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Hungary

Retail Food Sector

Annual Report

2004

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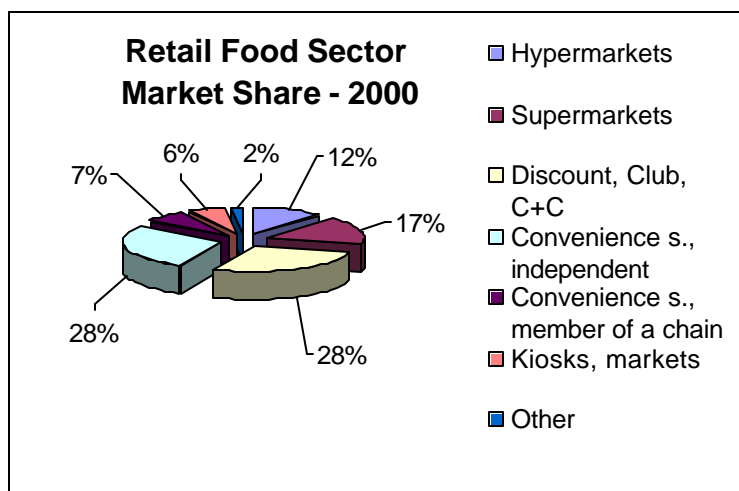
Report Highlights:

Hungary's grocery sector continues to modernize and consolidate. Multinational retail chains are driving this change with heavy investments and running battles for market share. Increasing consumer incomes, advanced trade infrastructure, and the opening of the Hungarian market to the huge common European market offer new opportunities for U.S. food and beverage exporters. U.S. food exports with best sales potential include dried fruits, nuts, seafood, distilled liquors, wines, spices, condiments, pet food, fruit juice concentrates, snacks, and instant foods.

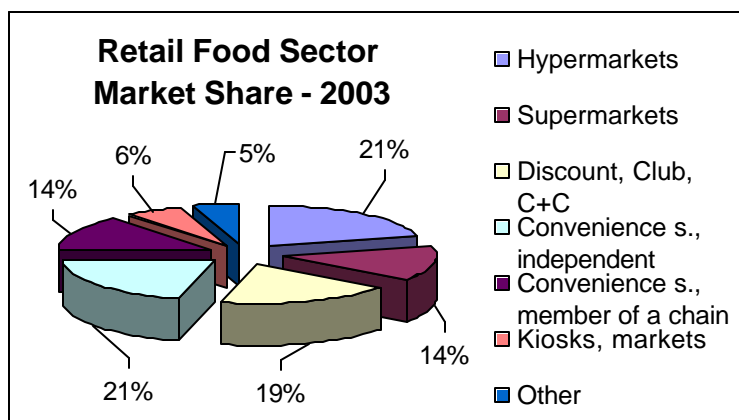
Includes PSD Changes: No
Includes Trade Matrix: No
Annual Report
Vienna [AU1]
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I. Market Summary

The value of retail food sales increased from \$7.9 billion in 2002 to \$10.1 billion in 2003. This represents a 2.7 percent increase in dollar terms (however, the growth figure is somewhat overestimated because of the depreciation of the dollar). Food sales volumes indicate modest increase for 2004. Considerable increases for retail food prices as an effect of the EU membership did not occur in the first months after accession. Only a few commodities, such as sugar and some sweets become more expensive, while price of a variety of dairy products and beverages went down. Concentration in the grocery trade continued over the last few years.



By 2003, more than 54 percent of the turnover was attributable to just six percent of all retail companies, and international retail chains controlled 43 percent of the market. The number of food shops is decreasing (from 51,603 in 2001 to 51,082 in 2003), and the average size of outlets and the number of hypermarkets is on the rise. Another tendency of the structural changes of the retail food sector is that convenience stores increasingly join to store chains and franchise networks. This tendency is strongly related to the concentration of purchases and logistics (see about purchasing alliances at II. Road Map for Market Entry)



