

The Avocado Market: A growth market in a mature food industry

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I think what I'm going to do is jump right into some of the conclusions at the outset to make sure that I get through them.

And you can see one of the conclusions if you read my title, which is that avocados in the United States are a growth market within a mature food industry. Now if you're going to be in a mature food industry, that's a position that you want to be in. You want to be one of the growth products that are around.

What do I mean by a mature food industry? We often use the term "saturated" as well. And, basically, what it means is, that in developed countries such as in the United States, Europe, and Japan, we tend to have low population growth rates, people are already well fed, and so they are not spending a lot more of additional income that they receive on food. However, what they do tend to do is to trade-up and purchase higher value products, higher quality, and more diversification in the diet occurs in developed countries.

Avocados are very fortunate in this regard because they are positioned as a higher value premium product in the United States, and are capturing growth in consumption from higher-income consumers, but from broader segments of the population as well. In particular, the Hispanic segment in the United States, which I'll talk a little bit about, which is growing very rapidly, as I'm sure all of you know, with a very high per capita consumption rate for avocados.

So we have several forces that tend to contribute to greater consumption of these items in the United States, despite the fact that in the aggregate we are a very slow-growth of the food industry, where everyone is competing for share of the stomach.

I want to just make one other point about that, because if we look at the fresh fruit and vegetable industry as a whole, the very large consumption items traditionally, such as apples and fresh oranges, have been experiencing stagnation and gradual decline in their per capita consumption rates over the last decade in the United States, because there are so many competing products now that consumers can choose from. And, the good news for avocados is that avocados are starting from a small base - you know we often talk about that as a negative - but on the other hand, if you're starting from a small base, you have room for growth potential, and avocados happen to be one of the types of products that people are diversifying toward.

I've said that avocados in the U.S. are in a good position, and so let's just take a snapshot of avocado utilization in the United States and how it has changed over the last decade. When I say utilization, I'm talking about U.S. production plus imports, so

I'm not subtracting exports, so it's not the same thing as consumption. And, what you will notice is that utilization has more than doubled over that time period, from around 154,000 metric tons back in 1994 to almost 322,000 metric tons in the year 2002 (Figure 1).

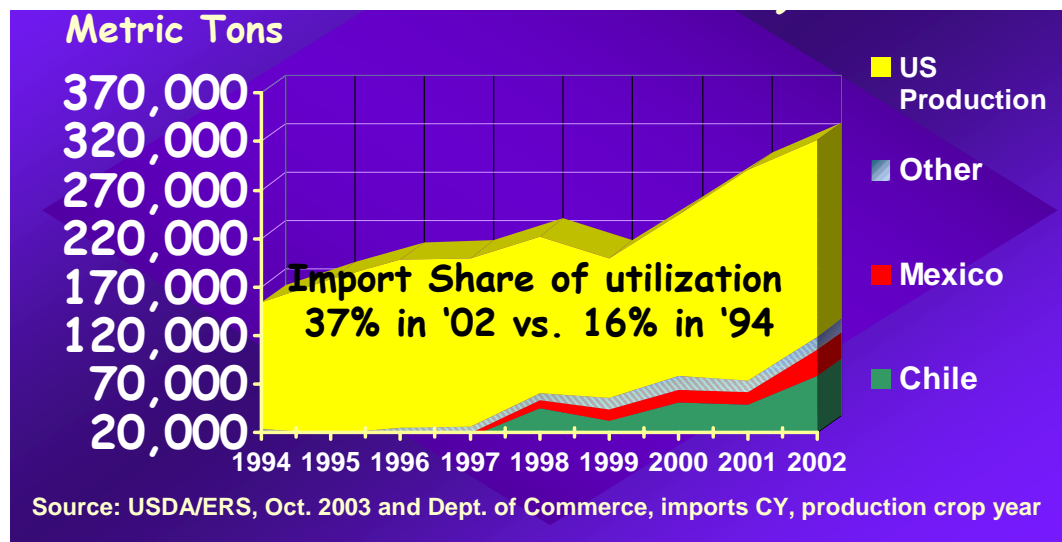


Figure 1. United States avocado production and imports from 1994 – 2002.

