (except UK & Denmark)

	Current (Dec)	3 months ago (Sept)	6 months ago (June)	9 months ago (Mar)	Year ago (Dec)
<b>Belgium</b>	0.51	0.84	0.71	0.65	0.47
<b>France</b>	0.84	0.86	0.86	0.88	0.89
<b>Germany</b>	0.70	0.71	0.72	0.72	0.74
<b>Italy</b>	0.88	0.85	0.72	0.79	0.64
<b>Netherlands</b>	0.67	0.67	0.68	0.71	0.75
<b>Spain</b>	0.74	0.99	0.80	1.07	0.79
<b>Denmark (DKr)</b>	4.11	4.11	4.41	4.61	4.76
<b>UK (£)</b>	0.48	0.48	0.48	0.49	0.50

## EU chick placings, 11 states

commercial broilers, millions



## EU average wholesale prices

per/kg, whole oven-ready chicken

	UK (€)	Germany (€)	Italy (€)	France (€)
Jan '02	1.65	1.41	1.05	1.60
Feb	1.58	1.39	0.96	1.59
Mar	1.59	1.38	1.20	1.50
Apr	1.60	1.38	1.17	1.50
May	1.56	1.38	1.20	1.59
Jun	1.52	1.36	1.19	1.64
Jul	1.53	1.35	1.56	1.70
Aug	1.54	1.32	1.59	1.70
Sep	1.55	1.32	1.45	1.69
Oct	1.56	1.31	1.45	1.58
Nov	1.54	1.31	1.45	1.55
Dec	1.53	1.38	1.45	1.55

## French industry faces up to tough conditions

FRANCE is expected during 2002 to have shown a trade deficit in poultry meat with the rest of the EU for the first time.

According to the French organisation Ofival, exports within the EU have dropped by more than 17%, while imports have risen slightly by over 2%. France remains a net exporter when trade with third countries is taken into account.

Adding to the industry's difficulties is a reported 3% fall

in domestic sales of poultry meat, so hopes are pinned on a restructuring plan for the industry which was put together by the French Ministry at the end of last year.

The plan aims to tackle the twin problems of current over capacity, and the long-term changes in the market - essentially the winding down of export subsidies to third countries and the pressure on the home market from cheaply-produced imports.

## Exchange rates

	Current (Dec)	3 months ago (Sept)	6 months ago (June)	9 months ago (Mar)	Year ago (Dec)
<b>£ / €</b>	1.54	1.58	1.55	1.59	1.59
<b>\$ / €</b>	1.03	0.97	0.91	0.89	0.90
<b>£ / \$</b>	1.58	1.53	1.46	1.41	1.44



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