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FOOD PRODUCTION AND MARKETING IN CROATIA: CURRENT ISSUES

Since 1995 food production and tourism have been officially designated major strategic economic activities to ensure the economic development of the newly independent Republic of Croatia. Since then, food production in Croatia has faced some serious challenges with natural resources, human resources, and technology, the major input factors of food production. Some of these have are inherited from the planned economy of the past, and some of them have arisen as consequences of war and transition processes.

Croatian food production nowadays is led by mostly small sized companies (85%), with major problems of inconsistent product quantities and quality and a small ratio of recognizably branded products. Most profitable food products in Croatia are produced by companies owned by foreign investors. The foreign trade balance is set for a long term negative, as trade is based on only a few products with low added value (sugar, tuna fish).

Marketing of food products in Croatia can be analysed in terms of the 4P's. Among products, there is powerful competition from foreign substitute products that are often of lower quality and price. These products are welcomed by Croatian consumers in circumstances where almost 35% of household income is spent on food. Promotional activities are at a very low level, since marketing and, especially, promotion are often perceived as unnecessary costs by food producers. In the area of distribution, distributors have significantly greater bargaining power than do producers.

Therefore, there is a need for both macroeconomic (structural) changes in areas of ownership, production, and market organization and microeconomic changes in food producers' marketing and innovation to create competitive advantage on both local and international market.

1. INTRODUCTION

As early as 1995, when Croatia, although independent for 3 years, was still in war and ⅓ of its land was still occupied by the ex-Yugoslavian army, the Government has proclaimed a strategic development concept known as the "blue – green highway". Blue meant Adriatic coast, i.e. tourism, and green meant fields, i.e. agriculture and food production. These two industries were seen as powerful triggers not only for economic recovery, but also for the long term development of Croatia. Both could contribute to the development of "silent" food exports.

This development paradigm was based upon existing natural resources and potential in both industries. However, it has brought up some problems concerning both industries. In this paper we concentrate on food production.

2. RESOURCES FOR FOOD PRODUCTION IN CROATIA

We can distinguish three major elements that create industry competitiveness: natural resources, human resources, and technology.

Natural resources at the disposal of the Croatian food industry have some advantages and some disadvantages compared to other European countries. The two major advantages are climate diversity and natural soil fertility. The different climate areas, continental, Mediterranean, and mountain, allow great diversity in agricultural production that could be a good basis for the food industry. Natural soil fertility is mainly due to a low level of previous exploitation by agriculture, the small farms that have formed the mainstay of Croatian agriculture in the past always found strong and destructive fertilizers to be too expensive to use. The major disadvantages in natural resources for food production in Croatia are unused fertile soil, small production units (farms), and non-specialized production. According to National Statistics Bureau data, about 30% of fertile land is not being used in Croatia. A good proportion of this is due to mine fields left over from the past war. The size of production units (farm units are extremely small in comparison to those in EU countries – only 2.8 hectares on average) does not allow either high specialization or high technological inputs.

The significance of human resources in food production is growing due to technological advancements. In the Croatian food production sector, human resources show some characteristics that are unfavourable for the creation of industry competitiveness: a low level of interest for the industry in general and bad education and age structures. The decreasing interest for the industry is visible in the constantly decreasing number of people interested in agriculture and food production as an occupation as well as in the decreasing number and size of farms. Only 4% of people employed in agriculture and food production have higher education degrees, and ⅓ of people employed in the sector are older than 55. These bad age and education structures significantly complicate the implementation of new technologies and human resources' active response to market impulses brought in by economic transition.

In comparison to EU countries, the technological competencies of Croatian agriculture and food production is lagging partly because of the inadequate quality of human resources and partly due to an underdeveloped food marketing system that lacks financial, distributional, and fiscal support. All these factors create an unfavourable investment climate, so that the investment ratio in agriculture is less than 10%. R&D expenses are about 10 times lower than in the EU, and even the research that is being conducted is mostly production, and not market-oriented (LEKO ŠIMIĆ, 2002). The long term low level of technological inputs into the food sector has preserved natural soil fertility that nowadays enables organic production, but, on the other hand, it has contributed to suboptimal productivity, higher production risk, and susceptibility to natural risks such as floods and droughts.