Keep in mind a little nuance in this. What I'm doing is I am utilizing USDA data for production, which is not on a calendar-year basis, it's on a crop-year basis beginning in November for the California crop, and I am combining that with calendar-year imports. So, it's an approximation.

But you will notice that imports also more than doubled during this period of time, now up to a 37% market share. But you should not think that production declined. Both production and imports were growing during this period. Sometimes you will see numbers that indicate that there has been a decline in U.S. production of avocados over the last decade, but that's only if you choose 1992-93 crop year as a base because that was a huge crop for California, way above historical standards. And so if you start in '93-'94 where the crop level was more normal, then there still has been growth in California over this period of time.

Now, of course, the big issue on everybody's mind is what will be the effect of Mexico gaining a broader market access to the United States. Mexico, everyone in this room knows, can produce close to a billion kilograms of Hass avocados per year. But we always have to keep in mind that the population of Mexico is approaching 100 million people, and that they have the highest per capita consumption rate of avocados in the world. Currently they're only exporting about 8% of the crop, and there are periods of the year in Mexico when, I think, prices can be higher in the domestic market than in the export market. And so, there's always that major issue of domestic demand increasing in Mexico as people receive higher income and diversify their diets over time, in contrast to the U.S. and Europe which, as I mentioned, are mature food markets.

So we have to keep that perspective in mind that there's a big domestic market at home in Mexico, which is not the case for Chile, which has a 13-15 million population and is, of course, much more export oriented. But I want to make a quick point about Chile relative to Mexico. When you look at these figures, which you can see with the relative shares is that Chile is the dominant source of imports into the United States, with about 2/3 of the total. And, of course, everybody likes to talk about the big growth that occurred in imports in 2002, both from Mexico and Chile. And you hear a lot of focus on the fact that Mexico more than doubled its exports to the United States over this period of time, which is true, and the rate of growth for Chile was not as large as it was for Mexico.

On the other hand, just the absolute volume increase that the United States market received from Chile in 2002 was larger than the total imports from Mexico, because avocado imports from Chile grew by about 29,000 metric tons, compared about 27,000 metric tons from Mexico.

What I would just point out to summarize on this point is that clearly there's going to be, as I am sure is no surprise to anyone here, greater market share battles for imports in the United States in the future, in particular between Chile and Mexico. Mexico with abundant supply throughout most of the year, and the opportunity to ship overland, gets the product here quicker, and with lower transportation costs. Certainly the foreign suppliers that have longer distances like New Zealand or South Africa will probably notice this increased competition over time.

Therefore, it will be very important to have orderly marketing in the U.S. market as these market share battles intensify over the next five years, so that the volume can be appropriately managed, and, certainly, it is important to always be demand driven as opposed to supply driven. So while there has been a positive situation for the industry in terms of expansion in demand, and we've seen an outward shift in the demand curve, as economists would say, which is a very good thing. But, on the other hand, producers can always over produce - we know this in all agricultural commodities - and expand supply at a more rapid rate than demand. That has not happened so far for avocados. We don't want it to happen in the future.

The per capita consumption level for avocados in the United States, as I mentioned earlier, is very low; it's about 2.3 pounds, a little over a kilo.

Now I want to turn away from those issues to talk about the overall marketing environment within which avocados and all food products are competing. And one of the items that is on everybody's mind is the increased level of concentration developing in food markets in the United States and globally. Figure 2 shows you a snapshot of what's happened in the United States; what it shows you is that, for a long period of time, there was not an increase in concentration ratios, and you notice that they started to jump up towards the latter part of the '90's. And I want someone to raise their hand and tell me why that was. I bet someone can do that. What effect was that?

The Wal-Mart Effect. Because Wal-Mart, with its super-centers and new mass-merchandising format that came into the U.S. industry in the 1990's, had major competitive impacts, and, really, all the retailers knew to combat this threat was to get bigger. They aren't necessarily streamlining their operating practices, as one would

expect, to really address the Wal-Mart threat, and I probably don't have a lot of time to go into that, but, nevertheless, the point is these firms did get bigger.

