Direct Investment Is Primary Strategy To Access Foreign Markets

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Firms use a full range of strategies to access foreign markets—imports and exports, direct investment in foreign food processing and distribution firms, joint ventures, and international licensing arrangements. Foreign direct investment is the major way large food firms reach international markets. In fact, sales from foreign affiliates of U.S. food processing firms were four times larger than U.S. exports of processed foods in 1994. At the same time, American affiliates of foreign firms sold more than $45 billion in processed foods in the United States, twice the level of U.S. imports. U.S. participation in foreign direct investment has grown steadily over the last decade both in U.S. investment overseas and in foreign investment in U.S. food processing, distribution, and retailing.

Foreign Direct Investment Growing Steadily

Foreign direct investment refers to investment in a foreign entity or affiliate in which a parent firm holds a substantial, but not necessarily a majority, ownership interest. Foreign direct investment is an ownership of assets in an affiliate by a foreign firm for the purpose of exercising control over the use of those assets (unlike foreign portfolio investments, which is more of a passive management role and does not seek control over decisionmaking for the firm).

The U.S. Department of Commerce defines foreign direct investment as ownership of 10 percent or more of a firm by a foreign firm, and no other firm has as large a share. However, the 10-percent ownership is only a minimum. Most affiliates are majority owned, with foreign parents owning at least half of assets. In 1993, for example, 83 percent of U.S. food processing affiliates in foreign countries were majority owned. Conversely, 98 percent of foreign-owned affiliates in the United States were majority owned by their foreign parents.

Sales from all U.S. food marketing affiliates abroad totaled $132.5 billion in 1993, while sales from foreign-owned food marketing affiliates in the United States were $124.3 billion. Sales from U.S. affiliates abroad were slightly higher than foreign-owned affiliates' sales in the United States throughout 1982-93 (tables 1 and 2).

Most foreign direct investment occurs by acquisition of or merger with existing companies rather than by construction of new facilities. The country receiving foreign direct investment gains from the investing firm's knowledge in technology, marketing, management, finance, and information services. There are obvious gains in employment and economic activity from investment in new facilities. But even when foreign direct investment occurs by acquisitions, the parent firm typically upgrades the acquired firm's production processes and equipment, quality and environmental controls, procurement practices, packaging, and distribution systems. If production increases sufficiently, net employment increases along with improved labor productivity.

Parent firms also frequently buy a company producing a leading brand in a foreign country to achieve the competitive advantages of owning a leading brand in a new market. Examples are Grand Metropolitan (UK) buying the U.S. firm Pillsbury, and Philip Morris buying Europe's largest confectionery firm Jacob Suchard. By acquiring an existing firm or brand in the host country, the parent firm avoids having to build a new plant, thereby achieving

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Table 1
U.S. Foreign Direct Investment Abroad Is Centered in Food Manufacturing...

Sector	Sales by U.S.-owned food marketing affiliates abroad 1982	1987	1992	1993	Share of 1993 total affiliate sales
	Billion dollars				*Percent*
Food manufacturing	39.0	50.1	89.2	95.8	72.3
Food wholesaling	6.2	9.2	14.4	15.8	11.9
Retail foodstores	8.7[1]	9.7[1]	21.2[1]	11.9	9.0
Eating and drinking places				9.0	6.8
Total, all U.S.-owned affiliates in food marketing	53.9	68.9	124.7	132.5	100.0

Notes: [1]Retail foodstores and eating and drinking places combined. Source: U.S. Department of Commerce, Bureau of Economic Analysis.

