

COMPETITIVENESS OF SLOVENIAN AGRO-FOOD SECTOR**KUHAR ALEŠ**

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ABSTRACT

The main objective of this article is to present an overview of the Slovenian food industry economic development in the period before the Slovenian EU accession and the first five years of the EU membership. The accession to the EU was certainly the most comprehensive change of economic environment since the state gained its independence. Nevertheless, already during the pre-accession period the changes intensified restructuring processes and increased pressures to the business performance of the sector. The agro-food industrial complex, however, is among the sectors of the acceding economies for which EU enlargement traditionally brings the most radical changes. Price level and cost differences, hardly comparable production structures, but mostly disparities in types and comprehension of the economic policies required large adjustments and caused notable economic pressures. Based on a framework of economic indicators the paper tries to answer some of the most recurrent questions related to the restructuring process of Slovenian food industry in the last decade. First we present past sectoral business performance using the appropriate mezzoeconomic accountancy indicators, whereas in the central part of the paper four key restructuring determinants are analysed and commented. The determinants are formulated into the four relevant questions dealing with cost-price developments, relations in the Slovenian agro-food chain, developments of the international trade and trends in the budgetary transfers to support competitiveness. Results confirm that the economic restructuring which had been hindered in the Slovenian food industry during the last decade has been triggered radically after EU accession. This brought to the termination of favourable economic conditions in the highly protected domestic market and deteriorated radically the business performance, and only those food companies which will restructure proactively will sustain in the EU markets.

Keywords: EU accession, restructuring; Slovenia; food processing industry

INTRODUCTION

Accession to the European Union has triggered substantial changes in the business environment of Slovenian food processing industry which intensified restructuring processes and increased pressures to the business performance of the sector. The agro-food industrial complex is among the sectors for which EU enlargements traditionally brought radical changes in the economic environment. Price level and cost differences, hardly comparable production structures, but mostly disparities in types and comprehension of the agriculture policies required large adjustments and caused notable economic pressures (EL-AGRAA, 1994). The largest European Union (EU) enlargement in May 2004 involved ten countries, most of which just completed their transition to market economy, and another two countries with similar attributes – Bulgaria and Romania – joined the Union in 2007, Croatia in 2013. The enlargement of 2004 differs from the previous ones since the margin in economic prosperity is notably larger compared to any previous enlargement. These disparities bring both distinct challenges and opportunities for the new member states and for the incumbent countries of the Union (ARTIS ET AL., 2006). However, neither the scale of the last EU enlargement nor the combination of the patterns and characteristics of agriculture, food processing, and rural economies are comparable with the past enlargements (MACOURS AND SWINNEN, 1997). Therefore, the evaluation of EU enlargement and its implications for the agro-food sectors has drawn considerable research attention.

There are several studies evaluating in a rather detailed manner the EU accession effects for the sectors of Slovenian agriculture (ERJAVEC ET AL., 1997; BOJNEC AND MÜNCH, 2001). The Slovenian agro-food industry has also been investigated; however focused studies are few (e.g. ERJAVEC AND KUCHAR, 2000; OECD, 2001).

MATERIAL AND METHOD

There is no generally accepted theoretical framework economic literature, for sectoral competitiveness; similarly there is no consolidated terminological definition. The concept of competitiveness is clearly multidimensional and therefore it is difficult to deal with theoretically as well as empirically. Some of the leading authors (e.g. TRAIL AND DA SILVA, 1996; LALL, 2001) therefore suggest a composite approach specifically designed according to the focus of analysis.

In a strict sense, there is no specific research methodology applied in this paper, however based on a framework of economic indicators we try to answer some of the most recurrent questions related to development of Slovenian food industry in the last decade. Four questions were put under the research scrutiny: 1) Is food industry facing cost - price squeeze?; 2) Who is creaming in the food chain?; 3) Are the trends in international trade with food surprising?; 4) Has the budgetary support to the sector stimulated competitiveness?.

The paper is structured accordingly to the elaborated four questions. Using data acquired from different official sources a series of economic indicators is calculated to elucidate the determinants of Slovenian food manufacturing sector development. In the first part of the paper the situation in the sector is presented using indicators of business performance, efficiency and profitability whereas in the central part, the article tries to answer the elaborated questions and comment competitiveness determinants.

