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Needs and Missions of Tomorrow's Food Distribution System

by
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During the past two years I have talked to many groups about food distribution's direction and role over the next decade. Of all these groups, none has more potential for exerting a positive influence on this evolution than the audience assembled here.

The food policy agenda in America today is crowded with issues we thought about only in passing just a few years ago. The food distribution system is finding itself face to face with new interest groups and new coalitions all demanding their place in the decision-making process. If I have learned one lesson as a result of my work with the National Association of Food Chains in Washington, and the Super Market Institute in Chicago, it is this: This industry cannot by itself achieve the economic and social growth being demanded of it. We need the cooperation of labor, government officials and regulators, the academic community, consumers and consumer activist groups, wholesalers, grocery manufacturers, retailers and bankers. Even with this long list, I have probably left someone out.

I hope you have come here today not merely to listen, but to become actively involved. We need your talent and we need your support.

I

The food distribution system is undergoing many important transitions which lay the groundwork for our discussion. I will mention a few of the most important.

First, the transition from family management to professional management. Those of you who have an industrial organization background know every industry eventually arrives at this point. The founders who built the businesses from the ground up become less actively involved either because of age or because they move on to new challenges. Professional management moves in to take their place. This is often a difficult transition because the philosophy of the organization must change. It takes a different personality to operate in a mature industry than it does to build an industry. Cost control and organizational efficiency move higher on the priority scale, risk taking and growth move lower. Those of you involved with training young people at our many universities should find a ready market for their talents in food distribution over the next decade.

Second, the transition from a growth-oriented economy to a more stable, quality-of-life oriented economy. As all of you know, growth covers a multitude of sins. We need to be much more careful in identifying and correcting inefficiencies than we have been in the recent past.

Third, the transition in information and control systems brought about by the technological explosion of electronic data processing. This technology has

made possible the electronic front end, electronic funds transfer, computerized warehouses, computerized meat processing operations, and automatic ordering systems. Perhaps of even greater importance is the potential finally to obtain item sales and item gross margin data. These data are not now available, despite the belief of government regulators to the contrary. When they finally surface, they will revolutionize our ability to control inventories, to tailor product mix to the neighborhoods, and to coordinate product movement throughout the distribution channel. Computer technology is not a homogenizer. It is a tool, if properly used, for managing variety of product and service on a scale never before possible.

New technology creates the need and opportunity for decisions. It also creates the need and opportunity for interface between previously uncoordinated interest groups. This arena will keep food distribution researchers busy for years to come.

Fourth, the transition of this industry to the front line of economic and social policy debate. Not so very many years ago, agricultural policy as a major area of study was at a very low ebb within the agricultural economics profession. Today we are witnessing a major rebirth.

Why this new interest? The Government is interested in food distribution because the United States has evolved a major comparative advantage in world food supply, and because food plays a major role in social welfare programs. Labor is interested in food distribution because its control over rail carriers, truck lines, and port facilities provides a mechanism for commanding the kind of national attention useful as a bargaining tool for a wide variety of purposes in the political arena. Labor is also interested because food distribution, and in particular food retailing, remains one of the most labor-intensive industries in our economy. Organized consumer groups are interested in food distribution because they have found this to be a highly visible sector, which may be used to mobilize consumers on issues which extend beyond our industry's boundaries.

By any standards, food distribution is caught up in a set of issues enmeshing us with our total society as never before. Our first mission in meeting tomorrow's challenges is to realize food distribution is now very much a part of a larger social system, and to learn to be sensitive to the needs and goals of new participants laying new claims to our resources.

Let me discuss the four transitions just outlined in greater detail.

II

I mentioned earlier that government involvement in food distribution is increasing. Congress is shifting its attention from an almost exclusive focus on production to a more balanced examination of the entire production-distribution chain.

Unfortunately, we have not kept pace in the research community. Research into food wholesaling and retailing is woefully inadequate. Let us take the U.S. Department of Agriculture as an example. By any standards, the resources devoted to production agriculture far overshadow resources devoted to distribution and marketing. Now it is certainly true that you must produce it before you market it. But it is also true that we currently have more to gain as a society from an extra dollar allocated to food distribution research, than from an extra dollar allocated to food production research.