Table 2
....While Food Retailing Accounts for the Largest Share of Foreign Direct Investment in the U.S. Food Marketing System

Sector	Sales of U.S. affiliates of foreign firms 1982	1987	1992	1993	Share of 1993 total affiliate sales	FDI as share of total U.S. 1993 sales
	Billion dollars				*Percent*	*Percent*
Food manufacturing	14.8	22.9	46.8	45.8	36.8	11.1
Food wholesaling	7.0	14.0	19.0	21.7	17.5	4.2
Retail foodstores	18.8[1]	24.3	48.2	51.5	41.5	13.4
Eating and drinking places		.5	4.9	5.2	4.2	2.4
Total, all foreign-owned U.S. affiliates in food marketing	40.6	61.6	118.8	124.3	100.0	8.1

Notes: [1]Retail foodstores and eating and drinking places combined. Source: U.S. Department of Commerce, Bureau of Economic Analysis.

immediate economies of scale. In addition, the parent firm often gains new product and marketing technology from the acquired firm. Thus, technology flows both ways.

Specialized engineering, packaging, and food ingredient firms facilitate foreign direct investment by making technology readily available and mobile across national boundaries. With the help of these specialty firms, food processors can pick and choose the best technology for specific functions from throughout the world and assemble it in a single factory wherever it is located—whether in Zimbabwe, Malaysia, India, or Venezuela.

U.S. Investment Abroad Concentrated in Developed Countries

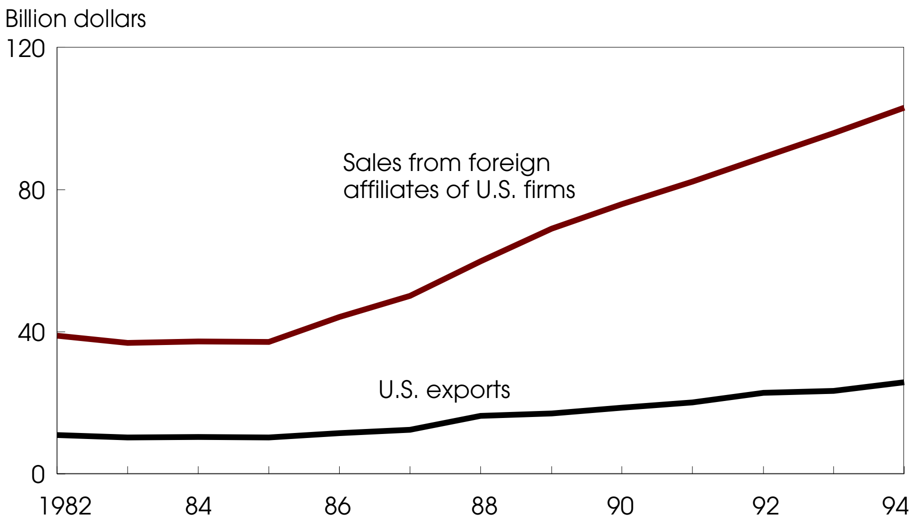
Most large U.S. food manufacturers rely much more heavily on foreign direct investment than on exports from their home country to access foreign markets. Sales from U.S.-owned food manufacturing affiliates abroad have long exceeded the value of U.S. processed food exports. But since 1985, the gap has widened (fig. 1). In 1982, sales from U.S. affiliates in foreign countries at $39 billion were 3.5 times larger than U.S. exports of $11 billion. Neither foreign direct investment nor exports grew in the early 1980's. Since then, both have recorded uninterrupted growth. From 1985 to 1993, sales from U.S. food manufacturing affiliates abroad grew 157 percent to $95.8 billion, while U.S. processed food exports increased 127 percent to $23.4 billion. By 1994, sales from foreign affiliates are estimated to have reached $105 bil-

Table 3
Sales by U.S.-Owned Food Processing Affiliates Abroad Grew 145 Percent Between 1982 and 1993

Country/region	1982	1987	1992	1993	Share of 1993 total affiliate sales	Increase, 1982-93
	Million dollars				*Percent*	*Percent*
Total, all countries	39,023	50,067	89,159	95,782	100	145.4
European countries	18,974	29,044	53,752	54,371	57	186.6
United Kingdom	5,696	7,124	12,214	11,579	12	103.3
Canada	5,258	5,522	NA[1]	10,891	11	107.1
Asia and Pacific	5,432	8,559	13,712	14,411	15	165.3
Japan	2,363	4,442	4,055	4,844	5	105.0
South America	5,133	3,911	6,794	8,033	8	56.5
Argentina	630	758	2,040	NA	NA	NA
Brazil	2,535	1,869	2,874	3,431	4	35.3
Central America	2,951	2,176	5,163	NA	NA	NA
Mexico	2,556	1,596	4,460	6,093	6	138.4

Notes: NA = Not available. [1]Withheld to avoid disclosure. Source: U.S. Department of Commerce, Bureau of Economic Analysis.

