Modern Market Growth and The Changing Map of The Retail Food Sector in Indonesia*

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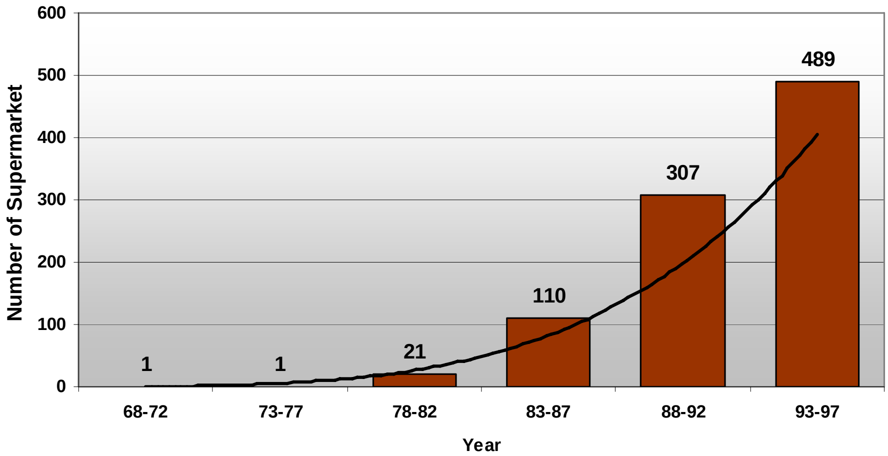
Development of Modern Market

According to BPS, the first supermarket in Indonesia was recorded in the early 70s and there was no further development for ten years. It was not surprising since it was a difficult year for Indonesia. At that period, Indonesia was recognized as the highest rice importing country and inflation was unbelievably high. Figure 1 describes that in the period of 1968-77 there was only one supermarket registered in Jakarta. Then, supermarket outlets began to spread rapidly after 1983 along with economic growth and increases in income per capita marked as the beginning of the green revolution era. During this period, the government of Indonesia expanded rice production to achieve self sufficiency. As the result, agriculture productivity, especially rice, grew very rapidly and its welfare effect on the economy was very significant. As the main staple, rice was available at low prices to urban dweller, and at the same time, farmers enjoyed increases in income from rising productivity and production.

Figure 1. Early Development of Supermarket in Indonesia 1968-97



Source: BPS, 2002

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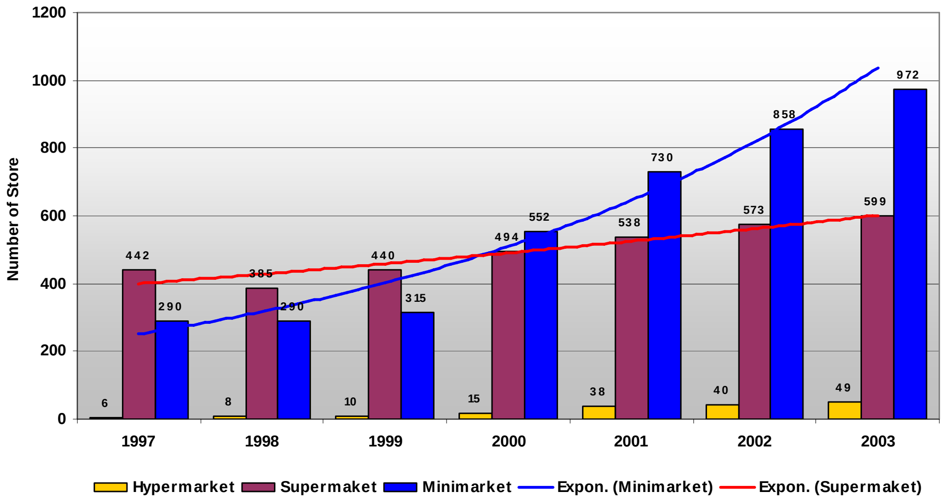
In the period 1978-1992, the supermarket sector grew 85% per year. While the growth rate declined, expansion continued at 12% per year between 1993 and 1997. However, supermarket development in the period of 1978- 1992 was mostly in Metro Jakarta and few large cities on the island of Java. Very centralized government of the New Order era has resulted in very concentrated economic development only in certain parts of the country, especially near the central government. The economic and political crisis that hit hard Indonesia in 1998 has changed the course toward decentralization which lead to some interesting changes in the development of modern markets.