Most, if not all, of the people in this room have been deeply involved in distribution and marketing research for years. We must work from this base to attract many more resources. If the U.S.D.A. and our universities had been responsive enough, we would not now be witnessing a drive by Congress to involve the General Accounting Office in food distribution research. While I am hopeful they will perform well in this new role, it would have been more efficient to build on our existing strength rather than to start from scratch with another agency. Congress is sending us a message, and we had better listen.

While I am on the subject of the Congress, let me point out a few facts. In the past five years, 2500 bills have been introduced to look into the food industry (Schlossberg and Cassidy). Consider this level of activity in light of the available expertise. Over one-fourth of the House and over 35 percent of the Senate were freshmen in the 94th Congress. In the upcoming 95th, we see an even younger, more activist profile. We look forward to a House with fully one-half of its members in their freshman or sophomore term and to a Senate with 17 new freshmen.

An important fact for you to realize is that almost none of our elected representatives has personal experience in the business community. In the 94th Congress, only one of the one hundred Senators and 17 of the 433 Congressmen had previously owned a retail business of any kind. Only 3 Senators and 13 Congressmen had previous executive experience with large corporations. And, in the food industry specifically, only one Senator and 4 Congressmen had any previous business experience with the food industry beyond the production level.

The National Association of Food Chains recently sponsored a survey of the 94th Congress to determine their level of knowledge concerning our industry. This was a mail survey and therefore a self-selecting sample. Even with this limitation in mind, I think some of the answers will startle you. All data are drawn from Schlossberg and Cassidy.

The farmer's share of the consumers food dollar is just over 40 percent. N.A.F.C. asked Congressmen and Senators for their estimate of that share. Of the Democrats responding, 32 percent estimated the share to be much lower, as did 63 percent of the Republicans and 95 percent of those not indicating a party affiliation. The most common share indicated was 15 percent selected by 79 percent of the Democrats and 50 percent of the Republicans.

Retail labor wages and fringe benefits account for over 65 percent of supermarket operating costs. Of the Democrats responding, 94 percent estimated the share to be lower, as did 90 percent of the Republicans and 90 percent of those not indicating an affiliation. The most common share indicated was 35 percent selected by 60 percent of the Democrats and 39 percent of the Republicans.

Chain stores account for approximately one-half of all domestic grocery sales. Of the Democrats responding, 83 percent estimated the share to be higher, as did 100 percent of the Republicans and 99 percent of those not indicating an affiliation. The most common share indicated was 80 percent selected by 35 percent of the Democrats and 44 percent of the Republicans.

We have then a Congress which overestimates the impact of big business on the food distribution channel, which views almost all food retailers as chain store operators, and which fails to understand the impact of labor on this system.

Another mission in meeting tomorrow's challenges has emerged: We must be much

more effective in communicating the basic facts of our industry to the public and to our elected officials. This industry has a good story to tell. Let's tell it.

I mentioned in my list of important industry transitions the information explosion being brought on by electronic data processing. This explosion has been brought about by the rapidly improving technology of the computer. However, all of us in this room know, I am sure, that computers will not solve all of our problems. In fact they bring problems of their own, since in actual practice they are not always used as top management intended them to be. Another mission in meeting tomorrow's challenges is to learn to deal with computer aided decision-making in a rational fashion.

The transition to professional management should prove very helpful in this regard. It is important that you realize the degree of sophistication already available in the food distribution industry. The expertise of professionally trained people in data processing departments is particularly impressive.

Of course you have all seen electronic scanners by now, and I assume most of you have seen some form of automated warehouse. If not, you soon will. But there are other uses less well-known. For example, computerized systems to track and control direct store deliveries are rapidly becoming popular, and scanning systems capable of tracking truck movement are now being tested.

As these systems grow, and as new applications surface, we must take care to coordinate research such that we maintain system compatability at the critical industry interfaces.

