Part IV · Reassessing Policies for Changing Structure or Behavior

In addition to policies to facilitate orderly marketing, policies of significant complexity have been developed to fundamentally change the market structure or behavior in the agricultural marketing channel. This group of policies includes cooperative policy, marketing orders and antitrust legislation. These policies and programs enabled by them have often been more controversial than market facilitation. Concern is expressed from time to time that the current industrial food system is less in need of these special priveleges.

The purpose of this section is to develop a general rationale for these policies and programs and to assess areas needing more development and areas needing de-emphasis or updating. It is also hoped this work will be useful to the planning committee that will prepare for a future conference – specifically focused on updating this area of policy.

Rationale for Public Intervention in Food and Agricultural Markets

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For a century, economists have recognized that free and functional markets do not always exist for farm products. Consistent with this recognition, several contingencies were developed for use by farmers, and others, to protect and enhance their interests in relation to product buyers and input suppliers. Probably the most visible and significant of these contingencies were antitrust policy, cooperatives and marketing orders. Each of these policy instruments enables changing the structure and/or behavior of the market.

Changing the basic power balance between buyer and seller is intended in each case. In this sense, these policies are considerably more ambitious than the group of policies (such as market news and grades and standards) that are intended to facilitate orderly marketing. Marketing orders and cooperatives are seen as a special privilege for the agriculture and food sector. Advantages farmers receive from all of these policies can lead to over production unless entry is restricted. Many people feel it is inappropriate for the federal government to facilitate marketing programs that restrict output and increase price. For these and other reasons, these policies have been more controversial than policies intended to enhance natural market forces.

This paper presents an historic evolution of the central ideas used in justifying government interventions to reshape agricultural market structure and organization. These justifications are then placed into a more modern context. A tentative assessment is drawn concerning how the historic rationale stands up to changing times. An effort is made to determine if there are aspects of modern and emerging food markets representing hazards not found in history. Finally, suggestions are made concerning what types of policies might better fit the modern context.

Historic Policy Determinants

Policies establishing antitrust legislation, marketing orders and cooperatives were developed almost entirely during the first third of the twentieth century. These policies are drawn from the events and experience during this period as well as the last third of the nineteenth century. In addition to understanding the characteristics of the economic environment of a century ago, it is useful to understand the political climate of the time and how it relates to economic power. From the very beginning, American policy has evolved in an atmosphere of great dread concerning vested power. This is true of political power, but also true of economic power.

In comparison to other nations, the "colonies" had great ethnic diversity. As they came together it was difficult for them to trust each other. Their best hope of getting a fair deal was perceived as an arrangement in which no one had much power.

This atmosphere was reflected in de Tocqueville's observation that the American democracy was built on a strong preference for weak central government. In our constitution, much space and effort were devoted to the establishment of rights of individuals and regions (states). de Tocqueville assessed that other nations might prefer such an arrangement but found it infeasible because of the pressure of territorially aggressive neighbors. Weak central government, in deference to the rights of regions and individuals, proved ineffective in war and defense. The American democracy grew with a well-recognized distrust of vested power while all other Western nations grew in tight ethnic homogeneity and with a greater tolerance of vested power.

From this beginning, American policy evolved to deal with the conditions of a frontier nation. Agriculture always moved to the frontier. As new lands were settled, a populous- and subsistence-oriented agriculture shared the economic development process with a few other extractive industries – trapping furs, timber, mining, etc. Early settlements were always pushed beyond the service range of the economic infrastructure of the time. Few services were available. Transportation was poor. Communication was difficult. The subsistence households were largely self-sufficient, only seeking a market for occasional surpluses and for supplies they could not produce.