Over the past few years, a number of hypermarkets, supermarkets, and Cash and Carry stores have been built in prime locations around Budapest and other cities. Their wide

variety of meats, fruits, vegetables, and bakeries have reduced sales for traditional retailers, butchers, green grocers, wet markets and others. Growing butchery and baking capacities of hypermarkets may be potential competitors for the food processors of the given region as well. Consumers are shopping less often and tend to stock up and buy food for use over a longer period of time. This trend is supported by the higher number (and larger) cars owned by people, and the increasing presence of freezers at home. For example, in 2003, 45 percent of households had a car, 75 percent had refrigerators and 54 percent had freezers. These tendencies support the preference of larger stores. As just one example, TESCO recently opened a 240,000 square foot hypermarket with 1,500 parking spaces, 60 checkout lanes, and 24 hours service. Stores of this scale are becoming the norm in Hungary. "Supermarket brand" products are on the rise at large retail chains. Domestic suppliers mainly manufacture these products, carrying the logo of the retailer or a distinctive "economical products" name. With the recent EU membership, own brand products start to be international, supplied from other European countries.

Value added products represent a small but increasing part of the agricultural products exported to Hungary. The export oriented food-processing industry of the country (which has also benefited from American investments) imports raw materials from United States for further processing. Consumer oriented products account for nearly one fourth of total agricultural exports from the United States to Hungary (USD 43 million) in 2003.

Advantages and challenges faced by U.S. food exporters in Hungary

Advantages	Challenges
Increasing consumption	Domestic food processing is very competitive
Western consumption patterns are emerging	Increased European competition, due to EU membership of Hungary since May, 2004
There is growth potential in the development of retail sector, especially in suburban and rural areas	Slow increase of real incomes
There are unexplored commodity areas	
Domestic industry needs certain ingredients	Many traders are inexperienced in conducting business with foreign companies
Purchases by tourists and transit shoppers are large and growing	High transport costs
Several experienced, multinational retailers	Relatively small delivery volumes
Innovative products and packaging are appreciated	Hungarian consumers are unfamiliar with the value of many U.S. products
Importers are open to new products and technologies	Importers have difficult time accessing reasonable local finance terms
Hyper- and supermarkets are popular	Introduction to retail shops of a new

among consumers	product is costly (registration, commission fee, "slotting fee" etc).
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II. Road Map for Market Entry

A. Hypermarkets, Supermarkets, Shopping centers, Cash and Carry and Club (Wholesale) Outlets

Entry Strategy

Because of the competitive market environment, the introduction of a new product to the Hungarian market demands planning and some market analysis. The help of a local agent may be necessary, both to advise on market conditions and to help with the required legal legwork. Participation in local food shows is a low cost gauge of product interest. The Agricultural Office in Budapest (contact information below) provides importer and distributors lists, as well as information on food shows.

Market Structure

The follow points describe market the market structure and give tips for importing foods into Hungary:

◆Many importers mostly the bigger ones, are wholesalers and/or distributors themselves.

◆**Some products enter via the European distribution network of multinational retail chains.** Exchange of products of the Central European NMS accelerated after May 2004. The leader of this trade, TESCO, estimated its imports to Hungary HUF 1.5 bn (USD 7.7) in 2004, consisted of frozen potatoes and sweets from Poland, cheese and cream from Slovakia, or beer from Czech and Germany.

Consolidators in Austria, the Netherlands or Germany may also supply some products e.g. rice, almonds, and various branded products. (See A Guide to European importers of U.S. food and beverage Products at <http://www.american-foods.org>).

◆**Importers usually specialize in a product area**, i.e. dry groceries, frozen products, brand name items, beverages, meat and poultry, seafood, bakery ingredients, etc.

◆**The use of local agents is recommended.** The local representative of a product must be authorized to discuss prices and conditions of sale as retailers are rather "picky" and the market is rather price sensitive and competitive.

◆**Purchasing alliances** of retail chains. Many of the big retail chains established purchasing partnerships. These giant buyers may negotiate better conditions at suppliers while the suppliers may appear at a wider market area and work with a partner of more stable financial background. Most well known purchasing alliances are Metspa (Metro and Spar), CBA, Honiker, Provera (Cora and Profi), Tengelmann (Plus and Interfruct) etc.