RESULTS

Economic performance of the agro-food sector

In Slovenia the agro-food sector represented 1.46% of value added in GDP in 2010 and 1.65 % in the total employment (SORS, 2012). According to the value added contribution in total manufacturing food industry is the third largest sector in Slovenia. However, in the last years the importance of food industry is declining in all macroeconomic indicators, since in the year 1998 the food industry contributed about 2.8% of Slovenian GDP and almost 2.5% of total employment. Industrial production of food manufacturing has mainly decreasing after the year 2000. Until the year 2003 the production volume somehow stagnated, but in 2004 volume dropped for more than 10% and then remained stable until 2007. In the year 2011 the food manufacturing was at about 10% below the level of 2004 and beverage sector at about 15% lower. Unfavourable conditions in business performance of Slovenian agro-food sector are discernable also from trends in productivity and value added per employee. In the year 2000 agro-food industry attained about 25% better productivity than average manufacturing and about one fifth higher value added per employee. However, the trends in the following years were constantly negative and in the year 2004 the value added per employee in food industry fell below the average of manufacturing (index for 2005 = 92.2), whereas productivity was still slightly above the manufacturing average (2005 = 101.5). In the following years the indicators fell again, where the productivity was still one tenth higher than on average of the processing sector,

whereas the VA/employee was almost one tenth below the same average. Consequently with worsening of productivity and value added creation, also profitability indicators have dropped, however with oscillating patterns in the last years. Trends of the profitability in the period between 2000 and 2007 measured as return to sales (ROS). In the pre-accession period the ROS was around 3.4%, but after the accession the indicator fell to negative value. Since then the results were constantly and steadily improving in order to reach 4.2% in 2007 which was higher than the average of the processing industry in Slovenia (ROA 2007=3.9%). However, after that, the indicator dropped again considerably, particularly due to the excessive loss in the beverage sector.

The brief overview of some key indicators of business performance above shows rather apprehensive changes in Slovenian agro-food sector. The sector has moved from one of the most prosperous industrial activities in Slovenia during the last decade to the average.

Is food industry facing cost - price squeeze?

Price trend comparison at different levels of measurements reveals general information about the economic environment of an industrial sector. *Figure 1* shows movements of price indices for agricultural inputs, producer prices of food, beverages and tobacco, the producer prices of the food processing industry aggregate and import prices of food in the period 2000-2012. The food retail price index generally fluctuates around the inflation rate if there is no radical structural change in the economy. After the year 2004 food retail prices in Slovenia started to lag behind inflation due to the EU accession. Further the retail prices were falling also in the subsequent period. After that lowest point in 2006 slight strengthening is present until the 2007, when the constant trend of food price increase started. In the last months of the 2011 the food prices were at about 30% higher than in 2005 and more than 50% higher than in 2000.