The 1870's was the decade in which rail lines grew the most. However, for the first third of the twentieth century, many mud roads were still making farm transportation difficult. Telephones, newspapers and radio eventually brought effective market communication to the farm. These services did not reach many farmsteads until the 1920's and 1930's, and the depression of the 1930's and WWII delayed the industrial adjustment and response to the more developed transportation and communication technology until after 1950. Most of the basic market intervention policy (Sherman Act, 1890; Capper-Volstead Act, 1922; Agricultural Marketing Act, 1937) was in place by the 1930's. It was drawn mostly from conditions, problems, perspectives and values that related to farmers' experience selling in markets made very narrow by lack of basic transportation, communication, processing, storage and other capabilities.

While the state of transportation, communication, technology and investment hindered the functioning of farm commodity markets at the "turn of the century," there were household characteristics that made markets work better. Markets for food commodities were more elastic because "turn-of-the-century" households were more flexible. There were on-site homemakers and much of the food preparation, preservation and storage was done in the home.

This system could adjust to changes in the availability of supplies. The low level of real income made it imperative for households to respond to price changes. Large seasonal production would move through the market as prices became attractive. Home preservation and storage of food in a large share of the households facilitated this flexibility.

Frontier Policy

Steen's account of a tobacco producer's marketing experience in the early 1900's gives perspective to the developing agricultural and food marketing policy.

> Following the establishment of the trust, tobacco prices dropped to a very low level.[3] Growers had been in poverty before, but their poverty now became actual misery. The situation was greatly aggravated by the behavior of the tobacco buyers. 'It was necessary to give the American Tobacco Company's local representative a ham before he would look at my tobacco, and very essential also to remember to lift my hat when I met him on the road,' a veteran grower declared.
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> [3] The trust was generally charged with forcing prices to extreme low levels. Undoubtedly it was a prime factor in depressing the market, though it must not be overlooked that there was a tremendous over-production of tobacco beginning about 1900 (Steen, p. 12).

The account goes on to discuss the "tobacco trust" emerging as a result of a merger in 1903 which was dissolved by the U.S. Supreme Court in 1911. The proud spirit of the Kentuckians rebelled. Organization (called tobacco pools) and behavior (called "night-riding") were developed to deal with this oppression.

Would the same story be told differently in another culture? We put the reflections of power (the ham and the hat) in the text and the less exciting economics (the "tremendous over-production") in the footnote. Even the footnote admitting over-production gives major billing to power. One explanation of this story is that high transportation costs and few buyers in geographically dispersed regional markets can exert market power, ham being just one part of the economic rent extracted from farmers. But, is it possible that another culture would have found the primary explanation for low prices in over-production? If so, would resultant policy be oriented to the basic power balance between farmer and industrial buyer? The American frontiersmen were rugged individualists. They had little tolerance for business bureaucracies or large government. They did not feel like "lifting their hat" to anyone. This individualism was a strong current in our culture as well as being written into our constitution.

Our country has always had a highly developed "industrial policy" relating to economic power. Even though our economy has long been the largest national economy in the world (giving more room for large firms in relation to the size of the market), we have always had the most developed monopoly policy. There are few economic studies that place the economic loss to "monopoly" as being very high. Most economic analysis assumes competitive behavior. The primary reason for this tradition of concern about market structure grows from our culture rather than an experience of market failure.

While it seems appropriate to develop the cultural determinants of our market intervention policy, it must also be recognized that frontier conditions exacerbate market structure and market power situations. The lack of infrastructure (especially transportation and communication) cuts off alternative buyers or sellers. It makes the relevant market small. Within these small markets, high concentration and lack of market alternatives are typical and perennial occurrences. This setting, combined with a culture sensitive to power imbalances, gave rise to our policy tradition.

An Alternative Industrial Policy

The most central topic under current debate in the area of industrial policy is not how to cope with monopoly but how to nurture and support key industries to enable them to be internationally "competitive." Over the past two decades, our economy has become increasingly integrated with a global economy. Many companies in industries in which we compete in international markets have the support of their governments – directly and indirectly. We have been slow and awkward in relating to this situation. We have little momentum – either in organizations or in relationships between public and private agencies. There is little education and training developed for guiding and enlightening such a process. Perhaps the biggest problem is that it is in conflict with our culture and tradition for industrial policy. Because of our tradition, this new policy pattern looks like putting the fox in the chicken house.

