USDA Foreign Agricultural Service

GAIN Report

Global Agriculture Information Network

Template Version 2.09

Required Report - public distribution

Date: 8/4/2006

GAIN Report Number: BR6014

Brazil

Retail Food Sector

2006

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Report Highlights:
The Brazilian retail sector is the major food and beverage distributor in the country, representing a feasible market entry point for US exporters. The primary goal of this report is to inform US companies how this industry operates, who the major players are and how they have performed during the past year.

Includes PSD Changes: No
Includes Trade Matrix: No
Annual Report
Sao Paulo [BR3]
[BR]

I. Market Summary

A. Economic Context

In June 2005 Brazil was shaken by claims of corruption in the government. The ensuing scandal dominated the political agenda throughout the year, nonetheless, economic performance was unaffected. For 2005, Brazil achieved a primary fiscal surplus above the targeted levels. The government also experienced a surge in tax revenues generated by higher income and benefited from higher surpluses achieved by public sector companies. The Brazilian Central Bank (BACEN) maintained a tight monetary policy, holding inflation within targeted levels.

Despite the appreciation of the Real, Brazilian exports continued to expand. The balance of payment has benefited from the high price of commodities in the international market and the overall growth of the global economy. Private capital inflows remain vital to the Brazilian economy, with foreign direct investment increasing and better ratings from risk management agencies on its sovereign credit rating, Brazil has also sustained its capital account surplus.

While authorities followed longstanding macroeconomic policies, the political environment put the government's reform agenda on hold. With the elections for president taking place in October 2006, the government has not advanced reform proposals impacting the business climate, such as the state tax system and public private partnerships on infrastructure projects.

ECONOMIC INDICATORS

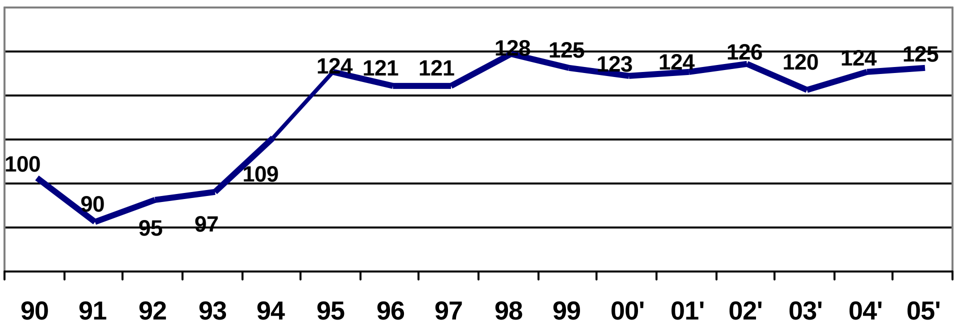
	2002	**2003**	**2004**	**2005**	**2006***
GDP Growth (%)	1.9	-0.2	4.9	2.3	3.5
Inflation-IPCA (%)	12.5	9.3	7.6	5.7	4.5
Interest Rate-Selic (%)	25.0	16.5	18.75	18.0	15.25
Total Exports (US$ billion)	60.4	73.1	96.5	118.3	132.0
Total Imports (US$ billion)	47.3	48.3	62.8	73.5	85.0
Trade Balance (US$ billion)	13.1	24.8	33.7	44.8	45.0
Average Exchange Rate (R$-US$)	3.54	2.90	2.93	2.43	2.20

Source: Brazilian Institute of Geography and Statistics (IBGE), Brazilian Central Bank, Secretariat of Foreign Trade (SECEX), Getulio Vargas Foundation (FGV), Research Institute for Applied Economics (IPEA)
(1) IPCA is calculated by the Brazilian Institute of Geography and Statistics (IBGE). It is the Government of Brazil's target measure of inflation and measures price variation for products and services consumed by families with earnings from 1 to 40 minimum wage salaries in metropolitan areas of Porto Alegre, Belo Horizonte, Recife, Sao Paulo, Belem, Fortaleza, Salvador, Curitiba, Distrito Federal and Goiania.
(2) SELIC refers to the Brazilian Central Bank interest rate.
(*) Forecast

B. Retail Performance and Trends

According to the Brazilian Supermarket Association (ABRAS), 2005 gross sales of the retail industry totaled R$106.4 billion, representing a 7.8 percent nominal growth rate compared to the previous year. In real terms, the increase was quite modest, only 0.9 percent. According to the Brazilian Institute of Geography and Statistics (IBGE), the industry accounted for 5.5 percent of Brazil's GDP of R$1.938 trillion in 2005.

