CHAPTER 3
Foreign Direct Investment in the Processed Food Sector

The Concept and Scope of Foreign Direct Investment

In addition to trade in goods themselves, such as processed foods, there is a large volume of international exchange of capital and technology used for food manufacturing and distribution. Modern measures of a country's or a firm's international competitiveness incorporate sales from foreign affiliates of home-country firms in addition to international trade (Horstmann and Markusen 1987, Kravis and Lipsey 1992, Porter 1990). Foreign affiliation can occur in various ways: license production to a foreign firm, franchise a foreign firm to market products under the home firm's trademark, acquire a minority interest in a foreign firm, develop a joint venture with a foreign partner, or obtain complete or majority ownership of foreign operations.

For purposes of this report, foreign direct investment (FDI) refers to investment in a foreign affiliate. The term "foreign affiliate" is used to identify a foreign entity in which a parent firm holds a substantial (but not necessarily majority) ownership interest. Parent firms are referred to as multinational firms or corporations (MNC's). U.S. firms' investing in production facilities in other countries is known as outbound FDI, while foreign firms' investing in facilities located in the United States is known as inbound FDI. Foreign direct investment is distinctly different from foreign portfolio investments and other international capital flows such as bank deposits. Portfolio investment takes a passive management role and does not seek control over decisionmaking within the firm. Foreign direct investment, by contrast, is defined as the ownership of assets in an affiliate by a foreign firm for the purpose of exercising control over the use of those assets. Since we are interested in the outcome of investing in foreign affiliates, we use sales of foreign affiliates as our primary measure of FDI. Using affiliate sales as an indicator of

FDI facilitates comparing the relative size of FDI and trade as strategies for accessing foreign markets. Using affiliate sales instead of "foreign direct investment position" (essentially the book value of assets) also avoids the problem of valuing assets of different vintages.

The source of FDI data at the industry level is the U.S. Department of Commerce, Bureau of Economic Analysis. The Department of Commerce defines foreign investment as direct when a foreign firm has a stake of 10 percent or more in a host country operation and no other firm has as large a share. The 10-percent ownership threshold reflects the notion that a foreign parent will normally have a strong say in the decisionmaking of a firm even if that parent does not own a majority stake. Other researchers have argued for a more restrictive 50-percent ownership cutoff to define foreign direct investment. But the difference in definition is minimized by the fact that the vast majority of FDI is majority owned. In 1992, 84 percent of U.S. food-processing affiliates in foreign countries were majority owned; and conversely, 98 percent of foreign-owned affiliates in the United States were majority owned by their foreign parents.

Furthermore, most FDI occurs by acquisition or merger rather than by building new facilities (known as greenfield investment). The country receiving FDI gains from the investing firm's knowledge in technology, marketing, management, finance, and information services. The gain in employment and economic activity is most obvious from greenfield investment. But even when FDI 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 capacity increases sufficiently, net employment increases even with improved labor productivity.

FDI by acquisition does not necessarily increase employment, technology, or product variety in the receiving country. Parent firms frequently buy leading brands produced by a firm in the host country. Motivations for the parent firm are to increase international volume, increase growth rate, and achieve the competitive advantages of owning a leading brand in a new market.

In this situation the parent firm often gains new product and marketing technology from the acquired firm. Thus technology flows become two-way. By acquiring a leading firm or brand in the host country, the parent firm avoids a major disadvantage of greenfield FDI, by achieving immediate economies of scale. Examples are Grand Metropolitan (UK) buying Pillsbury in the United States and Philip Morris buying Jacob Suchard, one of Europe's largest confectionery firms.

Direct foreign investment can also be classified as vertical or horizontal. An example of vertical FDI is a parent firm investing in successive stages of production, either upstream (away from final consumption) or downstream (toward final consumption). An example of upstream FDI by a food manufacturer would be investing in can manufacturing or in agricultural commodity production. Downstream FDI would include a flour miller's investing in a wholesale baking operation or retail foodstores.

Tables 13 and 14 give an overview of the relative size of outbound and inbound FDI as reflected by affiliate sales for the entire food-processing sector and for the major industries within the sector.

Sales from outbound FDI remained slightly higher than sales from inbound FDI throughout the 1982-93 period. Sales from all U.S. food marketing affiliates abroad totaled $132.5 billion in 1993 (table 13), while sales from foreign-owned food marketing affiliates in the U.S. were $124.3 billion (table 14).

The composition of outbound versus inbound FDI varies widely by type of industry. Food-manufacturing affiliates account for 72 percent of sales of all U.S. food-marketing affiliates abroad. But food manufacturing accounts for a much smaller 37 percent of total foreign-owned affiliate sales in the U.S. food marketing sector. For the food-retailing industry, just the opposite is true. Sales from U.S. food-retailing affiliates abroad account for just 9 percent of total affiliate sales abroad, while U.S. food-retailing affiliates of foreign firms account for 42 percent of sales of foreign-owned food-marketing affiliates in the United States.

The next section examines factors that help explain or incentives for firms to engage in FDI. This is followed by a more detailed industry-by-industry review of the general trends in FDI discussed above.

Factors Influencing Foreign Direct Investment

FDI in Historical Context

Foreign direct investment is the dominant form of international commerce in processed foods. This is in sharp contrast to global commerce in agricultural commodities where trade dominates and FDI is nearly invisible. It also contrasts sharply with neoclassical international economic theory that does not reveal incentives for FDI in a perfectly functioning world of free trade.

This section addresses factors that explain FDI. While theoretical explanations for FDI tend to be eclectic, empirical observations of incentives for firms to operate facilities abroad tend to be generally consistent with the major strands of theory. Indeed, a number of empirical studies of the determinants or motivations for FDI have been reported. These reveal several consistencies that can be viewed as empirical regularities. These empirical regularities form the foundation for our contemporary understanding of what gives rise to FDI in processed foods, and shed considerable light on why

Table 13—-Sales by U.S.-owned food marketing affiliates abroad by industry, selected years, 1982-93

Industry	1982	1987	1992	1993	Share of total
		Million dollars			*Percent*
Food manufacturing	39,023	50,067	89,159	95,782	72.3
Food wholesaling	6,172	9,206	14,388	15,783	11.9
Retail foodstores				11,930	9.0
}	8,691	9,674	21,169		
Eating & drinking places				9,007	6.8
Total, all food marketing	53,886	68,947	124,716	132,502	100.0

Source: Dept. of Commerce, BEA.