Hypermarket entered Metro Jakarta in the mid 90s. Two French giant retailers, Carrefour and Continent, introduced the hypermarket concept to Indonesia in 1997. The companies then merged into one with the name of Carrefour which operated 12 stores in Jakarta, Surabaya, and Medan. The US based retail giant, Wal-mart, also entered the Indonesian market in 1998. However, the first store of Wal-mart was burned down during the unfortunate riot in Jakarta in the same year. Wal-mart then decided to leave Indonesia afterward. Recently, there are two new actors in hypermarket business, Giant and Hypermart. Giant is managed by Hero Group and Giant, a retail company from Malaysia. Hypermart is managed by Matahari Group. As we can see from Figure 2, the number of hypermarkets is still quite small but consistently increasing by 27% per year in the last 5 years.

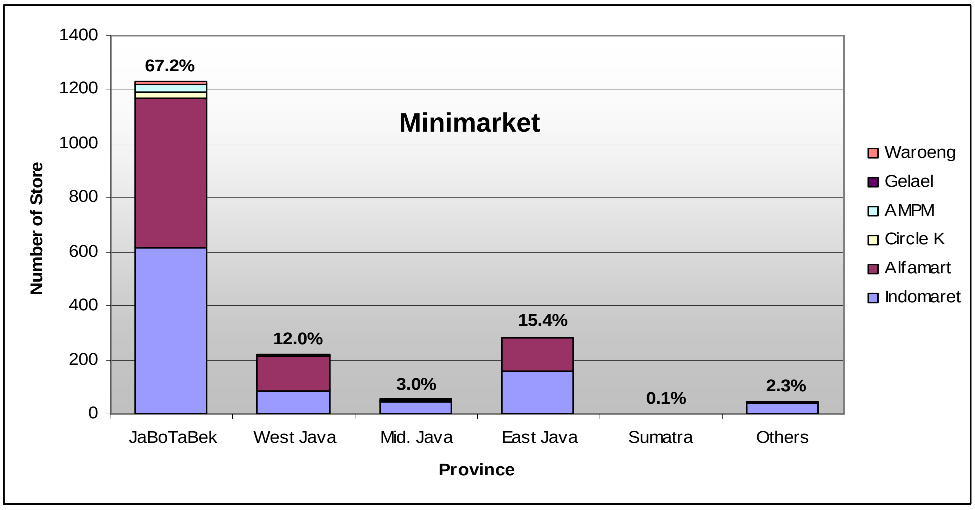
Figure 2. Development of Modern Market (1997-2003)