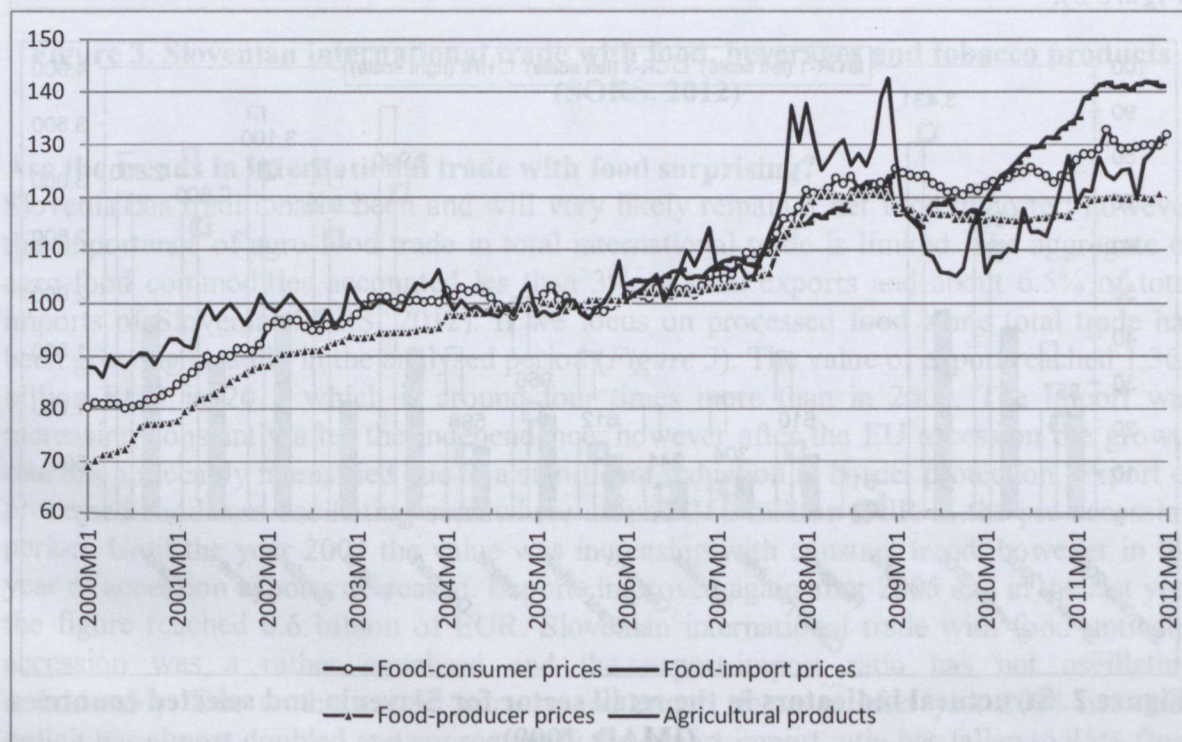


Figure 1. Indices for consumer prices of food, producer prices of food, import prices of food and agricultural products between 2000 and 2012; 2005=100 (SORS, 2012)

In comparison with year 2000 prices of agricultural commodities were lower by 12 % in real terms. In the subsequent years the real price started to increase and then two price

peaks of the decade were reached, one in end of 2007 and the second one in the first years of 2009, but immediately after the peak the prices started to fall sharply and in the summer 2009 almost reached the average level of 2005. In the following years the prices of agricultural commodities were growing with fluctuating trend, however in the January 2012 the prices were again 30% above the 2005 average. Prior the year 2005 the food producer prices were growing faster than consumer prices and agricultural prices, since they compensate 30% in the first five analysed years. Latter we can observe a significant push-up in the period of agricultural inflation (Y2007), however the price increase was not as high. After that a considerable lagging of the producer prices behind the food consumer prices is evident, which is being explained by the growth of the food import prices. The latter increase by impressive 20 percentage points in the last two years of analysis.

From the price trends and parities revealed above one can not firmly state radical cost-price squeeze for the agro-food manufacturers in Slovenia during the analysed period. Especially the sub-sectors with intensive agriculture input dependence (e.g. dairy, meat, bakery) could benefit from evident improvement of price parity, however this is not confirmed by business performance. A great part of potential positive price-cost development is however absorbed within the retail sector.

Who is creaming in the Slovenian food chain?

Today the food retailers are not only passive intermediates between producers and buyers but a dominant determinant in the agro-food chain. Domination of retail trade in is a global phenomenon (DOBSON ET AL., 2003). Slovenia here is no exemption and it ranges among the European economies with the highest level of concentration in food retailing sector (JUHASZ AND STAUDER, 2005). Already a basic analysis of data reveals significant trends (Figure 2).