Major Hypermarket and Supermarket Profile

Name of Retailer	Ownership	Food Sales	Number of Shops	Typical sales area	Number of Food Items
Type of Shop		CY 2003 USD million		Square foot	
Tesco (Hypermarket)	UK	995	8 6 24 Total 38	Hypermarkets 54,000-160,000 Supermarkets 26,000-63,000 Other	30,000 10,000
Interspar (Hypermarket)	Austria/UK	485	15	17,000-20,000	10,000
Spar (Supermarket)			96	9,000	10,000
Kaiser's (Supermarket)		N/A	21	13,000	12,000
Cora (Hypermarket)	France	438	6	120,000-162,000	33,000
Auchan (Hypermarket)	France	249*	8	86,000-215,000	35,000
Plus (Supermarket/Discount)	Germany	355*	139	539,000	1,800-2,200
Coop Hungary (Supermarket, C+C, & Convenience)	domestic	1,199	335 C + C 67 898 1100 Total 2400	6,500 N/A 3,300 2,000	3,000 1,200
CBA (Supermarket)	domestic	1,246	2 43 2,481 Total 2,526	86,000 43,000 5,400-6,500	8,000 6,000 3,000
Profi (Supermarket)	Belgian/ France	98	82	3,300-5,500	1,500
Penny Market (Supermarket/Discount)	Germany	537*	168	7,500	1,000
Interfuct (C+C)	Germany	185*	20	280,000	6,000
Metro (Club, C+C)	Germany	763	13	90,000	800

* CY 2002, USD million

B. Convenience Stores, Gas Station Shops, Kiosks, E commerce

Entry Strategy

Sources of imported products for convenience stores are the same importers-distributors used by supermarkets. Small independent shops purchase niche products from wholesalers

and at C+C shops as well. Suppliers of Convenience Stores, particularly specialty shops (gourmet food, sweets shops, organic and health food shops, beverages shops etc.) are more likely to stock specialty import items than supermarkets. Market Structure

- ◆ Convenience stores and other stores in this category receive products from importer distributors and/or wholesalers and C+C warehouses.
- ◆ Gas station shops are ready to sell high value, brand name, and convenience products.

Major Convenience Type Store Profile

Name of Retailer	Ownership	Food Sales	Number of Shops	Total sales area	Number of Food Items
Type of Shop		CY 2003 USD million		square foot	Items
CBA *					
Coop Hungary *					
BEE Foods Ltd.	Domestic	228	220	3,500-5,500	4,800
Tempo	Domestic	71	47	5,000	4,500
Heliker Rt.	Domestic	40	69	n/a	3,500
Slager (Franchise)	Domestic	95	250	1,500	3,000
Rema 1000	Sweden	5	12	3,800	1,750
* Although primarily supermarkets, these two chains are also strong in the convenience grocery shop category					

Gas Station Mini Marts

Most of the 1,000+ gas stations in Hungary have a convenience shop that is an important profit center. Market space of these convenience shops vary from 200-1,300 square feet. According to a recent survey, 35-45 percent of shop sales are food and beverage items. Sales of impulsive, high value products are still the key question for gas station shops. But further strengths of their operation are quick purchase and non-stop hours. Mini-marts needed to shift selling household essentials and handy ready-made food products for their increasing, mainly young, 'late bird' clientele.

Most of Hungary's ten major gas station companies have shops. However, Shell Hungary runs its "Select" stores under a franchise partnership with CBA, a major domestic grocery chain. Two of the big retailers turned the concept back. TESCO and AUCHAN have started to build their own filling stations besides the hypermarket. And these filling stations have their own mini-marts as well...selling at hypermarket price level.

Kiosks

Kiosks concentrate on sales in pedestrian-only areas of cities, subways, recreation areas and shopping malls. Sales have been declining for some time. Kiosks typically sell sweets, fruits, vegetables, beverages, and finger food. Kiosks and simple road side stalls are particularly active in selling tropical fruit and several seasonal sweets and gift items around Christmas, Easter and New Year's Eve.

E commerce

There are about 150 companies in Hungary that sell their products over the Internet and a few market leaders take 80% of the sales value. According to a 2004 GKI - Westel - Sun Microsystems Hungary survey, Internet sales revenues were forecasted about \$44.6 million in 2004. This is a 247 percent increase over 2000. Reasons of the increase of the last two years may be attributed to the technical development at the Internet access of households, and a government supported home computer sales program ("School-Net" Express program). The most common goods sold online are books, music, electronics and gifts. There are several grocery companies in bigger cities running e-commerce web sites for home delivery of food and grocery items. The majority of non-food B2C companies use the Hungarian Postal Service to deliver their goods; food retailers use their contractors or have their own car fleet. In most cases, payment is collected upon delivery.