We must also take care that the data generated become a part of the decision-making process in the boardroom. It is very easy to pass off the computer as a device for improving operating efficiency without exploiting its potential for aiding in strategic decision-making.

Good long-range decision-making requires the ability to forecast. Unfortunately, most of us have failed miserably at this task over the last few years and have adopted the philosophy. If you can't forecast well, at least forecast often.

Certainly one of the current confounding factors is the role of consumer expectations. In fact, a new subset of theory is being generated by the policy-expectations interplay. What all of this means is that we can no longer count on traditional lead times for consumer reactions. Our society now carries with it a great deal of latent consumer anxiety capable of surfacing very quickly. The mere expectation of a shortage creates a stampede of buying which guarantees the shortage. We fall victim to the self-fulfilling prophecy.

In time we will learn to deal with these problems and we will learn to improve our ability to forecast. EDP will play an important role in this process.

The remaining transition to explore in greater detail is the transition from a growth economy to a more static quality-of-life oriented economy. I would like to highlight one aspect of this not usually discussed.

As we move to a more stable economy, the public becomes more critical of industry inefficiencies. We must realize that in food distribution, the easy efficiency improvements have already been adopted. We are now faced with an industry which requires cooperation across traditional boundaries if efficiency is

to be further improved. I am most familiar with food retailers, and I can tell you that they are looking at major efficiency improving innovations which cannot be implemented by that sector alone. They require the cooperation of that long list of related groups and sectors mentioned at the beginning of my talk. It bears repeating: labor, government officials and regulators, the academic community, consumers and consumer activist groups, wholesalers, grocery manufacturers, and bankers.

Another mission in meeting tomorrow's challenges is to find ways to coordinate the activities of many divergent interest groups to improve the efficiency of food distribution. This is not an easy task, and I cannot overemphasize its difficulty or its importance. Let me give some examples to illustrate the coordination required, again from food retailing. You will note that most of these will involve improving labor productivity. With labor costs at approximately 67 percent of supermarket operating costs, retailers are focusing most of their efforts in this area.

The most-publicized recent attempt at improving productivity is the electronic scanner. Since grocery checkers earn up to $16,000 per year, it makes sense to use technology to make them as productive as possible. The scanning concept can increase speed and accuracy, and holds the potential for eliminating much of the labor required for individual item price marking. However, you all know by now that organized labor, fearful for job security, and organized consumers, who prefer item price marking to shelf price marking, are both actively opposed to any departure from conventional pricing practices.

The point of repeating this familiar story is to say the industry learned a painful lesson from this experience.

It is sad to see that others have not yet learned this lesson. Consider Electronic Funds Transfer (EFT) as an example. Here is an innovation which holds the potential for streamlining our payment systems. It has potential application in all phases of retailing. However, most of the initial installations have been in supermarkets. Yet the Congressional E.F.T. advisory commission was formed without a single food retailer representative. This commission is already deeply involved in the technical questions of E.F.T. application including whether a remote installation should be considered a branch or not. Food retailers recently appeared before a subcommittee of that group to suggest they were moving much too fast. The fundamental homework on consumer attitudes and needs has not been done.

Once again we see an innovation which involves divergent interest groups. Yet bankers and their regulators have not learned the lessons which would let them work effectively in this environment. They have not yet learned that consumers will be a part of the decision-making process, and that base must be touched early if confrontation is to be avoided.

Another innovation with tremendous potential for productivity improvement is modularization of secondary packages (shipping containers). Automated or mechanized warehouses cannot reach their full potential unless such a modular system is developed. Since a unionized order selector in a grocery warehouse (a job which requires one day's training) earns up to $20,000 yearly, mechanization is a high payoff item. The problem currently limiting the application of this technology is the difficulty of stacking cases from different manufacturers onto pallets for shipment to individual stores. Since these cases are not size-related by standard multiples (modular), load stability is a major problem. This is critical because current government warehouse

sanitation standards leave no margin for breakage due to unstable loads.