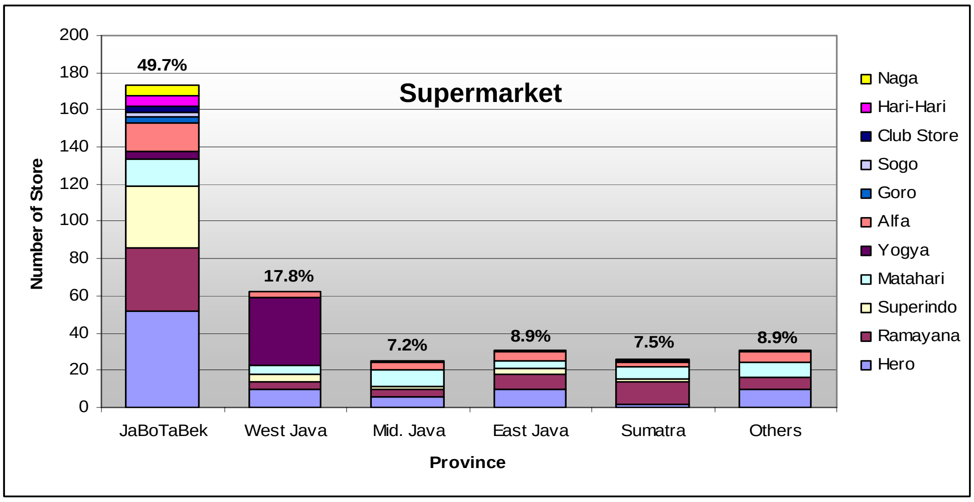


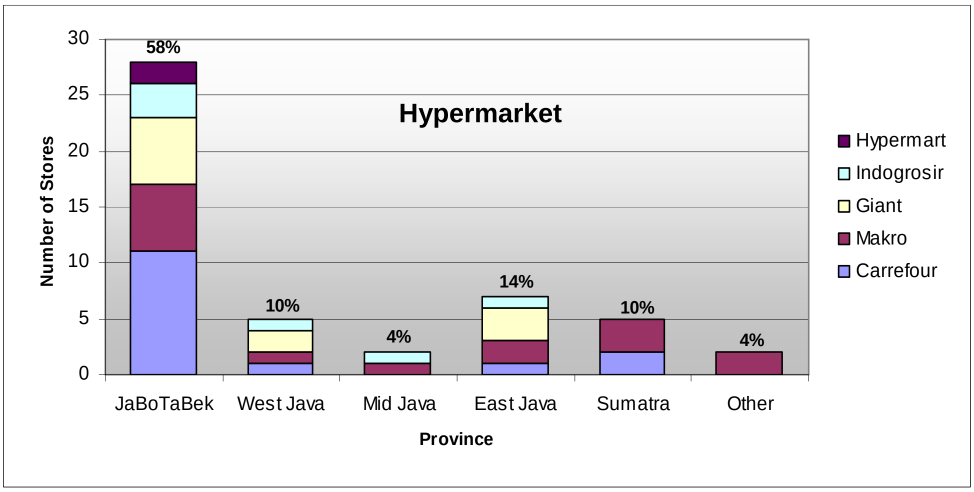
Source: DRI, 2004; Visidata Riset Indonesia, 2003

Figure 2 shows that when the crisis hit the Indonesian economy, development of modern marketd was affected seriously for a few years. In 1998, the number of supermarket stores drop by 13%. However, it's back on track and growing by 9% per year in the last 5 year. On the other hand, Minimarket, even during the economic crisis, has been steadily growing and spreading to every neighborhood and corner of the city, especially in Jakarta and other large cities very quickly. During 1997-1998, still strongly affected by the crisis, minimarket was not growing. Only one year later in 1999, minimartket already grew by 9% per year. In 2000, it's soaring to increase by 75% but slows down to an increase of 27% per year in the last 5 years. A sharp difference in the growth of supermarket and minimarket is described by an exponential curve. Even though the modern market has been growing quite rapidly in Indonesia, they are still concentrated in several areas, mainly Metro Jakarta and the Island of Java. See Figure 3 for the spread of minimarket, supermarket, and hypermarket in Indonesia in 2004.

Figure 3. Minimarket, Supermarket, Hypermarket and Their Store Locations







Source: Retail Indonesia, 2005; Visidata Riset Indonesia, 2003

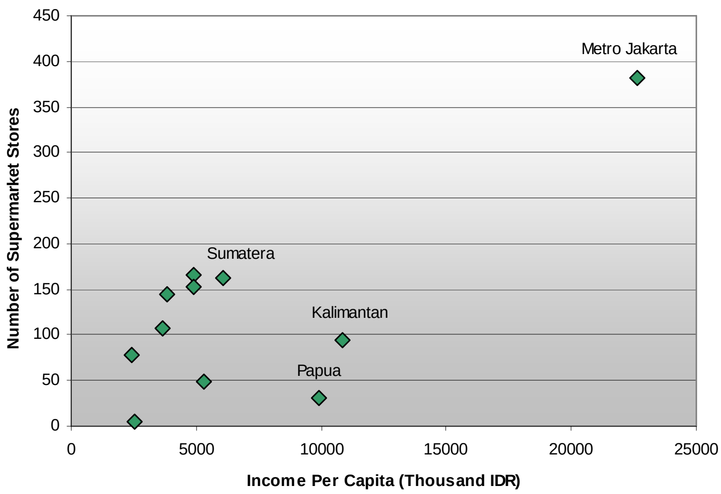
Figure 3 indicates unequal distribution of modern market in Indonesia. About 50% of the supermarket is located in Jabotabek, 18% in West Java province, and the remaining is spread in the rest of other provinces. On the other hand, minimarket and hypermarket has grown mainly in Metro Jakarta area and East Java provinces. Figure 3 shows that 58% of hypermarkets in Indonesia are located in Jabotabek, 14% in East Java province, and the rest spread to other provinces. Similarly, minimarket is also mostly (67%) concentrated nearby Jakarta-Bogor-Tanggerang-Bekasi (Jabotabek) area.