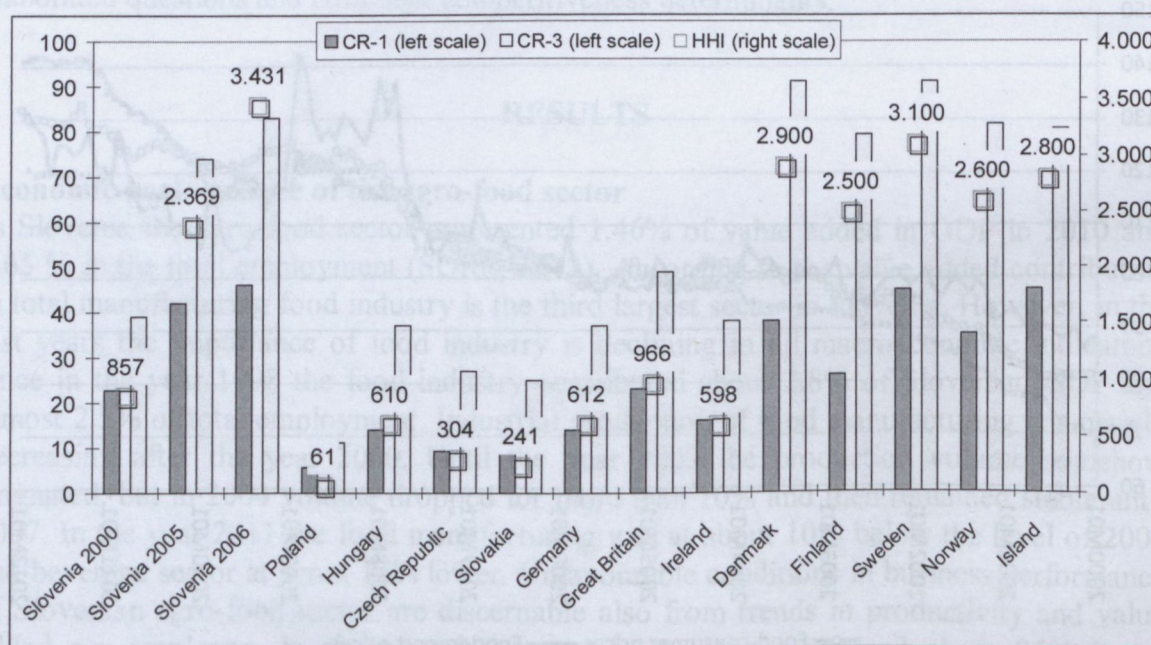


Figure 2. Structural indicators in the retail sector for Slovenia and selected countries (IMAD, 2009)

The data show enormous growth of the HHI value in the period between 2000 and 2006 since the index quadruplicated. In the last year the HHI reached the value of 3.431, a considerably higher value than estimated for Sweden and Denmark which have the amongst the highest HHI in Europe. Also according to the other indicator of the market

structure – namely the Concentration ratio (CR); Slovenian retailing sector is highly saturated. In 2006 the largest Slovenian retailer contributed 46% of the total sectoral revenue, whereas the first three retailers contributed as much as 83%. Both figures are among the highest in Europe. Simultaneously with the retail sector concentration growth also the nature of the supply chain relations has changed considerably. Retailers are imposing many other contractual and operational practices that negatively influence suppliers. Unjustified costs are carried onto agro-food producers which deteriorate their business performance and are of benefit to retailers.