RETAIL SECTOR GROSS SALES INDEX



Source: ABRAS/ACNielsen

Analysts estimate a loss of 30 percent in consumer purchasing power over the last 10 years. Since the retail sector is immediately impacted by consumers' response to economic conditions, industry sales did not follow the GDP growth registered in 2005. However, modest growth was maintained: the number of sector employees increased 1.6 percent (to 800,922), and the number of stores expanded 1.3 percent; by the end of 2005 there were 72,884. The total sales floor space also grew 1.7 percent and the number of checkouts, increased 1.8 percent. In addition, investments made in 2005 were 85.1 percent above the 2004 level, amounting 2.4 billion reais (divided into renovation, technology and equipment). According to ABRAS investments are expected to increase 17 percent in 2006, with 63 percent of this total going to new stores.

BRAZILIAN RETAIL INDUSTRY

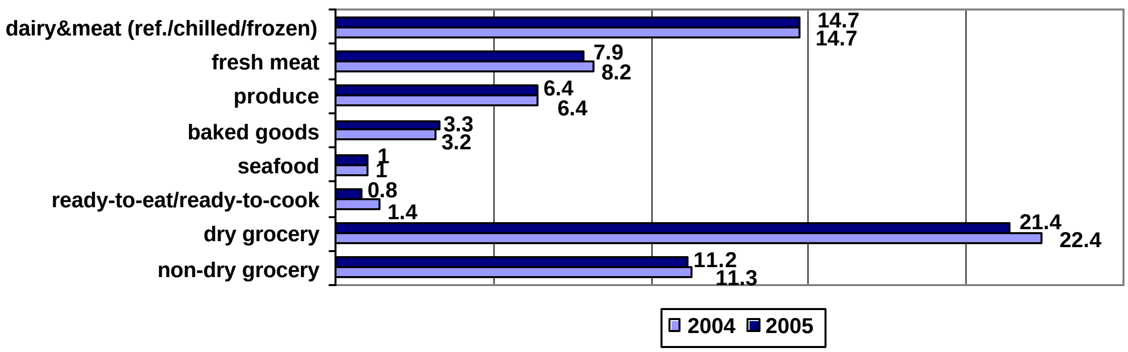
	2000	2001	2002	2003	2004	2005	2005 vs.2004 ? %
Number of stores	61,259	69,396	68,907	71,372	71,951	72,884	1.3
Gross sales (R$ billions/nominal value)	69.2	74.2	81.7	89.3	98.7	106.4	7.8
Share over GDP	6.3	6.2	6.1	5.7	5.5	5.5	0.0
Number of employees	701,622	710,743	718,631	739,846	788,268	800,922	1.6
Sales space (millions of m²)	14.3	15.3	15.9	17.9	18.1	18.4	1.7
Number of checkouts	143,705	156,022	157,446	163,216	166,503	169,583	1.8

Source: ABRAS/ACNielsen

Based on the profile of the top 500 retail companies, store formats of 250 m²-or-less continue to grow more than any other. Today they represent 45.6 percent of the total number of stores, and again in 2005 this format expanded 5.6 percent. Since 2001, this layout has experienced steady growth, pushed by Econ and Dia%. The product mix of these types of stores has also increased. In 2004 the average number of items carried was 4,699; in 2005 it went up to 5,120. Contrasting with this movement, stores with square meters from 251 to 1,000, seen their share of the market shrink from 27 percent to 24.9 percent.

Despite the decline in store size, Brazilian supermarkets are including more non-food products on their shelves. According to ABRAS, non-food products represented approximately 7 percent of overall sales in 2005. Another trend is the growth of gasoline sales: in 2004 this item corresponded to 2.5 percent of total sales, in 2005 it rose to 3.6 percent. As per food products, the share of the "perishables" category suffered a slight drop, going from 34.9 percent of total food sales in 2004 to 34.1 percent in 2005. This minor decrease was consistent with a decline in overall sales of food and beverage items, the share of these items fell from 46.4 percent to 46.3 percent of supermarket sales in 2005. The performance of private labels in Brazilian supermarkets is quite steady. Since 2002 products carrying supermarkets' brands has maintained their share at 4.7 percent.