It is not as if the new call for a nurturing industrial policy confronts a vigorous antitrust policy. While our market intervention policy has been highly developed on paper, it has been largely dormant and unenforced for years. It is quite likely that the cultural influences that were important in the frontier conditions in which the policy evolved have been greatly lessened as our culture has become more mature and modern. Our tolerance for vested power may be growing, approaching that of other countries. With lessened individualistic influences in our culture and a heightened perceived need, there is a growing sense that our policy course will take significant new directions in the near future. The new Clinton administration is more likely to embrace this kind of change than the past, more conservative, administrations.

The list of major changes in the economic environment most likely to affect the emerging industrial policy include at least the following:

- A growing public recognition that the economic well-being of U.S. firms is closely linked to job creation and economic growth in America. This recognition is giving rise to greater tolerance of concentrated economic power in U.S. firms.

- Development and enhancement of basic infrastructure for business transactions – transportation, communication, storage, expanded opportunity for processing and preservation, import/export services, etc. – making the relevant market broader and alternative competition more available.

- Increasing sensitivity to the importance of international competitiveness, its requirements and the growing reality of foreign competition as a constraint on market power of local firms, e.g., General Motors.

- Inflexibility in the consumer market for food. Consumers do not respond to price changes as they did when much of the preservation and storage of food stocks was performed in the household. Retailers now set prices more as a response to other retailers or as a way to promote the store than as a way to clear the market (Padberg, Knutson and Jafri). As a result, farmers need more functional means of controlling market volume.

In addition to changes in the economic environment, there may be other "standards" an updated industrial policy must meet. A greater share of our population participates in higher education than in any other culture of any size. We have a tradition of investigative journalism that is highly developed. There are advocates for consumers and public interests who bring great analytical and communicative power to bear on policy choices and enforcement processes. It is important that industrial policy make common sense and be understandable to citizens and businesses.

A century ago, the average household was larger and sought large volume purchases of a few staple foods. Price collusion was the most natural behavior pattern for the producers of homogeneous goods. There were few specialized "consumer products" as we know them today. Policy that made sense for homogeneous goods frequently became confused when applied to consumer products of more recent times. With consumer products, differentiation is the most natural behavior. Trying to apply the policies designed for nineteenth century commodities to twentieth century consumer products has resulted in inconsistencies among Federeal Trade Commission (FTC) and court decisions.

Firms the public sees as performing very well, IBM, Kellogg, ATT and Safeway (especially in Western Canada), have been the focus of antitrust action or concern. Truckloads of "data" have been collected in the discovery phase of litigations (Because no one knew what was important to learn or display in court, they collected everything). Of course, these conditions make enforcement very expensive and, at the same time, make the justification and purpose of antitrust policy difficult to define.

The Direction of Policy Evolution

It seems most unlikely that traditional antitrust policy will be formally repealed. That would be un-American. It would involve a clash with traditional values. There is uncertainty about the modern rendition of these values sufficient to sustain the traditional laws on the books. However, traditional antitrust policy has already been significantly de-emphasized by lack of enforcement.

This is likely to continue with new laws emerging to constitute new directions. The new policy will focus on new directions rather than actually changing the traditional structure.

Antitrust

Traditional antitrust policy has a central focus in market structure. The concern about structure is related to expected deficiencies in performance. Since traditional policy was developed in a culture sensitive to power, it was easy to link monopoly market power or concentrated markets to exploitive prices. This link will work less well in the future for three reasons: 1) the culture is more flexible in relation to power as an issue, 2) globalization of economic activity gives "competition" to a single firm industry in a particular country, and 3) barriers to entry within an industry have significantly declined in recent decades as firms have expanded horizontally into new markets and capital markets have become fully internationalized. The third point has been emphasized by Bau-mol, Panzar and Willig and is referred to as the theory of contestable markets.