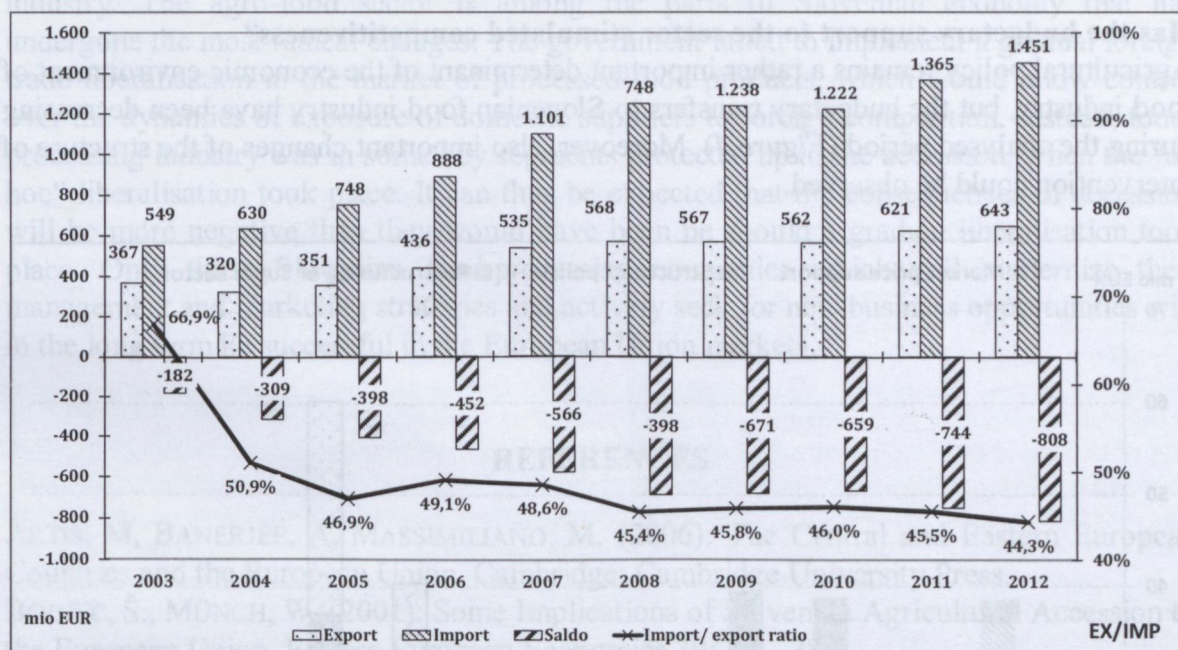


Figure 3. Slovenian international trade with food, beverages and tobacco products (SORS, 2012)

Are the trends in international trade with food surprising?

Slovenia has traditionally been and will very likely remain a net food importer; however the importance of agro-food trade in total international trade is limited. The aggregate of agro-food commodities accounted less than 3% of total exports and about 6.5% of total imports of Slovenia (SORS, 2012). If we focus on processed food alone total trade has been growing steadily in the analysed period (Figure 3). The value of export reached 1,365 billion EUR in 2011 which is around four times more than in 2000. The import was increasing constantly after the independence, however after the EU accession the growth rate has noticeably intensified due to a significant reduction in border protection. Export of processed food was oscillating somewhere around 350 million EUR in the pre-accession period. Until the year 2004 the value was increasing with constant trend, however in the year of accession exports decreased. Exports improved again after 2005 and in the last year the figure reached 0.6 billion of EUR. Slovenian international trade with food until the accession was a rather equalised and the export-import ratio has not oscillating considerably. Due to the import increase and export decrease after year 2004 net trade deficit has almost doubled and consequently the export-import ratio has fallen to 45% from the levels above two thirds in the pre-accession period. The Slovenian food market has been highly protected until the EU accession, since for the majority of food groups the effective tariff rate in the pre-accession period has been fluctuating around 10%. From the evaluated import protection one could anticipate the effect of the inclusion to the internal market of the European Union on Slovenian food trade. The effect of “trade creation”

appeared, which is described as a basic effect of trade union (EL AGRAA, 1994).

Also on the export side of the Slovenian trade balance the EU accession effects might be expected from the regional structure of trade, since not less than 60% of the food exports was realised on the markets of Former Yugoslavia. With these countries Slovenia signed preferential trade agreements which made food products competitive in comparisons with other imported products. However, after the accession the trade agreements were abolished. This has immediately resulted in export decrease, but the export switched to the EU markets. In the year 2011 the share reached almost two thirds of the total exports.

Has the budgetary support to the sector stimulated competitiveness?

Agricultural policy remains a rather important determinant of the economic environment of food industry, but the budgetary transfers to Slovenian food industry have been decreasing during the analysed period (Figure 4). Moreover, also important changes of the structure of intervention could be observed.