As an illustration of the container variety which now exists, a recent dry grocery warehouse study conducted by A.C. Nielson found 2,587 different secondary container sizes in a typical warehouse stocking approximately 5,000 items.

The conflict which arises over modularization is between retailers who would share in the benefits along with consumers, and grocery manufacturers who would bear most of the cost. Many similar conflicts will arise in the future as we attempt to further streamline food distribution. We simply must learn to cope with this problem.

Under this mission of coordinating divergent interest groups in efforts to improve efficiency, I have been focusing on new technologies. There is another concern which fits under this heading and is very much in tune with the issues of our recent Presidential campaign. We need to develop a mechanism for resolving disputes between regulatory agencies.

What does a store manager do when the Occupational Safety and Health Administration (O.S.H.A.) inspector tells him he needs a rough floor in the meat room to prevent falling, and the Food and Drug Administration (F.D.A.) inspector tells him he needs a smooth floor to facilitate sanitation? What does he do when the O.S.H.A. inspector tells him to put railings around the loading dock to prevent employees from falling off, and the F.D.A. inspector tells him to remove those railings because they contaminate sides of beef coming into contact with them? What does he do when the F.D.A inspector tells him to use stainless steel equipment in the meat room to facilitate sanitation, and the O.S.H.A. inspector tells him to find another type of equipment because of noise levels? Although most of the problems associated with these three examples have been solved, new examples will continue to arise.

We need a method of arbitration; a method for resolving disputes between regulatory agencies where jurisdictions overlap. The current movement toward reorganization must be sensitive to this need.

There is one more aspect of learning to deal with new and divergent interest groups on issues of efficiency improvement which is important enough to highlight as a separate mission. We must learn to make progress in efficiency and technology without destroying basic market alternatives for the consumer. This is particularly critical as we introduce new technologies.

New technology triggers the fear of Future Shock among a great many people. Couple this fear with the recent proliferation of regulatory agencies, and the political activism of labor unions and consumer activists, and you have a strong bias in favor of legislation. Unfortunately, this legislation tends to come very early in the evolutionary stages of technological development. The result of early legislation? We will find our system unable to perform the market testing necessary to refine our systems, and we will find ourselves with homogenous applications. You have already seen this tendency operating in drives to legislate the development of U.P.C. scanning systems and E.F.T. payment systems, to mention only two examples.

These new technologies are extremely complex and truly beyond our abilities to map their evolution prior to actual market exposure. We need to deliver the message that the best way to encourage responsive development is to slowly introduce these new technologies side-by-side with existing systems and let the market

speak. Only those developments offering real value to shoppers will survive.

Certainly part of the rush to regulate is due to the fear that a new, untried technology will suddenly sweep away familiar systems. This simply does not happen in our industry. Food distribution is evolutionary, not revolutionary.

How do we get this message across? I think we do it by doing all we can to act as consumer representatives. As an industry we must consider consumer's rights, we must bring consumer concerns into our decision making, and we must be very careful to communicate our intentions to consumers giving them ample opportunity for feedback. Already we have made progress in this direction and must push even further.

III

If you have been counting, I have just given you five missions. These have been very broad charges intended to serve as guideposts for the decade ahead. In the process, I have left out many specific issues which are of great importance. Energy programs, capital acquisition, and the susceptability of food distribution to destructive price wars are three topics which certainly fall into this category. These and many others were not included only because I saw my charge as providing a more general framework, and because time is short.

As you think about this framework, and how the immediate problems of the day fit into it, please keep one thought uppermost in your mind. Food distribution is finding itself exposed to increasingly sophisticated technologies and increasingly complex societal interactions. The problems of the future require as never before, sound professional research if we are to reach the right answers. We need an extraordinary commitment from each of you to provide that research, and to help in providing the leadership we need to keep the food distribution system healthy, vigorous and responsive.

Reference

Schlossberg, Cassidy and Associates, Congress and the Chains, Report to the National Association of Food Chains Annual Meeting, Los Angeles, October 17, 1976.