SHARE OF FOOD & BEVERAGE ITEMS AT BRAZILIAN SUPERMARKETS

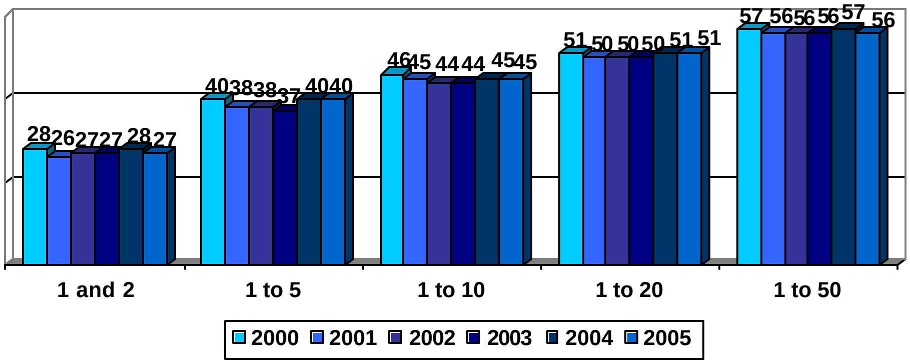


Source: ABRAS/ACNielsen

C. Concentration

To develop its sector profile, ABRAS analyzes the leading 500 companies. In Brazil, the top 500 supermarket groups are responsible for 64.6 percent of the total sector. Together they generate sales of R$68.7 billions. This result represents an increase of 6 percent compared to the previous year. These retailers comprise 4,866 stores, 5.9 million m², 345,879 employees and 46,672 checkouts. Despite the fact that the retail industry is one of the least concentrated in Brazil, the top 5 supermarket chains account for approximately 40 percent of total sales. In 2005 the most significant change in retailers rankings was made by Wal-Mart. The US company acquired Sonae's operations in Brazil, which led to the incorporation of 400 stores and an addition of approximately R$4.3 billion to their revenue. With this move Wal-Mart amplified its presence in the country and closed the gap on the country's second largest retailer, Carrefour.

CONCENTRATION TREND IN THE BRAZILIAN RETAIL SECTOR
(% gross sales)



Source: ABRAS/ACNielsen
Note: the horizontal axis represents the top retailers on sales value.

D. Demographics and Consumption Patterns

According to the Brazilian Institute of Geography and Statistics (IBGE), the average household size has decreased from 4 in 1981 to 3 in 2004. This phenomenon is driven by the increasing presence of women as heads of household and by lower fertility rates. In 2004, women were in charge of 29 percent of the Brazilian families, which is a substantial increase compared to the 80's when women were responsible for 17 percent. The traditional family has also changed, IBGE indicates that sole individuals occupy 10 percent of the Brazilian homes; this groups evenly distributed among men and women. IBGE also forecast an increasing presence of seniors in the next years.

In 2005, AC Nielsen conducted a study to evaluate how these changes have affected consumption of food and beverage products. There is an obvious interest towards smaller food packages or individual portions. Consumption of healthy products is also a rising trend. Nielsen shows that food categories considered healthy, on average, are 20 percent more likely to be consumed by families whose head of household is in his/her 50's.

In 2005, ABRAS did not conduct formal studies to measure the presence of imported products in Brazilian supermarkets. A study carried out by the association in 2004 demonstrated that the presence of foreign items had increased on supermarket shelves. While in 2003 these goods represented 1.8 percent, in 2004 it went up to 2.4 percent. Despite the lack of formal research, ATO observes a growing interest for US products due to the depreciation of the US dollar.

Given this outlook, there are challenges and advantages to be investigated prior to entering the market, as noted below:

ADVANTAGES	CHALLENGES
More supermarkets are showing interest in selling imported goods.	Brazil is self-sufficient in food supply. An imported product is a luxury item and not a necessity. Retailers offer foreign goods to differentiate themselves and develop new niche markets. Therefore, US exporters may start selling small volumes and also be asked for a wider variety of products.

Price is not always the determinant purchase criteria for high-end consumers.	High-end consumers are more demanding regarding other aspects of products such as innovation, packaging, status, new trends, etc.
The US food industry is able to respond to consumer demand promptly, regardless of the segment of products.	Consumers perceive US food products to be overly processed and relatively unhealthy.

II. Road Map for Entry

A. Entry Strategy

When approaching the Brazilian market, exporters should be aware that most imported foods and beverages considered consumer-oriented are not price competitive compared to locally produced products. This is due both to the low cost of locally produced goods and high import tariffs. The Brazilian food industry is well developed and the ever-expanding presence of major multinational companies contributes to making the sector quite competitive. Products imported from Mercosul members (Argentina, Paraguay and Uruguay) enjoy duty-free status and Chilean products face a reduced duty rate.