FDI is the preferred method of market globalization for these products.

The balance between portfolio and direct foreign investments changed markedly during the past century, with the United States playing a major role. An examination of the change suggests the underlying impetus of FDI and why FDI is particularly important for processed foods.

Until the First World War, nearly all international investment was portfolio; the United Kingdom supplied about half of the world's total, followed by France and Germany. Younger, rapidly expanding economies, primarily the United States, Canada, Australia, and Latin America, were the primary recipients. Yet, even before WWI, outbound American investment was getting underway.

From the outset, U.S. investment was different. As described by Södersten and Reed (1994, p. 468), "American investors seem to have been of a more dynamic type, not content to reap a fairly small interest-rate differential. Even before the First World War a dominant share of U.S. capital exports consisted of direct investments." In short, from the beginning, Americans investing abroad have shown a propensity to transfer know-how (or intellectual capital), more so than financial capital.

Between the world wars, international investment declined. But, the United States began to emerge as a major source, primarily of direct

Table 14—Sales by foreign-owned food marketing affiliates in the United States by industry, selected years,1982-93

Sector	1982	1987	1992	1993	Share of total
	Million dollars				*Percent*
Food manufacturing	14,847	22,862	46,799	45,765	36.8
Food wholesaling	7,039	13,953	18,984	21,734	17.5
Retail foodstores }		24,312	48,159	51,537	41.5
}	18,758				
Eating & drinking places }		498	4,904	5,236	4.2
Total, all food marketing	40,644	61,625	118,846	124,272	100.0

Source: U.S. Department of Commerce, BEA.

investments as American industrialists began to establish foreign operations in the image of their pre-Depression home-market successes. Following WWII, the United States became the primary supplier of international finance, first in the form of official loans and gifts, and second in the form of FDI as American firms made major contributions to postwar industrial rebuilding. By 1960, the United States was supplying about two-thirds of all international investment. By the 1980's, observing U.S. industrial success throughout much of the free world, other countries—principally those of the European Union and Japan—became more aggressive in exporting their management technology through FDI, much of which landed in the United States. By the 1990's, with the fall of Soviet communism and the liberalization of third-world economies, FDI became the main instrument for global industrialization. As the 20th century ends, the nationality of multinational firms—the organizational result of FDI—has blurred in many cases to the point of being indistinguishable.

Profits that firms can earn in their international operations appear to be a motivation for FDI. This is evident in a sample of 144 food-processing firms worldwide used by Henderson, Vörös, and Hirschberg (1996) to compare profitability based on sales from foreign affiliates. In that sample, sales from foreign affiliates exceeded exports from home countries by a ratio of 5 to 1. For firms with foreign sales equal to or exceeding 35 percent of total sales, net income as a percentage of assets was higher than for firms with foreign sales below 35 percent of total sales. In short, FDI occurs because a firm has some advantage it can exploit in foreign markets. In the food and agricultural sector, such advantage is more often a feature of processed foods than of basic commodities. The following analysis offers insight into why.

Determinants of FDI

Evolving developments in the theories of international economics accommodate conditions of imperfect competition such as those observed in processed food markets (product differentiation, for example, and economies of scope, scale, and size). Theoretical constructs help identify the motivations for firms to engage FDI.

These developments have been joined by an expanding body of empirical studies that reveal product, firm, industry, and/or country idiosyncracies that are associated with observed configurations of FDI. The major constructs and empirical findings reveal general patterns that characterize the dominant forces behind FDI in processed foods.

Theoretical Considerations

A number of theoretical developments contribute to our understanding of the determinants of FDI. Early on, Vernon (1966), in his work on the product-cycle hypothesis, advanced an explanation for FDI based on product differentiation. The essence of this hypothesis is, if a firm expands to a foreign market in early stages of a product life cycle, it typically does so through exports. But, as growth in production and sales expands, a firm finds it must nurture increasingly-close working relationships with both suppliers and distributors. The greater the product uniqueness (differentiation), the more important these special relationships. Firms often find that they can best manage such special relationships in foreign markets with on-site facilities, thus they engage in foreign production (outbound FDI). Subsequently, the importance of product differentiation (and other unique, firm-specific attributes) has become a central theme in theories of FDI.

Buckley and Casson (1976) extended Vernon's construct by emphasizing imperfections in the foreign upstream or downstream markets. Where needed inputs or merchandising and distribution methods (marketing services) are highly specialized, markets for those supplies or marketing services may be difficult to organize. This is particularly so in the presence of uncertainty over demand, high investment costs, and the need for rapid exchange of information, close coordination, and joint planning. Faced with imperfect external markets, firms elect to internalize the supply of these critical inputs or distribution and merchandising services, thus entering into outbound FDI in vertically-adjacent sectors.

Caves (1982) posited that many of the attributes associated with a firm's unique product(s) are intangible (examples include, technical production or merchandising knowledge, brand names, trademarks, team-specific management skills, special relationships with suppliers and customers). Because they are intangible, it is difficult for a firm in one country to sell them to a firm in another country. Thus, the firm has an incentive to develop overseas operations to capture the full earnings potential of these unique attributes in foreign markets.

Synthesizing several conceptual strands, Dunning (1977) advanced the *OLI paradigm* as an eclectic theory of FDI. OLI represents *ownership* advantages, *locational* considerations, and *internalization* gains. Ownership advantages are those firm-specific assets, such as the intangible assets discussed by Caves, that give a firm a competitive edge over both domestic and foreign rivals. Such intangible assets are also considered to be a firm's intellectual property or intellectual capital. Locational considerations encompass such things as transportation costs and import restrictions that give a firm a cost advantage for operating in a foreign market. Internalization gains concern factors that make it more profitable to carry out transactions within a firm than to rely on external markets (as in the Buckley and Casson construct, above). Dunning's theory holds that all three conditions are necessary; together they are sufficient motivation for a firm to invest in direct foreign production.