Looking to its development pattern, minimarket could become the most expansive retail business in Indonesia. Minimarket's development is mostly targeting the area closer to the residential and housing complexes. Minimarkets are preferred by many consumers because of its comfort and easiness in shopping. Minimarkets mostly dominated by the big retailers with big financial capacity which have superiority in pressing down the margin. Hence, minimarket selling price could be very cheap compared to the traditional retail shops in the vicinity. The dominant players in minimarket are Indomaret and Alfa Minimart. Indomaret has been the pioneer in the development of the minimarket concept in Indonesia. In 2001, Indomaret had around 566 outlets spread around Jabotabek, Bandung, Surabaya, and Yogyakarta. The growth of Indomaret's outlet seems to be closely related to the franchise concept that was started to be used in 1997. Alfa Minimart is the second largest player with around 150 outlets spread around Jabotabek, Bandung, and Surabaya.

PATTERN OF DEVELOPMENT

While other businesses grew slowly after the economic crisis, supermarket growth was very impressive, steady and consistent. In the period of 1999-2003 private consumption expenditures contributed about 70% of the GDP. It is not surprising that a sector serving the needs of consumers has been growing impressively in the last 5 years. However, it is still a puzzle which parts of the consumption need to be considered? The literature leads us to first consider the level of income. We should check the hypotheses: the higher the income of consumers in the area, the more supermarkets stores can be found. Figure 4 demonstrates the scatter diagram of income and number of stores. The plots show no strong correlation among them.

Figure 4. Scatter Plot of Income Per Capita and Number of Stores



Source: DRI, 2004; BPS, 2003

Figure 5. Scatter Plot of Number of Household and Number of Stores

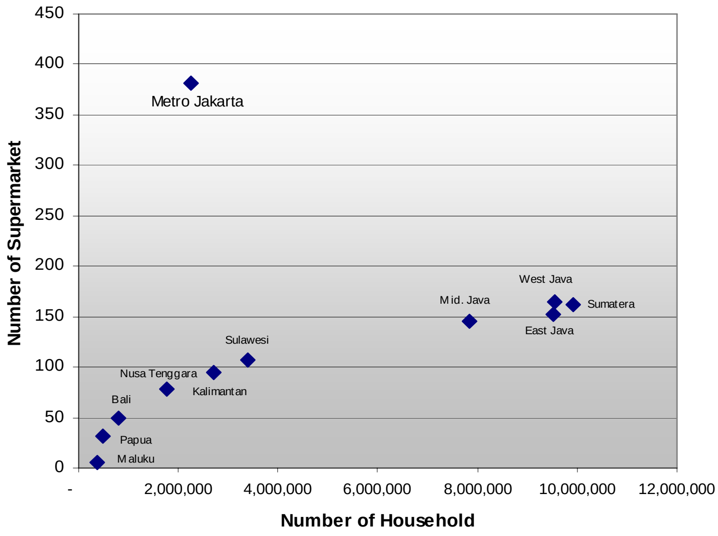
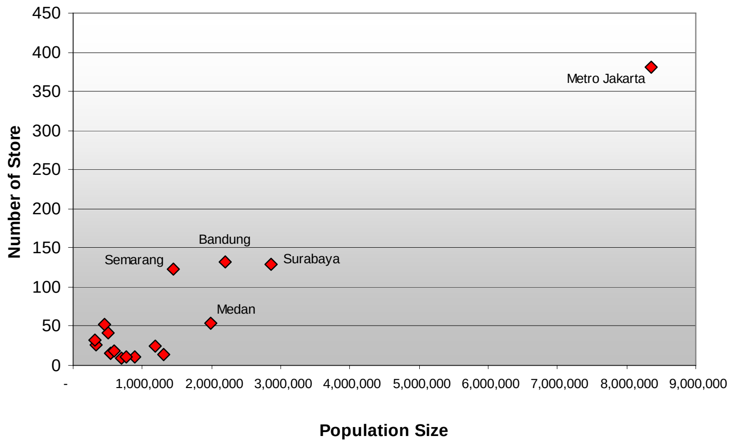