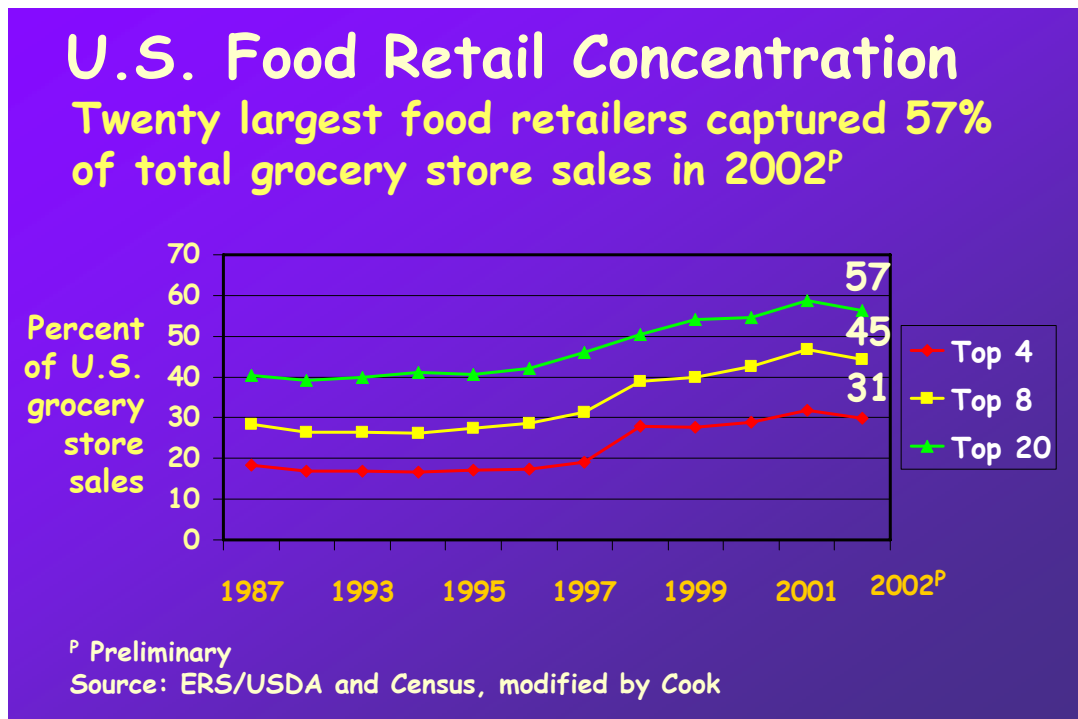


Figure 2. United States food retail concentration (1987 – 2002).

So we're in a situation now where we have twenty retailers who are responsible for purchasing about 57% of the total value of U.S. food retail sales, which is approaching \$50 billion, larger than the gross domestic product of a lot of countries. So that's pretty impressive, and that has important implications for suppliers, including suppliers of avocados, and it raises the issue of need for strategic alliances between suppliers to make sure that the market is supplied on a consistent basis, year-round, and that quality throughout the year is consistent, that we no longer have these early and late season quality issues. There's no reason to have that in the future, given the fact that the market will be more open, and the best sources of supply can be chosen at any point in time.

So let me just put the U.S. market in context. We talk about this high level of concentration that exists here, and people are concerned about it on the supply side. On the other hand, I just want you to recognize that the U.S. is an unconcentrated market relative to much of the world (Figure 3). There's much more that can be said about this, but I'll just make one brief point which is that there is globalization of retailing occurring, and that now we think there's thirty retail chains that are operating globally that have about 10% of overall food retail sales on a global basis. And that points out, again, the fact that we have these fewer larger buyers, and it will be important to work out on a more coordinated basis in the future.