The new directions in an industrial policy are likely to deal more directly with performance. "Disclosure" as a policy instrument has great promise here. A recently defeated Congressional proposal to require auto ads to report mileage data provides an example of a direct performance policy. With this instrument, the salience of different marketing strategy dimensions for different products can be controlled. Consumers are given full information about product characteristics and price. The full strength of this policy has yet to be developed and appreciated.

With food, unit pricing and nutritional labeling are examples of direct performance policies. Forced disclosure of basic comparative pricing and basic quality information brings major responses from food manufacturers and distributors to the way they use the power of the media and other competitive choices available to them. The extent and type of technology deployed is affected. Substance and content of the product or store image chosen in competitive rivalry are also affected by these policies. Clearly, disclosing basic facts about prices and nutrition (apparently for consumer use) causes manufacturers and distributors to do a more satisfactory job – whether consumers read the labels or not.

We are able to design and require disclosure of nutritional information because we have invested great energy in studying this complex subject and have an experienced enforcement body. There may be other aspects of products and industry performance that could be "disclosed" with similar positive results. We should give more study to the kind of performance measures the public demands and ways to describe them. We would like to see more of the "line of business reporting" that was once required. We may need to learn to select, articulate and report a new set of values. The accounting profession can develop appropriate financial measures salient to consumers as economic performance indicators are conceptually developed and described.

It should be noted that traditional anti-trust measures are likely to persist well into the future in agricultural commodity markets in which farmers sell homogeneous products in regionally concentrated markets. In these situations, high transportation costs and high perishability limit farmers' ability to seek alternative buyers and buyer concentration may indicate the possibility of above normal processor profits.

Marketing Orders

The modern pattern of marketing orders has its roots in the late 1920's and 1930's. Within the McNary-Haugen legislation (a developmental pattern for new ideas that was never implemented) the term "market agreement" was first used to refer to arrangements for control and disposal of commodity surpluses. Marketing agreements, which became law in the Agricultural Adjustment Act (AAA) of 1933, involved the power and finance of the federal government in cooperation with marketing firms – cooperative or corporate. Parts of AAA were invalidated by the Supreme Court in 1936.

Marketing orders grew from the Agricultural Marketing Act of 1937 which picked up the features of marketing agreements and added an array of other collective marketing strategies. While advertising, standardizing containers, control of grade, size and maturity, etc. were added to the list of permissible capabilities available to industries with marketing orders, "supply management" in the marketing channel was clearly the main provision in the enabling legislation. Entry into a market order was not limited, but provisions existed for destruction of developing crops.

This pattern of market intervention policy began in the Great Depression with a heavy emphasis on aggressive "emergency" supply control programs (Nourse). The administrators of these programs were surprised at how many conflicts emerged as a result of these interventions. There was a long list of conflicts within agriculture, in addition to the predictable conflicts with marketing firms and others. The WWII and post-WWII years of high food demand brought lessened urgency and a natural de-emphasis of most marketing order programs. Marketing order programs got more attention during the 1950's and 1960's. By the mid 1960's, the general thrust of the approximately one hundred federal and state marketing order programs had shifted to marketing services, such as advertising. Only 25 percent of these orders made use of the capabilities for regulating total quantity or surplus (National Commission on Food Marketing). While comparable data are unavailable, it seems the trend to marketing services has continued in the federal orders.

We look at marketing orders as policy enabling the changing of market structure and/or conduct. This is probably because such capabilities are available in the enabling legislation. In fact, marketing orders are primarily vehicles to provide collective marketing initiatives, services and programs. It is possible under their provisions to use a "check-off" to finance advertising or other marketing programs (some advertising programs have their own specific legislation that enables a check-off). The check-off enables equitable spreading of costs; an important result. Without being able to equitably spread costs, collective marketing programs could not be developed, in many cases. Almost all of the controversy concerning marketing orders is centered on the supply control features. Marketing services, now the most typical uses of marketing orders, have not been contentious – either conceptually or on the basis of practical experience.