Ethier (1994) introduced refinements to the OLI paradigm that reveal an expectation for the major flows of FDI between countries with relatively similar economic conditions. In the presence of ownership advantages (firm-specific assets) that can be emulated over time, and a high ratio of international transportation to host-country labor costs (locational consideration favoring host-country production), a firm is motivated toward FDI in order to internalize earnings accruing to ownership advantages, thereby reducing the chance of copying by a host-country firm. However, if, for example, host-country wages and salaries are sharply lower than in the firm's home country, a copycat host-country firm can pose a credible threat to sustained earnings from direct entry by the external firm. Knowing this, the external firm will engage FDI in the host country only if it believes that the wage difference is not great enough to offset copying costs (industrial intelligence) by a host-country firm. Therefore, FDI partner countries are expected to have different *but not greatly different* economic conditions (such as labor costs).

Empirical Studies

Empirical studies of the determinants of FDI have been hampered by two factors, a relative scarcity of detailed data on FDI, and complexities in measuring a number of the variables that are hypothesized to affect FDI in the various theoretical constructs (such as firm-specific advantage). Nonetheless, enough studies have been reported—some specific to processed foods—that stylized facts, or empirical regularities, can be raised.

In an early study of the shares of affiliates of U.S. firms in the outputs of Canadian and British industries, Caves (1974) found a statistically significant positive relationship between these shares and a set of factors taken to reflect firm-specific (ownership) advantages (such as experience with multi-plant management, expenditures on research and development (R&D), and advertising intensity). Wolf (1977), in a study of the share of production by U.S. firms accounted for by foreign operations, found this to be positively associated with a firm's technological expertise (as measured by the proportion of engineers and scientists in a firm's workforce) and size of firm.

A number of other studies have documented similar findings. Grubaugh (1987) reported results from an study of 300 U.S.-based multinational firms that tie FDI directly to relative levels of firm expenditures on both R&D and advertising. Handy and MacDonald (1989), using cross-sectional data on 32 U.S. manufacturing industries, also found positive impacts of R&D and home advertising on FDI, as did Yu (1990) in another study. Dunning (1981) cited evidence of a positive relationship between the value of a firm's intangible assets and FDI. Ray (1991), in a study of 32 manufacturing industries in five countries, found FDI positively related to specialized human capital, managerial intensity, and share of home market. In a study of 27 industries in 30 countries, Baldwin

(1979) found that product differentiation, managerial intensity, and home market share affect FDI.

Specific to processed foods, Connor (1983), using data on U.S. food-manufacturing industries, documented positive impacts of firm size, advertising, R&D, and home market share on FDI. Using pooled, cross-section, time series data for 628 food manufacturers in 16 countries, Henderson, Vörös, and Hirschberg (1996) found intangible assets, product differentiation, firm size, and home market share positively associated with FDI. Overend and Connor (1994) examined factors influencing FDI patterns for a cross-sectional sample of 33 U.S. food-manufacturing firms that also do business in the UK. Their findings show a positive relationship between a firm's investment in foreign marketing expertise and FDI. Ning and Reed (1995) examined factors explaining the location of U.S. FDI for a sample of six developed countries from 1983 to 1989. They found cultural linkage and trading bloc memberships are major incentives for FDI abroad, followed by a strong home currency, fast foreign market growth, and low foreign income tax rates.

Regarding national characteristics, Veugelers (1991), in a cross-sectional study of FDI patterns in OECD countries, found positive effects on FDI of common borders and similarities in culture, language, stage of economic development, labor costs, and trade policies between host and home countries. For processed foods, Handy and Henderson (1994) have shown that the same set of economically advanced countries (the U.S., Canada, Japan, and the countries of the European Union) account for nearly all of the world's FDI, both inbound and outbound.

Principal variables related to FDI are summarized in table 15. When viewed in the context of the food and agriculture sector as a whole, reasons for the relative importance of FDI to global commerce in processed foods become clear. Processed foods are highly differentiated products, the result of considerable effort by food manufacturers, distributors, and food service firms to develop a steady flow of new products and product innovations, and to intensely merchandise these products through advertising and other means of promotion. Global commerce tends to occur primarily among countries that are remarkably similar in overall economic character, yet whose firms have sufficient differences in intellectual property to differentiate their operations and products from those of rival firms in both home and international markets. This stands in sharp contrast to global commerce in agricultural commodities, where the dominant pattern is international trade in undifferentiated goods between fairly dissimilar countries.

Foreign Direct Investment in Food Manufacturing

Investment Abroad by U.S. Food Manufacturers

Most large food manufacturers rely much more heavily on foreign direct investment than on exports from their home country to access foreign markets. In 1993, the latest year in which industry-level data are available from the Bureau of Economics Analysis, 64 U.S. multinational firms held at least 10 percent equity in 762 food manufacturing affiliates in foreign countries. Figure 4 shows the relative value of shipments from U.S.-owned food-manufacturing affiliates abroad compared with the value of total processed food exports from the United States. Foreign affiliate sales have long exceeded the value of U.S. exports, but since 1985, the gap has

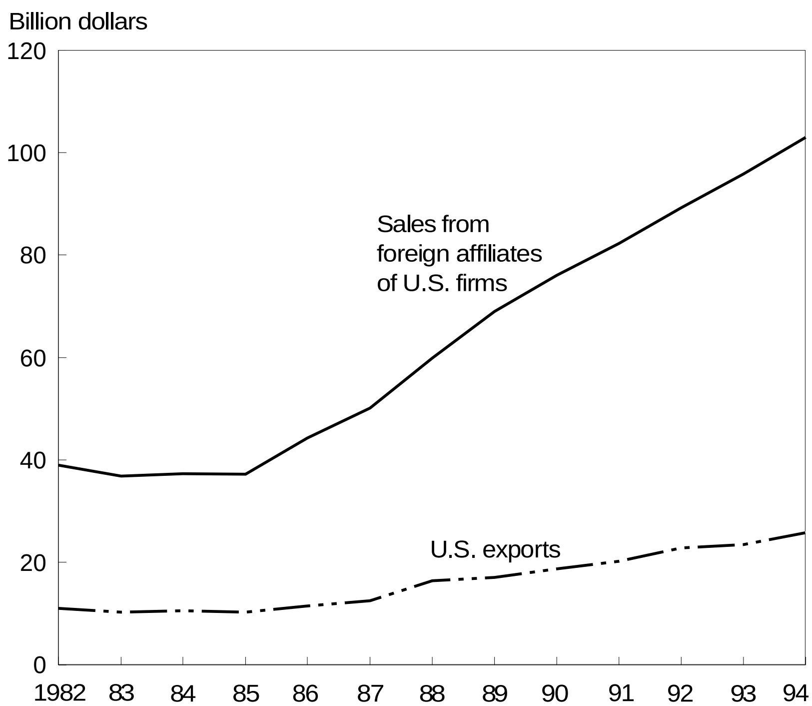
Table 15—Factors positively influencing sales by foreign affiliates