3. FOOD INDUSTRY CHARACTERISTICS

There are about 2800 registered food producers in Croatia. 85% of them are small size producers with fewer than 50 employees. There are a few "big players" comparable to multinational or regionally strong companies elsewhere in the world. These big companies have implemented the most modern technologies and developed strong technological and marketing competencies in both local and international markets. Very often they expand their core business activities into areas of agriculture and/or distribution. Through this they have built up enormous bargaining power in the Croatian food market.

There are still existing consequences of the war that affect food production. Mine fields are one of the reasons for unused fertile lands. Some companies still haven't fully recovered their infrastructure and production capacities. The breakdown of the former Yugoslavia has also downsized both supply and demand in the food market, so companies were forced to get involved in international business to grow and develop.

In addition to this, the non-systematic organization of food marketing system forces the majority of small food producers to disperse their production and market risk by diversifying production in type and size, which results in inconsistent product quantities and quality as well as small ratio of recognized, branded products with high added value. The most profitable Croatian food category products are produced by companies that were taken over by foreign multinationals (beer, beverages) or are non-food products (tobacco and cigarettes) or generic products with low value added (sugar, fish).

Another group of problems in Croatian food industry is related to the transition to a market economy and is evident not only in the food industry, but in other industries as well. However, some transitional problems are specific to the food industry. These are: unstable market conditions, non-existent market infrastructure, and an unspecified and undefined government role in the food marketing system. Inconsistent agricultural policy, changing laws on agriculture and food production and trade, exports and imports, and opaque and inconsistent fiscal system makes this economic activity a highly risky one in Croatia. Market infrastructure is underdeveloped in terms of financial support, since banks and other financial institutions are aware of these risks, especially with small producers, and are not willing to offer favourable credit lines for the sector. In terms of distribution, the few large companies that exist often get involved in vertical integration forwards, getting bargaining power and almost blackmailing small producers for a place in their distribution channels. There is also a lack of expertise for support in business development in agriculture and food production, especially in the area of marketing. Although the Ministry of Agriculture has created a network of expert teams for mainly agricultural production, this is mostly production-oriented, not market-oriented. This, combined with the bad educational structure mentioned above, creates a significant problem in the food production sector with low levels of technology implementation, innovativeness, and market-orientation. The government is still not fulfilling its role as a regulatory body, investor, or motivator for sector development and preparation for EU accession.

4. FOOD EXPORTS AND IMPORTS

Although boasting natural resources that could be turned into enough food production for about 20 million people (SHULTZ, CRNJAK-KARANOVIĆ and RENKO, 2005), Croatia has a foreign trade balance in food that is long term negative with an export/import coverage rate of only about 50%. The imbalance can be seen in *Figure 1*.

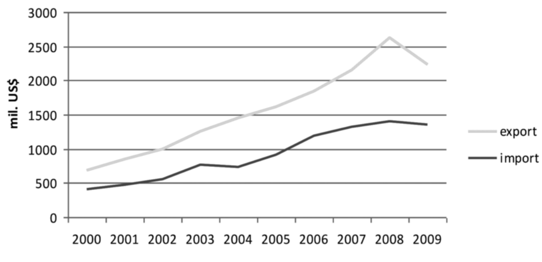

Fig. 1

Croatian food exports and imports

Source: CROATIAN NATIONAL STATISTICS BUREAU, 2010

This long term negative foreign trade balance is a result of uncontrolled food imports and exports. In qualitative terms, Croatian food exports are characterized by mainly passive exports of surpluses of mostly agricultural products or commodities and generic food products with low added value. As a result of inconsistent production quality and quantities, the same variations in exports and imports are evident. The most important export products are sugar (9% of total food exports), cigarettes and tobacco (7%), tuna (4%), and chocolates (4%) (CROATIAN CHAMBER OF COMMERCE, 2010). The top ten export food products make up 37% of total food exports, and none of these products belongs to the 6 products internationally recognized as branded foods of Croatian origin.