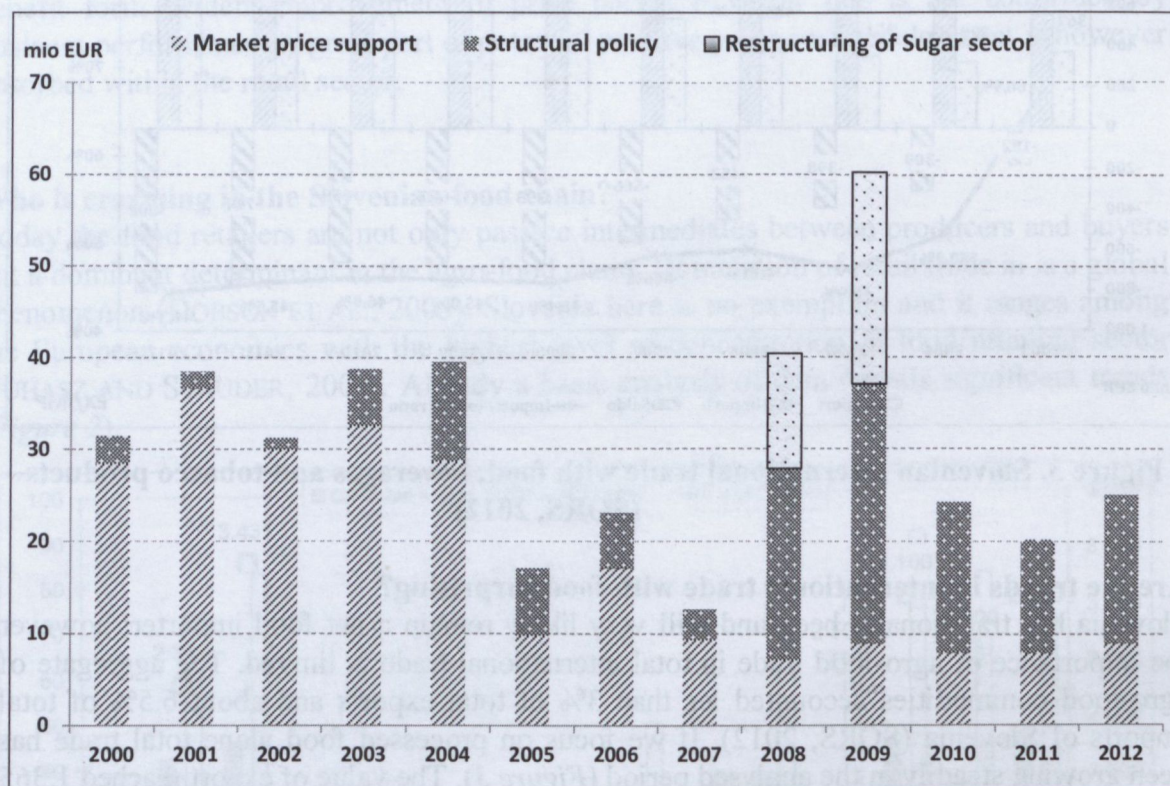


Figure 4. Budgetary outflows for agro-food sector in Slovenia (AIS, 2012)

The total budgetary transfers are divided into Market interventions and Structural policy measures. The first part includes mainly transfers to exporting food enterprises (export subsidy) and the Proportion of this type of support in total transfers was around 90% until 2003, when the share of structural measures increased, but also the value of export subsidies decreased considerably. The export subsidies in combination with bilateral trade agreements had clear distortive implications on competitiveness of Slovenian food sector and importantly influenced the structure of exports. Despite the considerable amount of budgetary transfers to Slovenian food sector, majority of them has not been intended for long term competitiveness improvement, but rather to stabilise domestic agricultural markets and to correct price distortions. Only in the last period the share of structural measures increased, however processes to build sustainable economic competitiveness are demanding and long lasting.

CONCLUSIONS

The economic restructuring that had been hindered in the Slovenian food industry during the last decade has been triggered radically after EU accession which brought to the termination of favourable economic conditions in the highly protected domestic market. Competition from the internal market, but more significantly the reduction of export competitiveness due to the abolition of free trade agreements has caused an important long term deterioration of economic performance in almost all sub-sectors of the Slovenian food industry. The agro-food sector is among the parts of Slovenian economy that has undergone the most radical changes. The government failed to implement a gradual foreign trade liberalisation in the market of processed-food products, which would allow control over the dynamics of exposure of domestic suppliers to foreign competition. Instead, food-processing industry was in some key segments protected up to the accession, when the "ad hoc" liberalisation took place. It can thus be expected that the consequences of accession will be more negative than they would have been should a gradual liberalisation took place. Only those Slovenian food-processing companies which will modernize their management and marketing strategies and actively seek for new business opportunities will in the long term be successful in the European Union markets.

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