Figure 5 gives a better correlation pattern. There is indication that the number of existing stores in different provinces is driven by the number of consumers which in turn reflects higher consumer needs. The greater the number of households, the more supermarket stores needed to support its consumption. The only exception is for Metro Jakarta which will be discussed later. Figure 6 also indicates a good pattern of correlation between the population size and the number of existing stores.

Figure 6. Scatter Plot of Population Size and Number of Stores of Major Cities



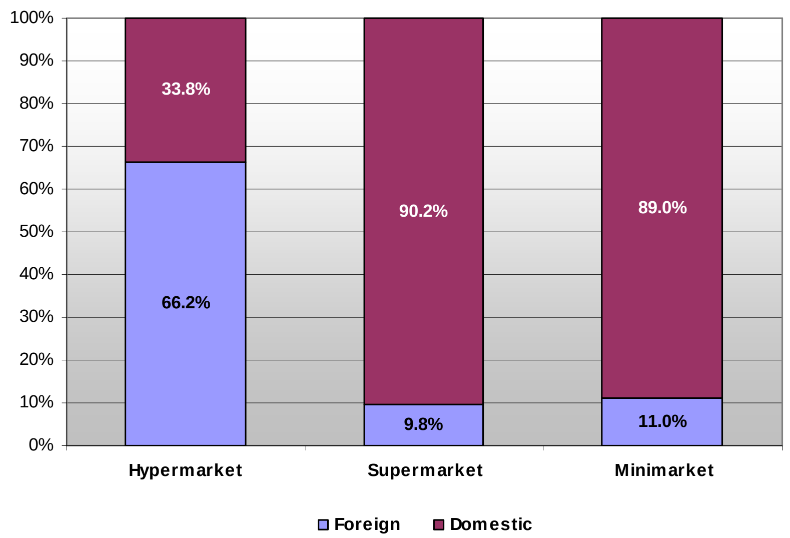
In the two figures, the location is showing the number of households and populations at the kabupaten (district) level. It is not actually comparable to Metro Jakarta in terms of the area size and population density. Metro Jakarta, with a population of 8 million people, is truly different from other locations compared in the graph. With high income and high population density, Metro Jakarta is capable of demanding more supermarket stores for another 5 years. This condition will not happen to other kabupaten since the population is spread in such a wide area that it will not be feasible for a supermarket to operate. Only in the capital city or special populated spot of kabupaten possibly can accommodate a supermarket. However, kabupaten level conditions are more suitable for mini markets that can be upgraded into small supermarkets.

ROLE OF FOREIGN INVESTMENT

The Indonesian government had closed the retail sector to direct foreign investment since 1969 in the effort to protect local retailers. However, there is a loophole in the regulation to enter the Indonesian market through franchise and technical arrangement with local companies. The aggressive entry of foreign retailers took place after the economic crisis that hit Indonesia in 1998. The Indonesian government in January 15, 1998 signed a letter of intent with the IMF stating that the Indonesian government should revoke the ban on foreign investors to enter the wholesale and retail businesses. Later, the open for foreign investor was legalized by a Presidential Decree No.99/1998 and a Decision Letter of the State Minister of Investment (Head of Capital Investment Coordinating Board) No. 29/SK/1998. The regulations stipulated that licensing procedures and all other requisitions that a foreign retailer has to fulfill are the same with those applicable to local large-scale retailers.

After the liberalization of the retail industry, some foreign retailers began to invest in Indonesia. Some foreign retailers invested in supermarkets and minimarkets. However, most foreign investment goes to hypermarket business. While there is no reliable data on the value of foreign investment in the Indonesian retail sector, Figure 7 shows estimates of the composition of capital investment in each business from the business sales turnover.

