

## PRICES AND COMPETITION IN SWEDEN'S FOOD MARKET

The food industry in Sweden employs about 10 per cent of the total labour force in manufacturing. In terms of value added the food sector is the second largest in Sweden. Moreover, as food products make up a considerable item in the basket of consumer goods (about 14 per cent in 1998), the development of food prices is highly important for UNDI<sub>X</sub> and CPI inflation.

### EFFECTS OF EU MEMBERSHIP

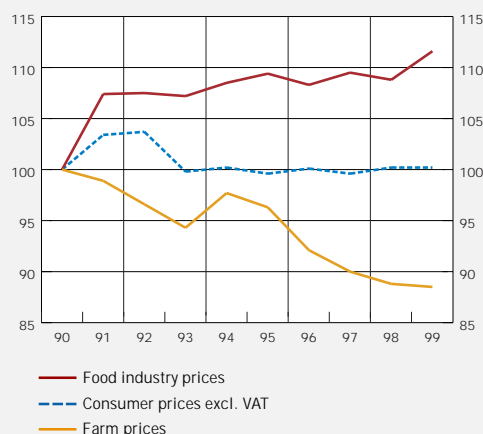
Food prices have fallen during the 1990s. Excluding VAT, however, the level rose by an average of 0.9 per cent a year from 1992 to 1999. Among EU countries, between 1990 and 1997 Sweden had the second slowest price trend for food. Even so, the level of food prices in Sweden is still about 19 per cent above the EU average. In the Nordic area, however, the price level is higher in Denmark and Norway than it is in Sweden.

EMU membership from January 1995 entailed considerable changes in the Swedish food industry's competitive situation and the development of food prices. It has been estimated that without the changes in agricultural policy when Sweden joined the EU, food prices in Sweden would be 6.3 per cent higher.<sup>34</sup> The price effects of EU membership differ markedly, however, between product groups. Prices of beef and beef products, for example, have fallen about 20 per cent, whereas EU's higher import tariffs on rice led to a 53 per cent increase in the price of rice during 1995. EU membership also implied free trade and competition in both the Swedish and the European market, which involves considerable changes in conditions for the Swedish food industry. With few exceptions, this sector had lacked access to markets abroad prior to EU membership.

34. HUI (1997), *Dagligvarupriser i de nordiska huvudstäderna efter Finlands och Sveriges EU-inträde* (Everyday goods prices in the Nordic capitals after Finland and Sweden joined the EU).

# PRICES AND COMPETITION IN AGRICULTURE, PRIMARY PRODUCTION

Figure B13. Agricultural and food product prices at different stages.  
Index: 1990=100



Note. The farm price series does not include income-enhancing support such as direct subsidies for acreage and livestock. For 1999 the data are the average for the first three quarters.

Sources: National Agriculture Administration and Statistics Sweden.

The effects of agricultural policy on consumer prices are indirect because the controls mainly apply to early stages of production. The agricultural sector was deregulated in Sweden in 1990, accompanied by a five-year period of support for adjustments, including income support to facilitate the transition. In the process of adapting to EU agricultural policy, the income support was replaced by acreage subsidies and the system of guaranteed wind-up prices was prolonged. EU membership from 1995 meant a changeover to the EU support system, with new market regulations as well as some new structural and regional measures, for example.

In order to make European agriculture more competitive, in 1992 the EU had approved a reform that resembled what had been done in Sweden in 1990. The agricultural prices that are set politically were reduced, offset by direct compensation to farmers. Further steps in this direction are being discussed at present under Agenda 2000. The aim is to make EU agricultural products more competitive in world markets at the same time as compensation to farmers makes it possible to maintain production in Europe. The Riksbank estimates that the planned reform will have a downward effect on CPI and UND1X inflation in Sweden of 0.1 percentage point in both 2000 and 2001.

Prices for agricultural products have fallen almost continuously in the 1990s on account of increased competition in the domestic as well as international markets (Fig. B13). Total compensation per unit, which also includes support of various kinds, is currently on the same level as in 1990, which implies that support has increased. Farm profitability has improved in general in recent years as a result of cost cutting as well as increased support.

### PRICES AND COMPETITION IN FOOD PROCESSING INDUSTRIES

Farmers sell their products via wholesalers in the food sector. Food prices are therefore affected by costs for further processing, distribution, marketing and profit margins, as well as by competition from imports. Wholesale prices have been broadly unchanged in the 1990s even though the prices paid by wholesalers to farmers have fallen more than 10 per cent. This is probably one of several factors behind the positive development of profits in the food sector and it raises questions about competition there (Fig. B14).

Prices paid by producers for imported food products have risen in the 1990s at an annual rate of over 5 per cent; the trend is mainly explained by the depreciation of the krona after the move to a flexible exchange rate in November 1995. The rising import prices have not, however, spread to home market prices to any appreciable extent.

The food industry is labour-intensive but successive rationalisation has reduced the number of employees and thereby tended to hold total wage costs down. The move towards a less labour-intensive food industry is another explanation for the strong increase in profit shares.