According to importers, the shelf price of imported goods is 2-4 times the FOB price at origin; thus, US importers need to evaluate the extent to which their products can compete and maintain saleability. Brazilian high-end consumers are willing to pay more for certain products. In fact, the market for luxury products is booming. For this niche market, emotion often overtakes reason; nevertheless, conducting primary research to determine whether the market offers real opportunities is crucial.

Because approximately 80 percent of food and beverage distribution takes place through retail stores, developing a relationship with retailers will be more likely to guarantee visibility and countrywide coverage. The commercial power of the retail industry vis-à-vis food suppliers has continuously increased over the past ten years. Starting in 1994 with the implementation of the Real Plan, and through the rest of the last decade, imported products became a true alternative to domestically produced goods even though the percentage of imported products in retail sales is quite small.

Retailers are well aware of their importance in the food distribution system and of their advantageous position vis-à-vis suppliers. While retailers exert considerable purchasing power and reach the overwhelming majority of Brazilian households, their purchasing of imported products can be characterized as follows: wide selection in small volumes. For retailers, Non-Brazilian products may be imported directly from the foreign supplier or purchased locally from an importer/distributor. US exporters should approach importers and/or retailers to further develop a market strategy.

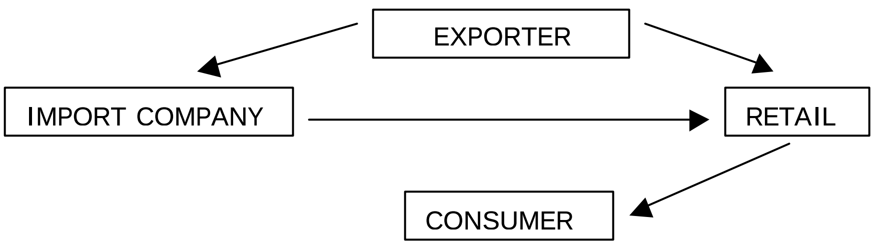
US exporters should always consider the local US Agricultural Trade Office (ATO) as an initial source of information and market guidance. The ATO maintains direct contact with the major players in order to facilitate market entry and is also able to provide assistance on Brazilian legislation and standards for imported goods. US companies can test market through ATO marketing activities and also profit from its market intelligence.

B. Market Structure

Foreign products are distributed in the Brazilian market mainly through specialized importers or retailers. Major retailers are willing to import directly in order to obtain better margins.

However, when volumes do not reach an advantageous level, retailers buy from local importers/distributors. While avoiding the middleman is a general goal, it only happens if retailers are able to fill containers and keep overhead costs in check. The more common option is, in fact, mixed containers. Brazilian buyers are hesitant to purchase full containers but, on the other hand, US suppliers are often unwilling to deal with small volumes. This situation has restricted entry of new US products in the Brazilian market.

MARKET STRUCTURE FOR IMPORTED PRODUCTS



C. Company Profiles through 2005

RETAILER NAME	OWNERSHIP	SALES (R$ MIL)	SHARE (%)	No. of STORES	LOCATION	PURCHASING AGENT TYPE
Cia. Brasileira De Distribuicao (Pao de Acucar, Extra, CompreBem, Sendas)	Brazil/France	16,169	15	556	South Southeast Center-East Northeast	LFP, DI, LI
Carrefour (Carrefour, Carrefour Bairro, Dia%)	France	12,546	12	399	South Southeast Center-East North Northeast	LFP, DI, LI
Wal-Mart Brasil (Wal-Mart, Sam's, BomPreco, Balaio, HiperMagazine)	US	11,732	11	295	South Southeast Northeast	LFP, DI, LI
Cia. Zaffari (Zaffari, Bourbon)	Brazil	1,410	1	26	South	LFP, DI, LI
G. Barbosa (G. Barbosa, ViaBox)	US	1,227	1	35	Northeast	LFP, DI, LI
TOTAL TOP 5		**43,084**	**40**	**1,311**		
DMA Distribuidora (MartPlus, Epa, Via Brasil, Via Atacado)	Brazil	1,212	1	68	Southeast	LFP, LI
Bretas Supermercados	Brazil	1,145	1	44	Center-East	LFP, LI
Coop	Brazil	1,077	1	22	Southeast	LFP, LI
Angeloni	Brazil	993	1	19	South	LFP, LI
Prezunic	Brazil	782	1	15	Southeast	LFP, LI
TOTAL TOP 10		**48,293**	**45**	**1,479**		

Note: LFP (local food processors), DI (direct imports), LI (local importers).
Source: ABRAS/ACNielsen

III. Competition

Mercosul members are the major exporters of consumer-oriented products to Brazil. Argentina, Paraguay and Uruguay benefit from this duty-free agreement. Another major player in the Brazilian market is the European Union, ranking second. EU suppliers are direct competitors to US exporters, as both target high-end consumers. European countries have an aggressive approach to promote their premium products in the local market. Countries such as France, Germany, Spain, Portugal, UK and Italy have their own trade and promotion branches established in Brazil to support their marketing programs.