Figure 7. Percentage of Foreign Investment on the Modern Market



Source: International Business Strategies, 2003.

Foreign investment is very dominant in the hypermarket business, with 66.2% of the capital coming from foreign investors. In contrast, supermarkets and minimarket businesses are mostly dominated by local investors. Local investors have about 90% of the capital share for supermarkets and minimarkets. However, foreign investment in minimarket businesses is a little bit higher since some of them are franchised by foreign retailers such as Circle K. Supermarkets mostly are supported by local investment.

IMPACTS ON TRADITIONAL AND SMALL RETAIL OUTLETS

Most of the medium and small income consumers in Indonesia still depend upon traditional markets, including small shops and kiosks located around residential areas. According to Visidata Riset Indonesia (2003), number of consumer visits to traditional markets and outlets is still as high as 23.3 days in a month. Number of consumer visits to minimarkets that are close by on the neighborhood is still only 4.1 days a month. Number of consumer shops to supermarket and hypermarket is 3.2 and 1.8 days a month, respectively.

Factors affecting potential demand for modern retail is changing pattern of consumer's shopping habit from traditional market to modern market. Five years ago (1999) share of modern market in delivering food to consumer was only 11% from the total food purchase of consumers in greater Metro Jakarta (Jabotabek). In 2001, the share was already increase to 14% (Visidata Riset Indonesia, 2003). Further, ACNielsen (2004), recorded that the share of modern retail in delivering food to consumer in 2000 was already about 21.6% (Figure 8). The share has been increasing consistently every year to become 29.6% in 2004, or an increase of 8% within only 4 years (2000-2004) based on 47 items surveyed in Jakarta. In other words, modern retail market is taking over traditional market by 2% per year. If this growth continues, it will no be too surprising if by 2020 the share of modern market will be 60%, the level of modern market share in the first wave countries of Reardon, Berdegue, and Timmer (2005), such as Argentina, Brazil, and Taiwan.

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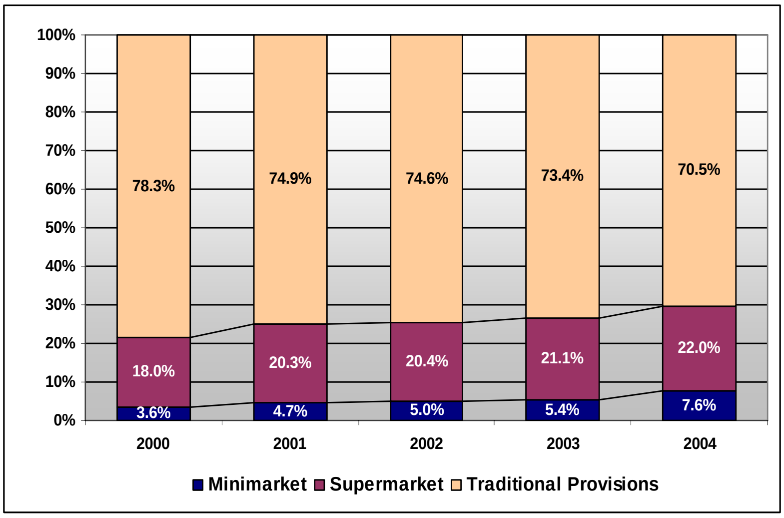
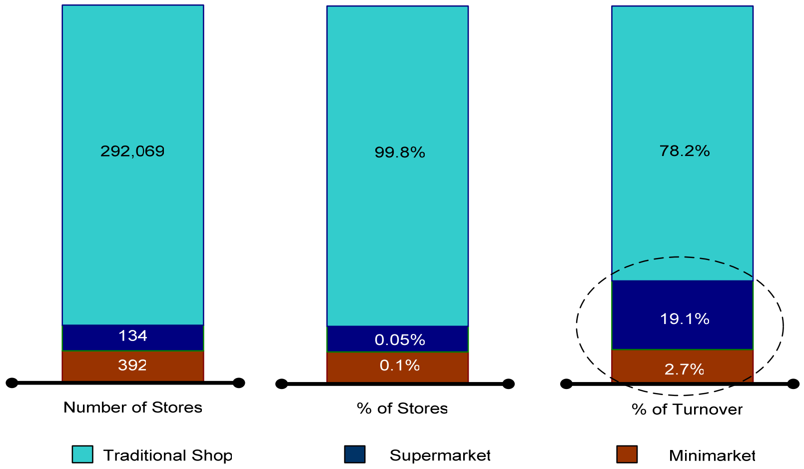
Figure 8. Market Share of Modern and Traditional Market