It is interesting to consider the importance of quantity control programs as permissive features of marketing orders. How has the need for this feature changed as we have adjusted to an industrialized food complex? The food production structure has become more stable as farmers have become more specialized, more commercial and much larger. The smaller general farms of the first quarter of this century could often double or triple their sales of a particular commodity, in response to an encouraging price signal. This was possible because they operated many farm enterprises and consumed a substantial share of many of their products. Within this complex, both production and consumption patterns could change to substantially shift sales of a given commodity. By contrast, the more specialized producer of today may intensify production and offer a larger quantity for sale, but the change will be a much smaller proportion of his normal output. High technology production has more fixed costs and is more inflexible. The fact that there are many fewer producers also makes production decisions more stable and predictable.

Since the supply control features were designed primarily to deal with a chaotic and unpredictable industry of small producers, greater rationality and more stable behavior of producers should lessen the need for these features. If everything else remained unchanged, that would be a credible position. At the same time, however, there have been changes in the demand side of the food system. Many foods are more processed today than in the past. When a processor gets shelf space for a product, it expects to keep the product there with a stable flow of goods regardless of fluctuations in marketings or price of a major (or minor) ingredient. A food manufacturer is not interested in producing more than usual output because of excess supplies of an ingredient. This would require "developing" a larger market only to relinquish it when production returned to normal. Marketing costs are too high for that. In addition, the costs of ingredients are a smaller part of total costs than was the case when food was less processed and less differentiated at the consumer product end of the system.

Food retailers are influential in establishing retail prices for unprocessed foods such as produce items. Their pricing patterns usually have more to do with competing retailers than being a market-equilibrating and market-clearing institution for produce. They may have 20,000 items or more to price. It is unlikely they have much incentive to even be aware of the supply conditions of each product (Padberg, Knutson and Jafri).

In addition to the inflexibility built into the industrialized food system, the typical consumer is responding to different conditions. Large households, buying food commodities in wholesale quantities, have been replaced by smaller households buying extensively prepared food products. In accordance with Engles Law, the proportion of income spent on food has dropped from about half a century ago to something like 12 percent. More than 40 percent of the food expenditure is for food away from home. All of these conditions make the consumer market less flexible and less responsive to price movements. The need for "vertical coordination" on the part of producers and the marketing system becomes greater as the retailer, manufacturer and the consumer become less sensitive to prices of output from the farm.

Unlike antitrust, there is not much of a basis for changes in the policy supporting marketing orders. The more contentious quantity control features are not the most used dimensions of this intervention policy. With the growing need for vertical coordination in farm output and within the marketing channel, there may be a greater need for quantity management in the future. These capabilities are still needed. The reasons for the need are different, but the need is no less important.

Cooperatives

Agricultural cooperatives experienced a long developmental period beginning well back in the nineteenth century. Around the world, there were broad structural changes in most societies emerging during this period. The industrial revolution was occurring, bringing much change to the life of workers and a more focused definition of "capital" and "labor." Many people experimented with communal societies (New Harmony, Indiana; The Shakers, etc). A group of flannel weavers in Rochdale near Manchester, England, developed a pattern of cooperation that struck an especially productive balance between the rights and responsibilities of participants. As the agricultural cooperative history in the United States developed over the next half century, these "Toad Lane Principles" became extensively used and appreciated.

Although there was extensive experience beforehand, the specific basis for cooperation was formalized in the Capper-Volstead Act of 1922. The formalization and growth of cooperatives shared the history and events described with both the antitrust movement and the development of marketing order legislation. There is a significant interaction between these patterns. The antitrust exemption was an especially important development for cooperatives. In many cases, there were close and harmonious interactions between cooperatives and the development and use of marketing orders. Often, cooperatives were able to enlighten and "manage" the political dimension of a marketing order (the requirement for getting farmer support in a referendum, etc.). In addition, cooperatives have typically put together the brain trust which developed and operated the programs enabled by the order.