Figure 1
U.S Exports and Foreign Affiliate Sales of Processed Food



lion—four times larger than U.S. exports of $25.8 billion. Employment in U.S.-owned affiliates abroad increased at about the same rate. The number of employees at U.S. food manufacturing affiliates in foreign countries grew from 447,700 in 1982 to 550,500 in 1993. Most of the 762 U.S. food manufacturing affiliates abroad are majority owned by their U.S. parents.

U.S. foreign direct investment is concentrated in developed countries (table 3). In 1993, European countries accounted for $54.4 billion, or 57 percent of total U.S. affiliate sales abroad. Within Europe, the United Kingdom is by far the largest recipient of U.S. foreign direct investment, followed by Germany, The Netherlands, and France. Adding Canada and Japan to the European holdings brings the share of U.S. foreign affiliate sales to about 73 percent. U.S. affiliate sales grew much faster in Europe (187 percent) than in either Canada (107 percent) or Japan (105 percent) during 1982-93.

U.S. food manufacturers also sought investment opportunities in other regions. Sales from U.S. affiliates declined in both South and Central America from 1982 to 1987, but have grown rapidly since then. From 1987 to 1993, sales from U.S. affiliates in South America doubled, and sales from U.S. affiliates in Mexico increased 282 percent. This reflects liberalized foreign investment rules in Mexico and most Latin American countries during this pe-

U.S. Food Marketing Firms in China

China represents a huge potential market for foreign food marketing firms. China's population in 1995 reached 1.2 billion, with about 28 percent residing in urban areas. Its gross domestic product (GDP) grew 12 percent in 1994 and another 10 percent in 1995, reaching $764 billion. While this translates into a per capita GDP of only $635 in 1995, that still represents a large increase from a per capita GDP of $407 in 1990.

While U.S. exports of processed food to China have increased in the last 5 years, many U.S. food processors are also investing in food processing plants located in China. As of 1996, at least 29 U.S. food processing firms had established joint ventures or majority-owned affiliates in China. U.S. food distributors and foodservice firms are also beginning to invest in China's food system.

The following are examples of U.S. investments in China's food processing sector:

- Kraft Foods, owned by Philip Morris, has established several affiliates and joint ventures in China: Beijing Kraft Food Corporation produces dairy products; Guangdong Food Co. produces Maxwell House coffee; Tianmei Food Co. produces Tang beverages; and Maxwell House Beverage Co. is a joint venture with Pepsi-Cola Mfg. Ltd. to produce ready-to-drink canned coffee. Kraft Foods has minority interest in four Beijing breweries owned by China's Fine Star Beer Group. Fine Star is licensed to brew and distribute Miller beers in China. Kraft Foods is also building a new factory to produce chewing gum in Guangdong Province.
- PepsiCo has established at least seven joint venture operations with Chinese beverage firms to produce and distribute PepsiCo and local brands of soft drinks. PepsiCo has built a snack plant in Guangzhou which produces a variety of snacks, such as Cheetos and potato chips. PepsiCo is also investing in the Chinese agricultural production system to help develop a local potato specifically for making potato chips.
- CPC International, a large U.S. manufacturer of mayonnaise, salad dressing, margarine, bouillon cubes, and sauces, has operated in China for several years. CPC has 80 percent equity in CPC Food Products Ltd., which produces Knorr bouillon cubes and sauces in Guangzhou, and produces mayonnaise, salad dressings, and chicken products in a joint venture located in Beijing.
- Other U.S. food firms invested in China as well. H.J. Heinz built and operates a large modern baby food plant in China, and Kellogg Co. opened a high-tech plant producing ready-to-eat cereal in 1995. Continental Grain Co. is a 60-percent owner of a large chicken processing company, with Mitsui (Japan) owning 20 percent and a Chinese firm owning the remaining 20 percent.

riod, as well as growth in per capita gross national product.