5. FOOD MARKETING IN CROATIA

The transition to a market economy has created an enormous pressure for change in the way of doing business. Traditional industries very often neglect and do not understand the need for market-orientation. Especially in the food industry, marketing activities are often seen as an unnecessary cost and not a worthwhile investment. Managers and company owners brought up and educated in a planned economy system often say that people have to eat, so they have to buy food. A study of the last decade in eastern Croatia, a region known for its tradition of food production has shown the following results (LEKO ŠIMIĆ, 1999):

- Of a total of 23 mid- and large-size food producers, only 13 have marketing departments (56.5%).
- 8 companies never do market research and 7 only occasionally do so.
- The most important marketing activity undertaken is participation in fairs and exhibitions.

As other research has shown (LEKO ŠIMIĆ and HORVAT, 2005), the low level of market-orientation results in low export performance and relatively bad performance on the local market.

Food marketing in Croatia can be analysed in terms of the 4P's. Among products, there is a high competition of foreign substitute products that are often cheaper and lower quality. The majority of really competitive local products are "oldies but goodies" – brand products with decades of tradition that still have a loyal consumer segment, like Vegeta, Gavrilovic salami, and similar brands. In comparison to imported products, local products are often more expensive, although often of better quality. However, in economic situation where about 35% of household income is spent on food (GFK, 2009), average consumers choose which products to buy primarily according to the price criteria. Within the whole food marketing system, "price scissors" often exist between agricultural products' prices that are government regulated and most food products and inputs to agricultural production prices that are market regulated. Promotion is considered to be very expensive and unprofitable marketing activity for food products, for the reasons mentioned above. Exceptions to this way of thinking are very large and foreign-owned companies. The majority of their promotion activities are concentrated on sales promotion and price-cutting advertisements. The distribution system is underdeveloped and enables large companies that have created not only their own production, but also their own distribution systems to have significantly stronger bargaining power than smaller producers. Smaller producers are often forced to accept bad terms of cooperation (production of private brands for the distributor, payment terms, etc.) if they want to enter a distribution channel.

6. STRATEGIC IMPLICATIONS

An efficient and effective food marketing system contributes to socio-economic welfare. A food marketing system evolves within the socio-economic, legal, cultural, and technological environment. The major components of food marketing system are institutions, processes, and functions performed by the actors of the system (KAYNAK, 2000).

According to the identified problems that create a suboptimal food marketing system, we note some strategic changes necessary to realize an efficient and competitive food production sector in Croatia, for which there is an evident natural resources potential. We have identified the need for structural changes in:

- ownership structure
- production structure
- market structure

A change in the ownership structure means a necessary enlargement of production units as a prerequisite for entrepreneurial, market-oriented production. This change will redirect the process from local consumption to market-oriented production. The current average size of an agricultural unit is less than 3 hectares, well bellow EU average. If we take into account only private farms, the average size is just 1.9 hectares.

Such production unit size doesn't allow higher investments in new technology, product specialization, and market-orientation in general. The average degree of marketability for basic food products in Croatia like meat, eggs, and milk, measured by the ratio of sold and produced goods, is only about 50%, while in EU countries it is 70-80% on average (KOLEGA, 1994).

Production structure change in the Croatian food sector would require replacement of basic crops (maize, grain) with other products for which there are resources and prerequisites and which can be developed into high-added-value and branded products (for example, organic food).

An efficient food marketing system has to be developed, especially in the area of supply chain coordination from agricultural production to food consumption.

All these changes require significant efforts on both macro and micro levels. On the macro level, it would be necessary to introduce adequate measures of economic policy to provide incentives for companies and entrepreneurs to get engaged in the food marketing system. Also, the existing actors in the sector need to implement actual, not merely formal, marketing concepts in the whole system of food production, processing and placement in order to ensure excellence.

These measures would help create sectoral competitive advantage through enabling and encouraging product and technology innovation, creation of high-added-value brand products, development of marketing and business skills, and a high quality food marketing system.

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