US companies are able to offer the same or better quality of products as do EU suppliers, but the EU starts the competition a few steps ahead. Brazilian eating habits have been strongly influenced by historical ties to Europe and consumers have a favorable perception of EU products as being traditional and sophisticated. With approximately equivalent prices, consumers tend to prefer EU products over US products. Segmenting the market on the basis of perceived benefits or attributes is a key factor for US companies to succeed.

Most imported food products are not considered essential by the majority of Brazilian consumers, especially since the Real started its depreciation in 1999. As a result, today, imported consumer-oriented products are considered luxury items. Exporters cannot be satisfied with merely supplying the product to the market, as it is important to establish a consistent positioning to persuade consumers and gain market share in the premium segment. The US Dollar's overall depreciation against the Euro and Real since 2004 continues to provide an opportunity to US suppliers.

BRAZIL'S IMPORTS OF CONSUMER-ORIENTED PRODUCTS (US$ million)

	2000	**%**	**2001**	**%**	**2002**	**%**	**2003**	**%**	**2004**	**%**	**2005**	**%**
Mercosul	1,003.9	63.5	635.5	55.6	649.7	58.5	602.9	60.6	569.0	50.7	796.7	58.0
EU	303.7	19.2	263.9	23.1	232.7	21.0	205.0	20.6	231.7	20.6	283.7	20.6
US	104.3	6.6	92.1	8.0	82.6	7.4	72.4	7.3	101.6	9.1	114.1	8.3
Others	168.4	10.7	151.7	13.3	145.3	13.1	114.6	11.5	219.8	19.6	179.8	13.1
Total	1,580.3	100	1,143.2	100	1,110.3	100	994.9	100	1,122.1	100	1,374.2	100

Source: WTA/Secretariat of Foreign Trade (SECEX)
Note: Mercosul values for 2005 include Chile and Bolivia.

IV. Best Product Prospect

A. Products present in the market, which have good sales potential

According to ATO analysis, in 2004 and 2005 consumer-oriented food product categories that have demonstrated the best performance in the market were: fruit/vegetable juices, processed fruit/vegetables, snack food, pet food, red meats fresh/chilled/frozen, dairy products, wine and beer. These categories also represented, for non-Mercosul exporters, the most significant in sales volumes.

Importers are most interested in brands that are well known in their original markets and in high-end products. In addition Brazilian importers/distributors usually prefer products with six-month shelf lives or more. In addition to the product itself, packaging, status and level of innovation are all important attributes. Products that combine these characteristics are more likely to successfully enter the market.

B. Products not present in significant quantity but which have good sales potential

Health foods, especially natural and organic products, have a limited presence in the Brazilian market. The Brazilian food industry has not directed consistent efforts to develop these segments, as the consumer base is restricted to a slice of the Brazilian population, which is therefore less attractive when considering return on investment. There are limited suppliers in the market for these products and consequently prices are high to prohibitive.

Small and medium-sized companies are responsible for 70 percent of local organic supply. In Brazil, prices of health foods, organic and natural products compared to conventional products are 40 to 300 percent higher. As the US industry for this segment has already achieved gains in scale and prices for these products, exporters can find opportunities in the Brazilian market as the price of the imported product could still be lower compared to locally produce ones.

C. Product not present because face significant trade barriers

Brazilian legislation requires all food items to be approved by Ministry of Health (MS) or Ministry of Agriculture, Livestock, and Food Supply (MAPA) prior to shipment. In general, there are few barriers to importation of consumer-ready food products; nevertheless, there are numerous bureaucratic procedures to be followed. Currently, poultry imports are banned (Brazil does not allow the entry of this item) and for products containing ingredients derived from biotech commodities there are also considerable restrictions.

V. Post Contact and Further information

Please do not hesitate to contact the offices below for questions or comments regarding this report or require assistance to export processed food products into Brazil:

U.S. Agricultural Trade Office (ATO)
U.S. Consulate General
Rua Henri Dunant, 700
04709-110 Sao Paulo – SP
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