The structure of food processing, like primary production, has changed substantially in recent years. The number of production units in the food industry was reduced by 40 per cent in the 1970s, mainly in connection with the introduction of new technology for processing and packaging. As this decline has continued, the sector has become more concentrated than before.

Agricultural cooperatives have a dominant position, with about 45 per cent of the food industry's total output in Sweden. Concentration is particularly high in certain activities. About 60 per cent of food industry turnover and employment (in persons) comes from operations such as slaughtering and meat processing, dairying, and milling and bakeries. In the largest of these groups, slaughtering and meat processing, Lantbrukskooperation (Association of Agricultural Cooperatives) had a market share of 78 per cent in 1996. The second largest group, dairying, was dominated by Arla and Skånemejerier, which are also agricultural cooperatives. In milling and bakeries, 45 per cent of grinding was owned by the Cerealia Group through Nord Mills and Kungsörnen.

Figure B14. Food industry's gross operating surplus.  
Percentage of value added at factor values



Source: Statistics Sweden.

Competition seems to have increased in recent years in the domestic market as well as in the EU and international markets. This is mirrored to some extent in the fact that about 30 per cent of the Swedish food industry is now in foreign hands. Still, the combination of a high degree of concentration throughout the industry and rising profit shares does raise the question of whether competition is adequate.

While tariffs on other manufactured products have been steadily reduced or abolished entirely in the postwar period, they are still relatively high for agricultural and food products. The WHO negotiations that are being initiated in December 1999 will probably cover agricultural products, which in time should lead to some downward pressure on agricultural and food prices.

#### COMPETITION IN SWEDISH EVERYDAY TRADE

The everyday food trade comprises wholesaling (selling to those who are not final consumers, i.e. retailers and caterers) and retailing. These two blocks are integrated in Sweden. In the 1990s retailing efficiency has been improved by reducing stocks and extending transportation (which is cheaper than holding stocks), as well as through increased price pressure from abroad, for example. The gains in efficiency should have been sufficient to result in lower prices than has been the case.

The operators in everyday trade are two voluntary chains (ICA and Dagab), the Cooperative Union & Wholesale Society (KF), other retail chains and independent traders. The three largest distributors controlled 68 per cent of the market in 1998. Their dominant position has probably been aided by regulations on new establishments in the Planning & Building Act.<sup>35</sup> Future shifts between the blocks' market shares may occur from takeovers and mergers such as the coming combination of D&D Dagligvaror with Hemköp, which belong to the Axel Johnson Group.

As a result of structural changes, the number of enterprises in everyday trade has decreased successively, from 10,000 in 1976 to 7,000 in 1996, and distribution facilities have become larger. The number of relatively small everyday retailers has also declined, by more than half from 1976 to 1996, and the survivors have expanded and been relocated outside city centres. New service and traffic outlets have sprung up at the same time as hypermarkets are taking a growing share of total turnover. The latter's share rose from 57 per cent

35. OECD (1998) *Economic Survey*.

in 1976 to 78 per cent in 1996.<sup>36</sup> An important factor for retail pricing appears to be local competition.<sup>37</sup> Internet trade may also provide competition in the future. A study by the Wholesale & Retail Research Institute in 1999 found, however, that food prices in internet trading were not lower than in traditional retailing.

#### CONCLUDING COMMENTS:

##### WHY ARE PRICES SO HIGH?

Consumer prices for food have fallen in the 1990s as a result of decreased VAT but their level is still internationally high. Many of the factors that may previously have impeded an equalisation with the price level in other countries have now been removed. The food industry can no longer be said to be protected from international competition and competition from imports has grown. Employment in agriculture and the food industry has declined, accompanied by cost cutting and increased productivity. Under these circumstances it is surprising that prices have not fallen more.

The picture in terms of costs, prices and competition is not uniform. Farm prices have fallen in the 1990s and the means of production have become more costly. However, the EU support system has compensated farmers for the decline in their product prices and farm profitability has risen. Moreover, changes in the structure of the agricultural sector have contributed to the rationalisation of costs.

Prices for semi-processed food products have fallen and increased trade has accentuated competition. Notwithstanding the increased competition, the degree of concentration is high in all stages of processing. Prices have risen, moreover, in later stages of processing and this is reflected in increased profit margins, for instance. Everyday trade is concentrated to a few operators and downward price pressure is still only modest from alternative outlets in the form of internet trade and diversified ownership. Another factor, often overlooked, behind the price difference between Sweden and continental Europe is the relatively high wage level in the Swedish food industry and retailing. Finally, a part of the price difference comes from VAT, which is higher in Sweden than in most other EU countries (12 per cent for food in Sweden as against the EU average of about 7 per cent).

36. *När mat kommer på tal* (When talk of food crops up) (1998), Statistics Sweden.

37. Asplund, M. & Friberg, R. (1998), Links between competition and inflation, *Quarterly Review* 3, Sveriges Riksbank.

Growing price pressure can be expected in future as a result of internet trade, increased cross-border trade, the WTO negotiations on agricultural products and possibly a harmonisation of VAT rates. A countering factor is the limited competition, which may tend to delay an adjustment of prices to the European level.