HOW WILL PRODUCTION, MARKETING, AND CONSUMPTION BE COORDINATED?

From a Marketing Viewpoint

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Agricultural marketing is big business. The marketing system for farm products in this country annually moves and transforms millions of tons of foodstuffs worth more than $65 billion (retail value). It likewise handles nonfood products of agriculture worth several billions more.

Each commodity passes through a succession of stages including production, processing, and distribution on its way to the consumer. The decisions made at each stage with respect to the commodity determine such matters as the variety and quantity produced, quality, size, weight, degree of processing, packaging, and method of merchandising before it gets to the consumer.

Proper coordination of the various stages is highly important for greatest efficiency in the whole process. Coordination of the various stages in the food industry can be both internal and external to the firm.

When coordination between production and marketing is lacking, the production side often turns out commodities for which the marketing side has no immediate outlet at a satisfactory price. One reason for such a situation stems from the basic characteristics of technology as it has evolved in agriculture and marketing. Production is efficient in relatively small units, whereas marketing is most efficient in much larger units. Historically, production and marketing functions have largely developed under separate control and management.

WHAT HAS BEEN HAPPENING IN PRODUCTION?

We have been witnessing the explosive period of farm technology when yields of crops and rates of livestock production have exceeded previous records year by year. For many products, output-increasing forms of technology have been adopted by farmers at a rate which causes total farm output to increase faster than demand is expanding. Once the capital investment is made in new technologies, the new production methods are irreversible and are likely to continue even though prices fall. Such a situation can mean trouble for farmers when production is not geared to meet the needs of the market.

SOME APPARENT WEAKNESSES IN MARKETING

In general, efficiency in marketing of farm products has lagged behind efficiency in agricultural production. The weakness is in the market system as a whole more than in the individual sectors and agencies that comprise it. This is mainly because the system has been and still is highly segmented and disjointed. Most serious of all has been the lack of proper coordination between production on the farm and marketing operations off the farm. When production is carried on by one large group of operators acting independently and distribution by another group acting independently with no coordinating or integrating mechanism in between, real difficulties can arise. If there is a third group of independent processors in the system, the difficulties are greater. And further, if additional groups of independent wholesalers, brokers, and jobbers are handling the product at certain stages, smooth operations and adjustments of supplies to meet specific market demands and specifications are all the more difficult.

WHAT HAPPENS WHEN COORDINATION IS LACKING?

Consider what sometimes happens when producers and consumers are widely separated by all these intermediaries, each acting independently:

First, production, prices, and consumption get badly out of line with each other because of poor communication between consumers and producers. Supply is slow in adjusting to demand, and this usually results in lower prices to producers.

Second, and closely associated with the foregoing, the spreads or margins taken by each independent segment tend to be the same on big crops as on small crops; and everybody makes more profit from a big crop than a small crop except the producer. This leads to rigidities that prevent retail prices from rising and falling as much as they should, and this keeps consumption from expanding as much as otherwise might be possible to absorb the larger crops.

Third, in a disjointed marketing system too many operators tend to go into business at the various levels in the marketing process. Much of the criticism of our marketing system is aimed at the high costs arising from too many links in the marketing chain. The number of links do not increase distribution costs so much as the number operating at each of the links. If more operators are needed to take care of increasing population, this might be justified; but if more country buyers, for example, set up business in a given area of relatively stable production and if all make a living, they are taking that much business away from other similar operators in the same area. Such operators can stay in business only by raising margins on business handled or getting along with smaller incomes. Most of them will manage to stay in business by doing a little of both.

Fourth, instead of lowering costs by increasing efficiency, as in production or manufacturing, the competitive force in procurement or distribution tends to maintain rival buying or sales organizations which try to take business away from each other through public relations, advertising programs, and the like. Under these circumstances, competition also works in such a way as to expand the services that go with the products far beyond what the buying public desires to pay for them.

Because of the need for sound answers to problems of this type, Congress unanimously passed a joint resolution on July 3, 1964 to establish a National Commission on Food Marketing. The principal duties of this commission are to study and appraise the marketing structure of the food industry. The commission is also to suggest changes in statutes or public policy affecting the food industry, which would achieve the desired distribution of power as well as desired levels of efficiency.

We shall all be very interested in the findings and the reports of this commission. These findings will have a strong bearing on the topic we are discussing this morning.

ADVANTAGES OF COORDINATION

Integration and coordination have many advantages for the whole food industry. From the production standpoint, efficiency and performance are improved in that production can be adjusted at one stage to meet the needs at the next to better advantage. Quality improvement and control can be facilitated, specialization at each level of management is possible, and improved technology and methods may be more rapidly and efficiently adopted.