U.S. firms are also increasing investments in Eastern and Central Europe, the former Soviet Union, and China (see box). At least 42 U.S. food manufacturers had invested in over 90 food processing affiliates or joint ventures in these countries as of early 1996.

Most of the Output Remains in the Host Country

In general, U.S. multinational food processing firms do not establish affiliates abroad for the primary purpose of exporting products back to the United States (although there are clear exceptions, such as U.S.-owned canned tuna operations abroad). Of the $95.8 billion in total U.S. affiliate sales abroad in 1993, 78 percent of the sales remained in the host country (local sales), while 22 percent was exported to other countries. Only 2 percent of sales ($1.7 billion) was exported to the United States. By comparison, other U.S. (nonfood) manufacturing affiliates abroad exported an average of 14 percent of their total shipments back to the United States.

Proximity of affiliates to the United States plays a large role in their export behavior. Even though Canada accounts for only 11 percent of U.S. affiliate sales worldwide, Canada accounts for 40 percent of affiliate exports back to the United States. Likewise, Latin America accounts for 16 percent of U.S. affiliate sales, but a much higher 27 percent of affiliate exports to the United States. Conversely, U.S. affiliates in Europe account for 60 percent of all affiliate sales, but their share of affiliate exports to the United States totals only 25 percent.

Japan a Growing Investor in U.S. Food Manufacturing

Foreign direct investment into U.S. food manufacturing doubled between 1987 and 1993, accounting for 11 percent of food manufacturing in the United States (table 2). The United States received large capital inflows in 1989, especially when the U.K.'s Grand Metropolitan purchased Pillsbury for $5.6 billion.

While there have been no megadeals in the U.S. food industry in the early 1990's, U.K.'s Cadbury-Schweppes' acquired A & W Beverages for $334 million in 1993 and Unilever's (The Netherlands) acquired Kraft Foods Ice Cream Industries and Klondike for $215 million. In 1994, Sandoz, a German pharmaceutical company, acquired Gerber Foods for $3.7 billion.

Sales of U.S. affiliates of foreign food manufacturers totaled $46.8 billion in 1992, triple 1982's $14.8 billion. Sales declined slightly in 1993 to $45.8 billion (table 4). Nearly all sales from these foreign-owned plants were in the United States, indicating that they were targeting the U.S. market; only $2.2 billion (4 percent) of those sales were exported from the United States. A third of the exports from these plants were shipped to the foreign parent company. U.S. affiliates of foreign companies imported more products ($3.2 billion) than they exported. Nearly half of the imports to these affiliates came from the foreign parent group.

Foreign direct investment in the United States is one way to circumvent some U.S. trade barriers. For example, Besnier is producing Brie cheese in the United States in much larger quantities than it would be allowed to import from its operations in France.

European companies were the dominant foreign investors in U.S. food manufacturing, with 68 percent of U.S. affiliate sales (down slightly from 71 percent in 1982). Sales from U.S. affiliates of European and Canadian companies grew during the 1980's and early 1990's, but sales from U.S. affiliates of Japanese companies grew faster. Japanese-owned affiliates increased their presence from 4 percent of foreign affiliate sales in 1982 to 13 percent in 1993. Canada's share declined over the decade, from 15 percent in 1982 to 11 percent in 1993.

Japanese companies have purchased or built U.S. affiliates that mostly produce their ethnic foods, such as noodles, surimi, soy sauce, and dry soup mixes. They have also ventured into livestock and meat processing, Mexican-style frozen dinners, and wine. Japanese investors were more apt to start up new businesses in the United States than were their European and Canadian counterparts.