Factor	As measured by
Product and process innovation	Expenditures on research and development
Product differentiation	Advertising expenditures
Intellectual property	Value of intangible assets
Managerial skill and intensity	Value added as a share of value of shipments; employee educational level
Foreign Marketing expertise	Foreign sales as a share of total sales
Home market success	Market share
Economies of size, scale or scope	Size of firm
Locational advantage	Transportation costs as a share of value of sales; ratio of transportation to host-country labor costs
Trade barriers	Tariffs
Size of host market	Growth in real GNP per capita

widened. 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 FDI nor exports grew in the early 1980's. Since then, both have recorded uninterrupted growth. From 1982 to 1993, sales from U.S. affiliates abroad grew 145 percent to $95.8 billion, while U.S. processed food exports increased 113 percent to $23.4 billion. By 1994, sales from foreign affiliates are estimated to have reached $103 billion—4 times larger than U.S. exports of $25.8 billion. Employment in U.S.-owned affiliates increased at a slower rate than sales. The number of employees at U.S. affiliates in foreign countries grew from 447,700 in 1982 to 550,500 in 1993, an increase of 23 percent. Most U.S. affiliates abroad are majority-owned by their U.S. parents. Of the total sales of U.S. affiliates abroad, 83 percent ($79.9 billion) came from majority-owned affiliates.

Figure 4

U.S. exports and foreign affiliate sales of processed food



Source: Economic Research Service, USDA.

Location of Affiliates

U.S. foreign direct investment is concentrated in developed countries (table 16). In 1993, European countries accounted for $54.4 billion (57 percent) of total U.S. affiliate sales abroad. Within Europe, the United Kingdom is by far the largest recipient of U.S. FDI followed by Germany, Netherlands, and France. Adding Canada and Japan to the European countries brings the share of U.S. 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. Sales from U.S. affiliates declined in both South and Central America from 1982 to 1987, but have grown rapidly since. From 1987 to 1993, sales from U.S. affiliates in South America doubled and sales from U.S. affiliates in Mexico increased 282 percent.

Further evidence of growing U.S.-owned food-processing operations in developing countries is available from a data base of over 75 large U.S. food-processing firms maintained by USDA's

Table 16—Sales by U.S.-owned food processing affiliates abroad, 1982-93

Country/ region	1982	1987	1992	1993	1993 share	Change 1982 -93
		Million dollars			*Percent*	
Total, all	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

NA= Not available.

[1] Withheld by BEA to avoid disclosure.

Source:Dept. of Commerce, BEA.

Economic Research Service. In 1993, a subsample of 39 of these firms operated over 860 food-processing plants in foreign countries. Roughly one-third (about 295) of these plants were in developing countries, with over 200 plants in Latin America. U.S. firms are also increasing investments in Eastern and Central Europe, the former Soviet Union, and China. According to data compiled by ERS from media and company reports, at least 35 U.S. food manufacturers had invested in over 70 food-processing affiliates or joint ventures in these countries as of 1995. In China at least 29 U.S. companies had invested in food-processing operations.

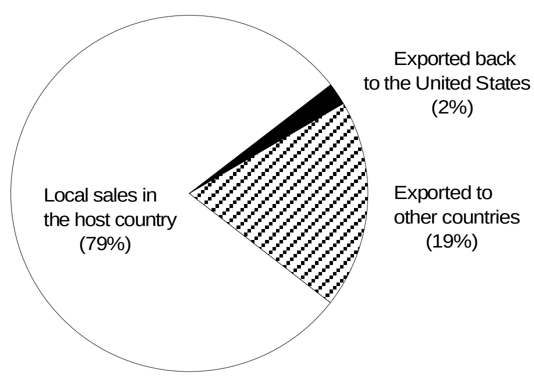
Specialized engineering, packaging, and food ingredient firms facilitate foreign direct investment by making technology readily available and mobile across national boundaries. With the help of these specialty firms, food processors can pick and choose the best technology for specific functions from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

U.S. firms are continually reassessing and adjusting their foreign direct investment position by buying or building new plants overseas, consolidating existing plants, or divesting entire lines of business. From the ERS firm-level data base, observations are available on a constant sample of 32 U.S. multinational food processors for the years 1988-93. The total number of food-processing plants operated by these 32 MNC's increased from 1,955 in 1988 to 2,078 in 1993. All the increase came from foreign plants. The number of U.S. plants declined from 1,312 to 1,265 as these firms consolidated U.S. production into larger plants. At the same time, the number of majority-owned plants operated by these firms in other countries increased from 643 (33 percent of the total plants) to 813 (39 percent of the total). Nineteen of these 32 firms increased their number of foreign plants, 8 firms had no change, while 5 firms decreased the number of plants they operate abroad. During this time, 7 firms withdrew entirely from one or more foreign regions (such as the Middle East), while 8 firms entered new foreign regions for the first time. The number of firms that had at least 50 percent of their food-processing plants located in foreign countries increased from 8 to 14. CPC International, manufacturer of Knorr, Hellmann's, and Mazola products, had 95 of its 123 plants (77 percent) located outside the United States in 1993. Philip Morris (Kraft General Foods) had the largest absolute number of foreign plants with 119 of its 251 plants located in foreign countries**.**

Destination of Affiliate Sales

In general, U.S. food-processing MNC's do not establish affiliates abroad for the primary purpose of exporting product to the U.S. market (fig. 5). Of total U.S. affiliate sales abroad in 1993, 79 percent remained in the host country (local sales) while 21 percent came from sales to other countries (BEA 1995A). But only 2 percent ($1,885 million) of affiliate sales were to the United States. By comparison, U.S. non-food manufacturing affiliates abroad exported an average of 14 percent of their total shipments back to the United States.