The cooperative structure had an especially functional history on the American frontier. The lack of business infrastructure was a major problem and limitation to marketing activities. Cooperatives were able to create the most needed parts of a marketing and business infrastructure time after time. This is an innovation role. Many of these early cooperatives were not very profitable, but they enabled an industry to develop. As industry developed, there was enough marketing business to support investor-owned businesses and they followed. As cooperatives became competitors with investor-owned businesses, cooperatives placed greater emphasis on providing a competitive yardstick useful for understanding and negotiating with conventional business. As the thrust of food marketing has come to involve highly differentiated consumer products, the role of cooperatives has shifted again. Of course, there are many fewer cooperatives in the brand development business than in the development of frontier infrastructure. This is not necessarily a reading on the effectiveness of cooperatives. Developing successfully differentiated products happens only in an industry of a few giants. It is just the nature of that business. There are fewer investor-owned firms at this level also.

The future of agricultural cooperatives poses interesting and difficult questions. Today's environment is fully developed and often redundant in the provision of most marketing services. The role of cooperative development of new and needed services is less than on the frontier. Yet, several of the traditional roles of cooperatives are still needed. The "competitive yardstick," the packer of private label products, the manager of producer politics in marketing order initiatives, the developer of branded products, the introducer of new technology – requiring careful management of producer politics, such as bovine somatatropine (BST) – all may be roles cooperatives will occupy effectively.

Summary and Conclusions

As the colonists pushed the American frontier westward, they devoted most of their attention and energy to the problems of life on the frontier. Little energy or respect were reserved for jockeying for position within political or economic bureaucracies. Their presence on the American frontier represented a flight from such human hierarchy. They had chosen to be rugged individualists, often at a high price. This evolution had a conditioning influence on the development of our new nation's political philosophy and also shaped the basic ways farmers related to each other and to markets. The new pattern of policy developed upon the philosophy that economic power should not be vested in the marketing system. Conversely, anything that could be done to increase the power or leverage of the frontier farmer should get careful consideration.

From this beginning, a package of antitrust policy, unique in the world, developed in the US. It was hard to explain why the largest economy had the greatest problem with concentrated industries. Part of the explanation came from markets made thin by the lack of communication, transportation, processing or storage alternatives. Natural monopolies like the railroads had an influence. In addition, it was a conditioned reaction in our culture to be threatened by economic power. As we lay the policies developed in this situation against modern economic realities and problems, many of them fit poorly.

A century ago it was not difficult to explain to a common citizen what was wrong with a highly concentrated industry (or "trust" in the vocabulary of the time). Today it is more difficult. It is a common occurrence to see large firms and concentrated industries that are held in high esteem. Not only has modern antitrust become mysterious to the man on the street, experts are now unsure what constitutes a violation of this policy. Litigation has come to require a search process collecting and processing vast quantities of data and records, consuming vast budgets and staffs for both the prosecution and the defense. Only a tiny minority of professional economists put much trust in this process. While it is unlikely these laws will be repealed, we will see much less of them in the future (Isn't this called benign neglect?).

An optimistic possibility would be to see a policy of affirmative disclosure replace the traditional pattern. This policy could describe the aspects of industry performance of greatest public concern and require facts about those aspects be disclosed to the public. This process harnesses advocates and the press to encourage the behavior of large firms to correspond closely to the public interest.

Marketing orders and cooperatives have survived into times and conditions very different from those of their beginnings. While their roles and focus of attention have made several adjustments to new conditions, the basic structures are still needed. Power balances may figure less in the purpose of these institutions than in the past. Both provide an enabling structure to support collective marketing initiatives. These structures are just as important in providing vertical coordination and advertising programs as they were in their earlier tasks.

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