C. Traditional Markets

Entry Strategy

Traditional markets in Hungary are either open-air "farmer's" markets or market halls, both with booths for traders. The most important commodities in these markets are fresh meat and poultry, processed meats, fish, fruits and vegetables. A wide variety of cooking ingredients, spices, dry fruits, nuts, and imported specialties (e.g. flowers) are also typical traditional market items. As with specialized convenience shops, traders in traditional markets handle smaller volumes and specialty products. One example of a product sold through traditional markets is California raisins. These are imported bulk for confectionary and sweets. They did not prove to be competitive in standard American retail packages. California raisins now can only be bought at farmers markets "out of the box."

Market Structure

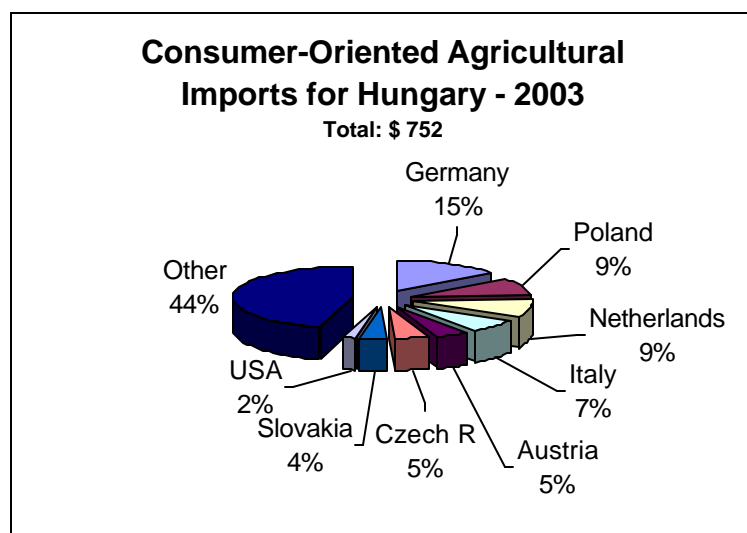
- ? Traditional markets sell domestic and imported produce obtained through local wholesale markets.
- ? Meat, poultry and grocery items are usually supplied by the same wholesalers as that supply bigger food stores. For really small vendors, there may be an additional middleman consolidating orders.
- ? The share of wet markets sales dropped to less than five percent of total grocery sales in 2000.

III. Competition

The main competitors to U.S. exports of consumer oriented agricultural products are the EU countries and other nearby Eastern European countries. Purchases from these traditional sources are facilitated by not only by geography and traditions but the recently opened EU domestic market.

Both the domestic food processing and the food trade are dominated by strong multinational food companies. Distribution of their finished products and the re-export of their raw materials from western Europe (including the U.S. products such as almonds and rice) strongly influences Hungary's direct imports from the USA.

EU firms also tend to spend heavily on food promotions, such as in-store promotions, supermarket training, trade servicing and trade missions.



IV. Best Product Prospects

1. Raisins
2. Dried Fruit
3. Almonds
5. Peanuts
6. Rice
7. Meat (Pork and Beef)
8. Seafood
9. Distilled Liquors
10. Wine
11. Spices & Condiments
12. Pet Food
13. Fruit Juice Concentrates
14. Instant Food
15. Misc. Grocery Items (Snacks, Peanut Butter etc.)

The fastest growing consumer oriented import commodities are snacks, breakfast cereals, dairy products, out of season fruits and vegetables, nuts and alcoholic beverages where the changing consumer tastes and way of life and the demand for wider choice open new markets.

Temporary shortages on the domestic market (meat, poultry) or limited availability of a given commodity or quality provide temporary U.S. sales opportunities, e.g., fruit juice concentrate, rice, tobacco, peanuts, seafood, raisins, tree nuts, dried fruit etc.

V. KEY CONTACTS AND FURTHER INFORMATION

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