Figure 5
Sales by U.S. owned foreign affiliates by destination, 1993



Total sales by U.S. affiliates abroad $95.8 billion

Source: Economic Research Service, USDA.

Proximity of foreign affiliates to the United States plays a large role in explaining their export behavior. Even though Canada accounts for only 11 percent of U.S. affiliate sales worldwide, it accounts for 40 percent of affiliate exports 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 have 60 percent of all affiliate sales, but their share of affiliate exports to the United States is only 25 percent.

Intra-firm trade between U.S. parents and their affiliates is substantial. While U.S. affiliates abroad export only 2 percent of their sales to the United States, most of these exports (71 percent) are shipped to their U.S. parents, with the remaining 29 percent shipped to other firms in the United States. Exports from the United States to its food-processing affiliates abroad were also relatively small ($2,582 million) in 1993, but were still considerably larger than imports from those affiliates. Again, U.S. parents accounted for most (79 percent) U.S. exports to their affiliates.

Operations of Foreign Food-Manufacturing Firms in the United States

A rapid increase of foreign direct investment into U.S. food-processing industries was a phenomenon of the late 1980's. Foreign direct investment into the industry doubled between 1987 and 1992, and left 12 percent of the industry foreign-owned. The United States received large capital inflows in 1989, especially

Table 17—Sales by foreign-owned food processing affiliates in the United States, 1982-93

Country of origin	1982	1987	1992	1993	Share, 1993	Change, 1982-93
	Million dollars				*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

Source: Dept. of Commerce, BEA.

when the UK's Grand Metropolitan purchased Pillsbury. Japan's appearance in the U.S. food industry in the late 1980's was also a break from the past. While there were no megadeals in the U.S. food industry in the early 1990's, 1993 activities included UK's Cadbury-Schweppes' acquisition of A & W Beverages and Unilever's (Netherlands) acquisition of Kraft Foods Ice Cream Industries and Klondike. In 1994, Sandoz, a Swiss pharmaceutical company, acquired Gerber Foods.

These foreign acquisitions made their impression on the U.S. food industries through sales, employment, and foreign trade. Sales of U.S. affiliates of foreign firms were $46.8 billion in 1992, triple the level of 1982 ($14.8 billion). Sales declined slightly in 1993 to $45.8 billion (table 17). Nearly all sales from these foreign-owned plants remained in the United States, indicating that they were targeting the U.S. market; only $2.2 billion (4 percent) of those sales were exports (BEA 1995B). Moreover, only a third of the exports from these plants were shipped to the foreign parent company. U.S. affiliates of foreign companies imported more processed food products ($3.2 billion) than they exported. And nearly half of the imports to these affiliates came from the foreign parent group. Foreign companies generally found it less expensive to locate production of many high-value products closer to the U.S. market than to the foreign source of the raw product. Foreign direct investment in the United States was also one way to circumvent some U.S. trade barriers.

European companies dominate as a source of inbound investment and sales (table 17). 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. Japan raised its presence to 13 percent of the sales from foreign firms in the U.S. food industries, compared with Europe's 68 percent. Canada's share declined over the decade to 11 percent in 1993.

There is some variation among countries in their choice of products. Japanese companies have purchased or built plants that mostly produce their ethnic foods such as noodles, surimi, soy sauce, sake (a rice-based alcoholic beverage). They have also ventured into

Mexican-style frozen dinners and wine. Food and feed additives are also important Japanese investments, along with cutting-edge biotechnology as it relates to food. Japanese investors were more apt to start up new businesses than their European and Canadian counterparts.

European companies are broader based. Wine, cheese, chocolate products, and bottling plants are some of the enterprises of their U.S. affiliates. Grain products, frozen and canned vegetables are also included. Some chemical companies have also become important producers of food and feed additives. Recent investments of European conglomerates have cut across product lines.

Canadian investments are mostly in the U.S. distilled spirits industry. In recent years they have expanded into wines, fruit juices, and frozen foods. More recently, some Canadian companies, acting as conglomerates, expanded their investments into many nonfood areas, principally chemicals and entertainment.

There is a variation in the market share of the U.S. affiliates in relation to their industries. Overall, the market share of foreign-owned companies in U.S. food-processing industries is about 12 percent (BEA, 1995B). Foreign-owned companies have roughly one third of the U.S. market share in cookies and crackers and edible fats and oils. In comparison, foreign-owned distilled liquor plants have one-half of the industry. Foreign-owned dairy products and canned specialties comprise 10-15 percent of those industries.

In addition to geographic and market concentration, a number of general observations can be drawn from the study of the Department of Commerce data on FDI in U.S. food processing. Most FDI is horizontal rather than vertical. Food processors invest primarily in other food-processing facilities rather than in upstream or downstream operations. Second, most FDI outlays are to acquire existing facilities rather than to invest in newly constructed operations.

Inbound foreign direct investment has brought jobs to the U.S. food industries. U.S. food-processing affiliates of foreign companies employed 200,000 persons, who were paid nearly $5.5 billion, for an average salary of about $27,500 in 1993. This compares with the 1982 employment of 126,000 persons who earned $2.5 billion (nominal dollars), for an average salary of about $20,000. Employment in foreign-owned companies is nearly 12 percent of the total employment of the sector, compared with 7.7 percent in 1982.

These trends show the importance of sales of affiliates of other countries since 1980. Foreign direct investment will likely continue to grow, and companies will be morely likely to expand their markets through their foreign affiliates rather than through exports and imports. World trade in food products has increased since 1980, but sales of foreign affiliates has increased faster.

Foreign Direct Investment in Food Distribution

The food distribution industries include food wholesalers and brokers, and food retailers. Both inbound and outbound investment levels have grown steadily over the past decade.

Food Wholesaling

Sales from foreign affiliates of U.S. grocery wholesalers (outbound FDI) increased to $15.8 billion in 1993, a 9.7-percent increase over 1992 and a 156-percent increase from 1982 (table 13). Sales from U.S. grocery wholesale affiliates owned by foreign firms (inbound FDI) increased to $21.7 billion in 1993, growing 14.5 percent from 1982 (table 14).