Source: ACNielsen, 2004a

The changing pattern of food retail is not only noted in term of percentage outlets, but also even more significant in term of food value sold. ACNielsen (2004) indicated that in term of percentage, modern retail outlet is only about 1% of the existing number of market traditional outlets (Figure 9). However, its contribution in term of sales turnover is about 25% of the total market. ACNielsen further indicated that more than one third of foods purchased from the modern market are considered as fast moving consumer goods (FMCG). From the supermarket total sales on 47 item category audited, fifty percent of the item purchased by the consumer is from the food category. In term of sales growth, household item category has the highest sales increase.

Figure 9. Market Share and Sales Turnover of Modern Market

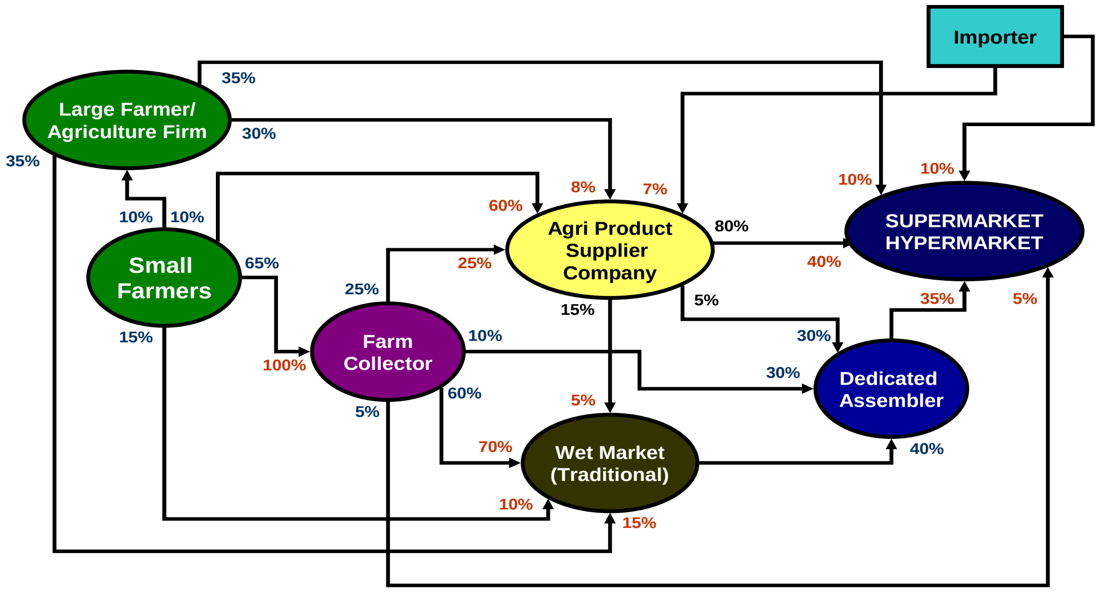


Source: ACNielsen, 2004

IMPACTS ON DOMESTIC AGRICULTURE

Most small farmers in Indonesia with the average of 0.3 ha per farmer land ownership do not have direct access to the market. Usually they market their agriculture product through local farm collectors. In the case of horticulture product, small farmer sell 65% of their produce to local farm collector. Only about 10% of farmers connected and have arrangement with the agri-product supplier to supermarket. Agri-product supplier, which mostly supply to supermarket (80%), needs to maintain relationship with several farmers who can plan horticulture products according to their supply need and with customized product specification. This group of farmer (60%) is very

Figure 10. Supply Chain of Horticulture Products to Supermarket



Adapted from: DAI-CDS IPB, 2003

important for the company in order to be in the supermarket supply chain business in maintaining the product consistency, quality, and quantity sustain ably. The agri-product company supplies mostly (80%) to the supermarket/hypermarket. Because of inconsistency product quality bought from the collector, generally the company has to re-sale 15% of the product to the wet market.