European food manufacturing investments in the United States were broader based. Wine, dairy products, chocolate products, frozen and canned vegetables, grain products, and bottling plants were some of the enterprises of their U.S. affiliates.

Canadian investments in U.S. food manufacturing were concentrated mostly in distilled spirits, wines, fruit juices, and frozen foods.

U.S. Food Wholesalers Also Expand Into Foreign Markets

Sales from foreign affiliates of U.S. grocery wholesalers increased to $15.8 billion in 1993, up 9.7 percent over 1992 and 156 percent from 1982 (table 1). Sales from U.S. grocery wholesale affiliates owned by foreign firms increased 14.5 percent from 1982 to $21.7 billion in 1993 (table 2).

Many U.S. food wholesaling firms have expanded into foreign markets. Facing saturated markets in the United States and unfulfilled demands globally, Wal-Mart, the parent firm of Sam's Warehouse Club, has been particularly aggressive in its expansion plans for Asia and South America. As part of its first move outside of the Western Hemisphere, Wal-Mart established a joint venture with Ek Chor Distribution System Co. Ltd., a Hong Kong subsidiary of Bangkok-based C.P. Pokphand Co. in 1994. This grocery wholesaler's joint venture is part of a plan to open Value Clubs as a stepping stone into China. Value Clubs are smaller versions of the Sam's Club membership warehouses, which carry frozen foods and other grocery items. In addition

Table 4
Value of Shipments by U.S. Food Manufacturing Affiliates of Foreign Firms More Than Tripled Between 1982 and 1993

Country of origin	1982	1987	1992	1993	Share of 1993 total affiliate sales	Increase, 1982-93
	Million dollars				*Percent*	*Percent*
Total	14,847	22,862	46,799	45,765	100	208
Europe	10,527	17,967	32,994	31,159	68	196
Canada	2,218	3,174	5,113	5,208	11	135
Japan	564	612	5,131	5,737	13	917
Other	1,538	1,109	3,561	3,661	8	138

to expansion in Asia, plans call for an additional 10-12 warehouse clubs and 10-12 supercenters in Mexico. Wal-Mart has also opened Sam's Clubs and supercenters in Brazil and Argentina.

Another leading wholesale club, Price Company, went international for the first time in 1993, opening units in the United Kingdom and Mexico. Price/Costco, formed by a merger between the Price Company and Costco Wholesale Club, opened seven warehouse stores in Canada during the first half of fiscal 1994. In early 1995, Price/Costco, Inc., agreed to acquire Price Enterprises' stake in the companies' Mexican joint venture. Mexico Clubs operates 12 Price Club membership warehouse stores in Mexico.

The largest distributor of food and supplies to U.S. foodservice establishments, Sysco Corp., has a U.S. affiliate in British Columbia called Sysco/Konings Wholesale. It was acquired in the late 1980's as part of the purchase of Staley Continental. Another leading U.S. foodservice distributor, Rykoff-Sexton, operates a Mexican distribution center that opened in 1992.

The largest U.S. grocery wholesaler, Fleming, formed a joint venture in 1993 with Davids Holdings, the leading wholesaler in Australia. The joint venture, Davids Investments Asia PLC Ltd., was formed to establish full-line distribution centers in Asia. Fleming expects the joint venture to also help with its exporting and importing activities. Fleming has foreign affiliates in the Caribbean, Japan, Mexico, Korea, and the former Soviet Union.

Food Retailing Also Attracts Foreign Investors

Sales by U.S. food retailing affiliates of foreign firms reached $51.5 billion in 1993 (table 2). Food retailing affiliate sales amounted to 13.4 percent of total U.S. foodstore sales in 1993. The 5 largest U.S. food retailing affiliates of foreign firms were among the 30 leading food retailers nationwide, generating sales of $39.5 billion in 1994 (table 5). Albertson's, headquartered in Boise, ID, was the largest foreign-owned affiliate, and the fourth-largest food retailer in the United States with sales of $11.9 billion in 1994.