Many food wholesaling firms have expanded via joint ventures in foreign markets. Sam's Warehouse Club is the leading wholesale club in the United States. Facing saturated markets in the United States and unfulfilled demands globally, Wal-Mart, Sam's parent firm, has been particularly aggressive in this regard with expansion plans for Asia and South America. As part of its first move outside of the Western Hemisphere, Wal-Mart set up a Hong Kong joint venture in 1994 as a foundation for further expansion into the Far East. The joint venture is part of a plan to open Value Clubs as a stepping stone into China. Value Club is a joint venture with Ek Chor Distribution System Co. Ltd., a Hong Kong subsidiary of Bangkok-based C.P. Pokphand Co. Value Clubs are smaller versions of the Sam's Club membership warehouses. Plans called for construction of two units in China in 1995. In addition to expansion plans in Asia, plans called for an additional 10 to 12 warehouse clubs and 10 to 12 supercenters in Mexico. Wal-Mart also plans to open Sam's Clubs in Brazil, through a joint venture with Brazil's major retailer Lojas Americana, and Sam's Clubs is in the first phase of its expansion program in 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 7 warehouses 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 king of foodservice distributors, Sysco Corp., has a company in British Columbia called Sysco/Konings Wholesale. Another leading foodservice distributor, Rykoff-Sexton, operates a Mexican distribution center.

Food wholesaling industry-leader Fleming formed a joint venture with Davids Holdings, the leading wholesaler in Australia. The joint venture, Davids Investments Asia Plc. Limited, was formed to establish full-line distribution centers in Asia. Fleming expects the joint venture also to help with its exporting and importing activities. Fleming has foreign affiliates in the Caribbean, Japan, Mexico, Korea, and the former Soviet Union.

Food Retailing

Inbound Investment

Sales by U.S. food-retailing affiliates of foreign firms reached $51.5 billion in 1993, according to the most currently available data (table 14). Food-retailing affiliate sales amounted to 13.4 percent of total U.S. food store 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 18). Fourth-ranked nationally Albertson's (Boise, ID) was the largest U.S. affiliate, with sales of $11.9 billion in 1994. U.S. affiliates 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 (eighth-ranked nationally) have 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 Tenglemann (Germany), have grown by acquiring small local and regional supermarket chains.

Most Americans could not identify these food retailers as foreign-owned firms, for a variety of reasons. Foreign investment and ownership can take a variety of forms, and most foreign firms imitate marketing and merchandising practices of their domestic counterparts. Store banners (names) are often maintained after foreign acquisition. Products and services offered are little different from those carried by domestic retail counterparts. Foreign parent firms have thus far shown little interest in exporting retail products to their U.S. operations. Although foreign investors and retailers have introduced new concepts in the United States, their success has varied.

Table 18— Sales of leading U.S. food retailing affiliates of foreign firms, 1994

U.S. affiliate	Foreign investor (country)	National ranking	1994 sales
			$Billion
Albertson's	Theo Albrecht (Germany)	4	11.9
Atlantic and Pacific Tea Company[1]	Tengelmann, AG (Germany)	7	10.3
Food Lion	Delhaize, Le Lion (Belgium)	8	7.9
Ahold, USA [2]	Ahold (The Netherlands)	9	7.4
Shaw's Supermarkets	Sainsbury PLC (U. K.)	29	2.0

[1] A&P, Waldbaums, Food Emporium, Super Fresh, Farmer Jack, Kohls.

[2] Edwards, Mayfair, Finast, Giant Food Stores (Carlisle, PA), Martins, Tops, BI-LO.

In the 1980's, French retailers built very large stores in excess of 100,000 sq. ft. 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 breakeven 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 Kings Supermarkets was acquired by a British firm (Marks and Spencer), they introduced high-quality, upscale private label food products (with emphasis on store-prepared product lines) more typical of their upscale European foodstores. Although the concept has been successful, few, if any, domestic retailers have directly applied the format elsewhere.

Outbound Investment

Foreign sales by U.S. food-retailing affiliates reached $11.9 billion in 1993 (table 13). U.S. affiliates abroad generated an income loss of $433.0 million in that year and employed 108,800 persons. Safeway Inc., owns and operates 235 supermarkets in Canada, accounting for sales of US $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 convenience store operator, has joint venture and franchising agreements in 19 countries, including Canada and the Pacific Rim countries. Although technically not considered a foreign investor, IGA, Inc. (Independent Grocers Alliance), a cooperative supermarket operator, has licensed IGA foodstores in a number of countries in recent years. IGA provides training, product procurement, branding, and merchandising support for overseas retailers. There were 385 foreign supermarkets located in 19 countries participating in the IGA program in 1994.

As the aggregate figures indicate, inbound and outbound foreign investment by food retailers is disproportionate. The greater involvement by overseas investors in U.S. food retailing is due to a number of factors: (a) the U.S. market is quite large relative to many foreign markets, (b) the U.S. food distribution infrastructure is probably the most highly developed relative to any other country, (c) there are fewer restrictions to overseas investors than in many other countries, (d) regulations related to the building of new stores and support facilities are less stringent in the United States than in many European countries, (e) overall growth prospects are more favorable than in other industrialized economies, and (f) the political and business environment is stable, contributing to lower investment risk. 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.

Recent overseas investment by U.S. retailers has tended toward developing economies, especially those in the Pacific Rim region. U.S. investment abroad is much smaller than that of many foreign investors in U.S. food retailing. Although reasons for this pattern are not yet fully understood, it is likely that investment risk in developing countries is viewed as a barrier by U.S. retailers despite opportunities for growth. The persistence of these conditions facing U.S. food retailers overseas will likely result in inbound investment continuing to exceed U.S. investment abroad.

Foreign Direct Investment in the Food Service Industry

U.S. food service companies are moving into international markets as they look to foreign countries for expansion. U.S. chains have already penetrated foreign markets. Japan, Canada, Australia, and Mexico are popular locations for many fast food chains. More companies are scheduled to open additional units there and in other countries around the world in the next several years.

Foreign firms are also gaining ground in U.S. markets by purchasing U.S. firms and establishing affiliates here. Burger King and Hardee's, once U.S. owned, are now foreign-owned chains.