Large farmer, on the other hand, has an ability to supply the supermarket directly (35%) because of their size of production and more standardized product. The other30% of the large farmer supplies supermarket through an agri-product supplier. The company supplies 40% of horticulture product needed by the supermarket. The other large share of supplier to supermarket is from the dedicated assembler (35%) that customizes the package horticulture product to the supermarket. Figure 10 show that only 10% of products sold by the supermarket are imported products directly by the importer. Agri-product supplier company is also sale imported product to supermarket.

A side from its fast growth which is good news to consumers, the supermarket revolution poses serious risk and threat to small farmers in developing country who traditionally supplied the local wet market. Since supermarkets require large quantities of products of consistent quality and quantity, it is good news only for a big, efficient, and well organized farmer. For small farmers dealing with procurement requirement of supermarket chain can be a painful shock. Several problems faced by small farmers in supplying to supermarket are: difficulties in responding to demand of agriculture product with specific quality, quantity, and time consistently; Low technology investment; No extension service help on the technology and invasion; Farmers mostly work individually.

For an agro-product supplier, supply chain to supermarket is also poses problems, such as: payment of supermarket is not cash and carry, paid in 10-20 days; credit payment of supermarket cannot be used as collateral for a loan from banking system; difficult to find consistent quality and quantity of produce sustain ably, buy 1 ton, 0,4 ton to supermarket and 0,6 ton has to be resale to wet market; and difficulties to built long time working relationship with farmers, they always looking for short term gain.

Share of supermarket in Indonesia is predicted to grow continually. However, at the moment is only 10-15%, it seem to be not too important. The picture may change if supermarket grow and spread outside Java and kabupaten level. Looking to the development in other countries, the share can reach as much as 80% of the food market; small farmers will face very limited share if cannot join the growth of supermarket chain. The real threats to local farmers happen If the supermarkets cannot find the product locally; they will import from some where else cheaper and give better quality.

THE FUTURE OUTLOOK OF INDONESIA'S RETAIL FOOD SECTOR

With the continue growth of the Indonesian economy, modern retail will continue to expand with the growth between 15-25% annually. The growth of hypermarket will soon move to large city in Java, Sumatra, and Sulawesi. The expansion of supermarket and minimarket will even be wider covering other island (off Java) down to Kabupaten level. There is still plenty room to grow since the ratio of modern market space and the population is still far for congestion.

Supermarket, hypermarket, and minimarket in Metro Jakarta, Bogor, Tanggerang, Bekasi will continue to grow for the next 5-10 years. However, the growth of will soon slowing down since competition getting higher and there will be no more room for the new entry unless somebody exit from the market. The growth is expected to be less than 10% in the following year.

The expansion of supermarket will take offer some portion of traditional market share. The traditional market need to be reposition and improve in term of its sanitation and health standard. The existence of traditional market still needed by community in the outskirt of the city and kabupaten level consumers.

There will be a new regulation controlling the establishment of new modern market outlet. The local autonomy government as well central government is now talking about such a rule. It still not clears where the policy is heading. The regulation is driven by the cry and concern of local players in traditional market that they will be driven out of business with out some protection.

To release the tension with local producer and trader, product from local farmers and local SMEs have to be the priority of product to be marketed through the modern market. There have to be an effort and communication in such away that local farmers and SMEs understand the requirement of product accepted by modern market. There is a need to assist farmers and SMEs with the technology investment and innovation. University and other research center can be an ideal candidate to be position with higher responsibility for getting the farmers and SMEs ready for the technology needed to face the global supermarket era.

The government policy has to prevent "direct" competition of hypermarket and supermarket, with traditional market according to local socio economic characteristics and population density. The government also should improve the technology of farmers, SMEs, and traditional provisions, so that their product standard fit with the supermarket standard. Farmers and SME organization need to be strengthen Long term credit for investment and support of bridging financial support to help actors of supply chain to supermarket

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