U.S. affiliates of foreign retailers have grown both by building new stores and by acquiring other food retailers. There are successful examples of both strategies among the largest retailers. Both Albertson's and Food Lion relied almost exclusively on internal growth strategies. Ahold, USA, the U.S. subsidiary of Royal Ahold (The Netherlands), and The Atlantic and Pacific Tea Company (A&P), owned by Tengelmann (Germany), have grown by acquiring small local and regional supermarket chains.

Most Americans could not identify these food retailers as foreign-owned firms, as most foreign firms imitate the marketing and merchandising practices of their local U.S. competitors. Although foreign investors and retailers have introduced new concepts in the United States, their success has varied.

In the 1980's, French retailers built very large stores in excess of 100,000 square feet of selling area called hypermarkets, a European retail concept. Early successes were not sustained, and in the 1990's, a number of foreign-owned hypermarket firms, such as Carrefour and Leeds, failed to generate break-even sales volume, resulting in their exit from the industry.

Not all European retailers have failed in efforts to transplant new concepts to the United States, however. When the British firm of Marks and Spencer acquired Kings Supermarkets, the firm introduced high-quality, upscale private-label food products and instore-prepared products typical of their upscale European foodstores. Although the concept has been successful in the United States, few, if any, U.S. retailers have applied the format.

Foreign sales by U.S. food retailing affiliates reached $11.9 billion in 1993 (table 1). Safeway, Inc., owns and operates 235 supermarkets in

Table 5
The Leading U.S. Food Retailing Affiliates, 1994

U.S. affiliate	Foreign investor (country)	National ranking	1994 U.S. sales
			Billion dollars
Albertson's	Theo Albrecht (Germany)	4	11.9
Atlantic and Pacific Tea Company	Tengelmann, AG (Germany)	7	10.3
Food Lion	Delhaize, Le Lion (Belgium)	8	7.9
Ahold, USA[1]	Ahold (The Netherlands)	9	7.4
Shaw's Supermarkets	Sainsbury PLC (U.K.)	29	2.0

Notes: [1]Ahold owns the following U.S. supermarket companies: Bi-Lo, Mauldin, SC; Edwards Super Food Stores, Windsor Locks, CT; Finast, Maple Heights, OH; Giant Food Stores, Carlisle, PA; and Mayfair Super Markets, Elizabeth, NJ.

Canada, accounting for sales of $3.4 billion in 1994. In addition to majority ownership, food retailers have used joint ventures, franchising, and licensing as means to enter foreign markets. Circle K, a U.S. convenience store operator, has joint venture and franchising agreements in 19 countries, including Canada and the Pacific Rim countries. I.G.A., Inc. (Independent Grocers Alliance), a cooperative supermarket operator, licensed I.G.A. foodstores in a number of countries in recent years. I.G.A. provides training, product procurement, branding, and merchandising support for overseas retailers. More than 385 foreign supermarkets located in 19 countries participated in the I.G.A. program in 1994.

As the aggregate figures indicate, investment by foreign food retailers in the United States swamps foreign direct investment by U.S. food retailers abroad. The greater involvement by overseas investors in U.S. food retailing is due to a number of factors. The United States offers a large and diverse market for overseas food retailers, making it attractive to foreign investors. In addition, the United States offers foreign investors a highly developed food production and distribution infrastructure—food production capacity, extensive transportation and delivery system, and efficient food wholesaling services—enabling foreign firms to focus their investment capital on food retailing operations.

The U.S. market also offers foreign investors a stable legal and political system that is consistent with private enterprise and international trade, and contributes to lower risk relative to other countries. The competitive environment of U.S. markets may not be fully appreciated by overseas investors, however, as evidenced by the failure of many hypermarket format stores opened during the 1980's.

Worldwide, foreign direct investment and trade in processed foods will continue to increase as firms seek to maximize their unique marketing advantages.

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