Table 19—Top U.S. food service firms in foreign markets by number and sales

Chain[1]	Total systemwide units, 1994	Foreign units, 1994		Total systemwide sales, 1994	Foreign sales, 1994	
	- - - *Number* - - -		*Percent*	- - - *$Million* - - -		*Percent*
McDonald's	15,205	5,461	36	25,986	11,046	43
KFC	9,407	4,258	45	7,100	3,600	51
Pizza Hut	11,546	2,928	25	6,900	1,900	28
Subway	9,893	944	10	2,500	265*	11
Domino's Pizza	5,079	840	17	2,500	415	17
Dairy Queen	5,542	628	11	5,542	300*	09
Wendy's	4,411	413	9	4,277	390*	09
Church's	1,171	233	20	590	125	21
Arby's	2,789	168	6	1,770	74	04
Taco Bell	5,615	162	3	4,290	130	03
Little Caesar	4,855	155	3	2,000	70*	04
TCBY Yogurt	2,801	141	5	388	22*	06
Sizzler	600	119	20	858	230	27
A&W	671	104	15	236	68	29
Big Boy	940	90	10	1,130	100*	09
Denny's	1,548	58	4	1,779	63	04
Popeye's	772	48	6	584	35	06
Sbarro	729	41	6	384	22	06
Ponderosa	680	40	6	690	40*	06
International House of Pancakes	657	37	6	632	32*	05
TGI Fridays	314	37	12	897	114	13
Bonanza	264	30	11	267	32	12
Round Table Pizza	576	29	5	351	15*	04
Carl's Jr.	649	20	3	587	30*	05
Long John Silver's	1,456	16	1	938	6	01
Jack In The Box	1,224	16	1	1,050	23*	02
Whataburger	517	9	2	383	5*	01
Perkins	432	8	2	626	12	02
Showbiz Chuck E. Cheese	332	8	2	370	7	02
Total	90,675	17,038	19	72,333	19,171	27

[1]Includes U.S. company-owned and franchisee-owned establishments.

*Technomic Estimate.

Source:Restaurant Business, June 1994.

U.S. Investment Abroad

In 1993, the latest year for which industry-wide data are available, there were 10 U.S. food service firms with 78 foreign affiliates (BEA 1995A). These affiliates had sales of $9.0 billion, 7 percent above 1992 sales (table 13).

The figures given above came from industry-wide BEA data. However, trade data were used to compile information at the firm and chain level. As U.S. markets become saturated and U.S. companies look for alternative markets, more fast food outlets are showing up in other countries. Twenty-nine of the top 50 restaurant chains operated a total of 17,038 units in other countries in 1994 (table 19). Seven of those chains accounted for 15,472 or 91 percent of those units operating outside the United States (table 20). At the beginning of the 1970's, only 900 total units operated outside the United States.

Asian/Pacific countries accounted for the largest share of these units, 37 percent. Twenty-nine percent operated in European, African, or Middle Eastern countries. Canada accounted for 24 percent of the units and Latin American countries, 10 percent. Hamburger, chicken, and pizza chains dominate the international market.

Table 20—Major U.S. food service chains operating outside of the United States, 1994

Chain	Asia/Pacific	Europe, Africa, Middle East	Latin America	Canada	Total
		Number of establishments			
McDonald's	2111	2197	436	717	5461
KFC	2172	817	396	873	4258
Pizza Hut	910	1148	415	455	2928
Subway	115	31	62	736	944
Domino's	232	160	203	185	780
Dairy Queen	125	36	16	451	628
Wendy's	143	41	51	178	413
Total	5808	4430	1579	3595	15412

Source: Company annual reports.

McDonald’s, KFC, Pizza Hut, Subway, Domino’s, Dairy Queen, and Wendy’s are the top 7 U.S. restaurant chains accounting for the largest number of foreign units (table 20). McDonald’s, the largest single food service organization in the world, had 15,205 units worldwide in 1994 and sales amounting to nearly $26 billion. McDonald’s operates in 79 countries and accounts for the largest number of units operating outside the United States, 5,461. Thirty-six percent of McDonald’s total units operated outside the United States compared with 34 percent in 1993. Most McDonald’s units are franchised. McDonald’s also leads in foreign sales, accounting for $11 billion in 1994. Major markets for McDonald’s units include Japan, Canada, Germany, England, Australia, and France. Foreign sales account for about 43 percent of McDonald’s systemwide sales.

In 1994, McDonald’s opened its first restaurants in Bulgaria, Bahrain, Kuwait, Latvia, Oman, United Arab Emirates, New Caledonia, Romania, Egypt, Trinidad, and Saudi Arabia. McDonald’s expects to open 900 to 1,200 restaurants around the world in the next several years with two-thirds of those being outside the United States. England, France, and Germany will be popular locations.

The McDonald’s chain not only operates traditional restaurant units but satellite stores as well—smaller units such as kiosks or mobile carts— which serve simpler menus. McDonald’s expected to open about 1,000 satellites around the world in 1995. They believe the key to aggressive satellite programs is alliances with retailers and oil companies that operate convenience stores. In 1994, McDonald’s satellite units operated in 377 Wal Marts throughout the United States, Canada, Mexico, and Puerto Rico. The United States, Finland, Denmark, and Italy now have McDonald’s in service stations.

KFC, a division of PepsiCo, Inc., has the second largest number of units outside the United States, 4,258, which operate in 73 countries. Sales outside of the United States, $3.6 billion, accounted for 51 percent of their systemwide sales in 1994.

Forty-five percent of all KFC units are located overseas. One fourth of KFC's foreign units are in Japan, 11 percent in Australia, and 8 percent in the UK. Of the six largest restaurant chains, only KFC and Pizza Hut operate units in Africa.

Pizza Hut, also a division of PepsiCo, Inc., has 11,546 units operating in 82 countries. Twenty-five percent or 2,928 restaurant units are located outside the United States. Pizza Hut chains are located primarily in Australia, France, Spain, the United Kingdom, and Trinidad.

Subway, a subsidiary of Doctor's Associates, Inc., operated 9,893 units in 21 countries in 1994. About 944 of those restaurants were located outside the United States. In 1994, Subway opened new units in 11 countries including Mexico, China, Japan, Indonesia, Philippines, Iceland, Slovenia, Cyprus, Kuwait, Saudi Arabia, and Korea.