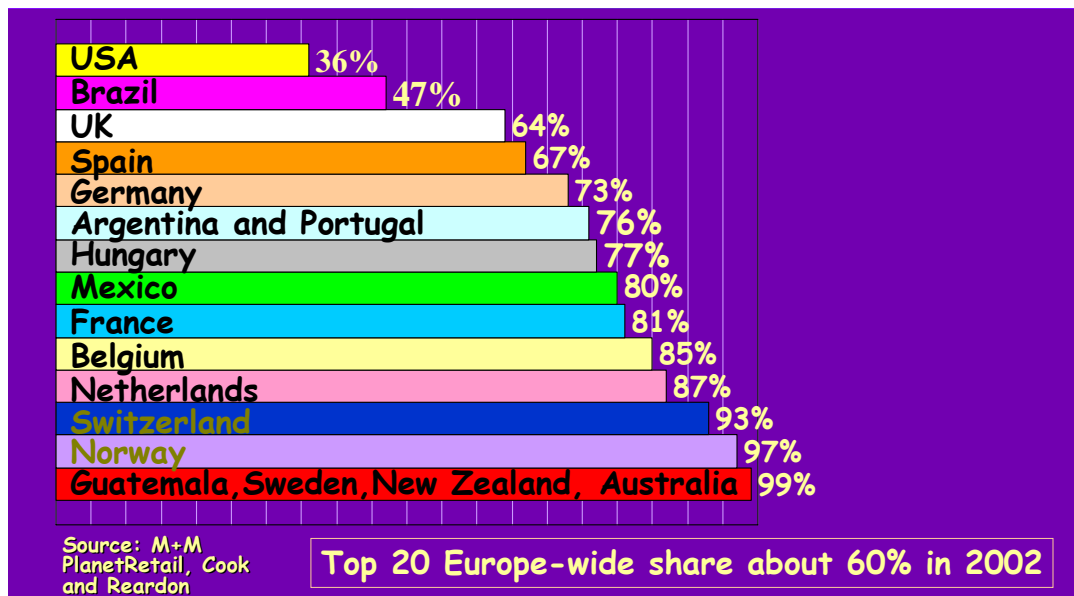


Figure 3. 2002 market share of the top 5 retail chains per selected country and the % of supermarket sales.



Figure 4. Key drivers in the food industry.

And so, to sum up that point, there are key drivers that are moving the food industry, and, if you follow the list down, you get to the bottom of declining role of the spot market. And, of course, we all know that fresh fruits and vegetables traditionally have been spot market orientated, daily sales oriented, but the trend is a movement towards contracts, and dealing with a smaller number of suppliers. Retailers want to deal with a smaller number of suppliers for the same product or product line, and they want those suppliers to put together the consistent sourcing services for them.

Therefore, it's important, if you're thinking about exporting to the U.S. market, to think about working through suppliers who already are involved with retailers on a contract basis, and who have a streamlined distribution system in place. Those are the types of suppliers that will create less chaos and more orderly marketing.

Some general points about what else is happening in the U.S. industry. You have to understand that the U.S. retail industry is becoming increasingly competitive - not that it was not in the past - but it has been threatened over the last thirty years by growth in food service, demand, and we have a phenomenon called "[channel blurring](#)", which is causing the retail landscape to be over-stored. And, again, food service channels are competing with all kinds of food retailing: the newer ones and the conventional ones as well.

So what does that mean? It means that conventional retailers must identify value propositions if they are going to remain viable in the future. And one of the ways they do that is they focus on fresh produce, because fresh produce is something that has color and excitement - it's not the same as a can of beans. And so it gives them the ability to differentiate themselves relative to the competition. And they can do things now, and are more interested in programs like handling ripe avocados as part of that process. So, there's a lot of positive forces in the food distribution system, in that sense, for the avocado industry.

And the other thing is that food service demand is growing rapidly in the United States. We have the biggest food service industry in the world, but the world is beginning to catch up to the U.S. food service industry as more people in all countries are eating out away from home. We don't really know in the United States, I understand from the Avocado Commission, exactly what share of production goes into food service, but the estimates are 20-40%, and that, certainly, will grow in the future.

So the bottom line is, more structural change is expected in the U.S. in the global grocery industry, and there will be more pressure on suppliers. But on the other hand, these buyers that are interested in working with preferred suppliers are more and more willing to cooperate with suppliers on information-based programs designed to increase retail sales and profitability.

And that's where I think the good news exists for the avocado industry, because you spend more in promotion than most other fruits and vegetables, and have better information systems in place than most other fruits and vegetables. That has been developed by the California Avocado Commission, and is something that is now going to be to the benefit of the entire industry supplying avocados to the U.S. market through the [Hass Avocado Board](#).

So, I think that you are well positioned to be able to capture this growth. Thank you very much.