Domino's, the second largest pizza restaurant chain, operates 840 franchised units in 37 countries. Japan and Canada are popular locations. Domino's future growth will depend more on international expansion. They already have about 90 stores in the UK and expect to grow in South America.

Dairy Queen, a subsidiary of International Dairy Queen, Inc., had 628 of its 5,554 units operating outside the United States in 1994. Dairy Queen has opened new stores in Mexico, China, Slovenia, Cyprus, Kuwait, Saudi Arabia, and Korea since 1993. Dairy Queen operates in 16 countries.

In 1994, Wendy's operated 4,411 units in 32 countries and territories. Four-hundred thirteen of their units operate outside the United States. Canada is the largest market for Wendy's restaurants. Nearly half of the units outside the United States are located there. Other popular markets for Wendy's restaurants are Japan, with 42 units, Philippines with 30, and Korea, with 29. Wendy's plans called for 100 new international units in 1995 to be concentrated in Latin America, the Pacific, Western Europe, and Canada. Wendy's anticipates a total addition of 550 new units abroad over the next 3 years.

Though fast food outlets paved the way into the international market, family chains such as Denny's, Big Boy, and International House of Pancakes are following (table 19). Casual dinner house restaurants such as TGI Fridays and grill buffets like Sizzler, Golden Corral, and Ponderosa are also moving into the international arena.

Table 21—Major foreign firms with U.S. food service operations, 1994[1]

Foreign investor/ location	U.S. chain	Type	U.S. sales[2]	U.S. units[2]
			Bil. dol.	*Number*
Grand Metropolitan, PLC London, England	Burger King	Sandwich	7.250	6,090
Imasco Ltd.	Hardee's	Sandwich	3.511	3,404
Montreal, Canada	Roy Rogers	Sandwich	0.460	530
Allied-Domecq, PLC	Dunkin' Donuts	Snack	1.332	2,979
London, England	Baskin-Robbins	Snack	0.560	2,355
Compass Group , PLC London, England	Canteen Corporation	Contract	1.077	1,600
Onex Corporation Toronto, Canada	LSG Lufthansa Services/Sky Chefs	Catering	0.460	34
Sodexho	Sodexho USA	Catering	0.435	490
Paris, France	Gardner Merchant Food Services	Catering	0.355	1,100
The Albert Abela Group Paris, France	The Wood Company	Contract	0.305	296
Total			15.745	18,878

[1] Includes company-owned and franchisee-owned operations.

[2] Projected.

Source: Nation's Restaurant News, Aug. 1994.

Foreign Investment in the U.S. Food Service Industry

Foreign-owned food service firms had 77 U.S. affiliates in 1993 according to industrywide data (BEA, 1995B). These U.S. affiliates accounted for sales of $5.2 billion (table 14), and had 116,800 employees. Trade data were used to report information at the firm and chain level. Trade sources report that food service sales in the United States by major foreign investors amounted to $15.7 billion in 1994 (including franchise sales), up 11 percent from 1993 sales of $14.1 billion (table 21). The number of U.S. units operated by these investors increased from 15,656 in 1993 to 18,873 in 1994.

Major foreign investors in the United States are Grand Metropolitan, PLC, London, England; Imasco, Ltd., Montreal, Canada; and Allied-Domecq, PLC, London, England. Grand Metropolitan, PLC, owner of the Burger King chain, is the largest foreign investor in U.S. food service operations. Grand Metropolitan acquired Burger King in 1988 with the purchase of Pillsbury. Among the top 50 franchised chains operating in the United States, Burger King was number two in 1994 with total worldwide sales of $7.5 billion. Foreign sales accounted for only 19 percent of that total. Burger King operated over 7,500 units worldwide with over 6,000 units operating in the United States in 1994.

Imasco, Ltd., Canadian-based owner of the Hardee's and Roy Rogers chains, is the number two foreign investor. In 1989 the Marriott Corporation sold most of its Roy Rogers restaurants to Imasco. Imasco operates about 4,000 Hardee's/Roy Rogers outlets in the United States with 1994 sales amounting to nearly $4 billion.

Dunkin Donuts was acquired in 1990 by London-based Allied-Domecq, PLC, the third largest foreign investor in U.S. food service operations. Allied Domecq also owns Baskin-Robbins ice cream stores. The firm operates 2,979 Dunkin Donuts outlets and 2,355 Baskin-Robbins outlets in the United States with combined sales of $1.8 billion.

London-based Compass Group, PLC, made its initial debut into the United States in April 1994 by buying the majority of Flagstar Cos.

Inc.'s Canteen Corp. U.S. sales for Canteen total $1.1 billion. Canteen operates 1,600 accounts in the United States.

Onex Corporation, the Canadian-based owner of Sky Chefs, recently signed a deal with Lufthansa AG of Frankfurt, Germany, that changed its signage to "LSG Lufthansa Service/Sky Chefs. This agreement created a global catering company with combined annual revenues of $1.3 billion.

Sodexho is a French contract catering company that has units in 60 countries and revenues in excess of $1.9 billion. In 1995, Sodexho acquired Gardner Merchant Services Group, creating the world's leader in contract catering with 11,745 units worldwide. The merger represents combined annual revenues of $3.65 billion. In the United States, Waltham, MA-based Sodexho U.S.A. operates 490 units and reported $440 million in sales. Combined, Sodexho and Gardner Merchant operated about 1,588 accounts in the United States with total revenues of approximately $800 million in 1995.

Sodexho's Gardner Merchant Services Group, which has been operating in the United States for 15 years, recently bought two of the catering segment's biggest accounts. In 1994 the Trumbull, Conn.-based division of London's Gardner Merchant Services Group, purchased from Morrison Restaurant Inc. the business and education accounts of its Morrison Hospitality Group. This acquisition increased Gardner Merchant's U.S. portfolio to more than 1,000 accounts and will nearly double its projected annual revenues in the future.

Other major foreign investors in U.S. food service include Kyotauru Co., Ltd., Tokyo, Japan (Acapulco, Charlie Brown's, Paragon Steakhouse); Nestlé (Stouffer Hotels, Top Restaurants, Rusty Scupper); and Unigate PLC, London, England (Black-eyed Pea, Dixie House, Taco Bueno, Casa Bonita, Crystal's Pizza).