From the marketing viewpoint, coordination improves efficiency in production and lessens waste in marketing by reducing the number of operators handling the product, by reducing unnecessary duplication of activities, and by achieving some economies of scale in operations. Coordination also facilitates proper timing of production operations with marketing operations so that a continuous supply of uniform-quality products is forthcoming to satisfy the needs and requirements of retail outlets.

HOW CAN COORDINATION BE ACCOMPLISHED?

The basic question we are considering here today is: "How will coordination in the food industry be done?" We know that vertical integration or coordination is being accomplished in varying degrees through the use of several methods, including:

1. Farmer cooperatives.
2. Processor-producer contracts.
3. Ownership of larger farm units with each being capable of buying supplies, producing, processing, and marketing products effectively for itself—initiated from either the production or processing end.
4. Voluntary coordination or "gentlemen's agreements."
5. Marketing agreements and orders, which are sort of a hybrid between a private venture and a government program. They are often referred to as "self-help programs." They can be initiated by virtue of special legislation that imposes compliance on a minority of farmers and upon handlers if a prescribed majority votes them in.
6. Government programs (supply management).
7. A combination of the above devices.

The coordination in agriculture may be partial or complete, depending upon the particular functions and services that are under control of a single management unit. In the private sector of our present system, the integrator or coordinator undertakes the coordination and control of the product when he sees the potentialities for additional net earnings that might be realized. How complete the business coordination may be depends upon the aims and objectives of the coordinator and the finances and abilities available to reach those objectives.

Information on the marketing situation and outlook is an aid to those concerned with production and marketing coordination. For more than thirty-five years the U. S. Department of Agriculture and workers in every state have tried to supply farmers and marketing firms with up-to-date information about trends in production, consumption, and marketing, which would aid them in coordinating supplies and services to meet the specific needs of the market. The U. S. Department of Agriculture and the land-grant colleges at various times have conducted studies and developed projections and production guides to aid farmers in adjusting to changing economic trends.

Such efforts are helpful, but incentives are usually not strong enough and the adjustments are not made quickly enough for many farmers to avoid difficulties.

In the foregoing paragraphs I mentioned that several methods can and are being used to help obtain better coordination. Time allotted will permit detailed evaluation of only one or two of these methods.

COORDINATION THROUGH COOPERATIVES

Large farmer cooperatives that handle the products all the way from the farm to the consumer or alternately, large consumer cooperatives that do the same thing, but from the consumer end, both place the whole marketing process under one management, which is thus in a position to integrate all the steps in the system and make them efficient.

Many cooperatives operating today fit into this pattern, some going further in the total process than others. As cooperatives move into more integrated types of operation, they must develop better methods to enable members to share risks and earnings equitably throughout the whole integrated process. Much progress could be made to achieve better coordination of production and marketing through cooperatives if membership understanding and support for the various proposals could be developed. This comes slowly and requires much patience and educational work to overcome "the human element."

The farmer cooperative is one logical form of business structure for producers to use in their effort to bring about market improvement, development, and coordination. To be most successful in today's food economy, cooperatives must adjust their organizational structure, management, and membership relations to three basic goals:

1. To plan and coordinate the entire farm operation in advance to yield products wanted by the trade.
2. To program delivery of products in the quality, packs, packages, amounts, times, and places required to meet the operating and merchandising needs of customers.
3. To speak for the farmer in the new markets in which the prices of his supplies and his product are determined.

These goals must be sought in a world of technological change, increased capital requirements, changing marketing methods, and increasing scale of operations of plants and firms. As co-ops become larger and more complex, members may have to surrender some decision-making power to the central group. The challenge is to develop procedures for making fast and sound decisions by management with prompt and meaningful accounting to members. This is not easy now and will be more difficult as co-ops grow larger.

The economic interests of the farmer members should be the paramount concern of co-op management. Likewise, the farmer himself must realize that production, processing, and sales are inseparable for a successful operation. The possibilities are there. The big question is: Will farmers work well enough together to build and sustain the type of cooperative association that can do the job that has to be done?

GROWER-PROCESSOR CONTRACTS

Grower-processor contracts can be an effective tool for controlling the quantity and quality of products produced for a specific market. Contract terms may vary widely from simple understandings to detailed specifications.

Through such contracts, growers of processing vegetables, for example, are able to assure themselves before planting of a market at a known price for the production from the contracted acreage. Processors similarly are able to assure themselves of a source of supply, subject to variations in yield, at a predetermined price and to exercise some measure of control over what is produced.

Strong bargaining associations established by farmers in some areas of the country have been instrumental in developing the types of contracts used and negotiating annually for price and other contract provisions.

Similar grower-processor contracts are used by other commodity groups with variations to suit their particular conditions. Nothing is wrong with this type of production-marketing coordination if the contracts are sound and equitable for both parties.

COORDINATION BY PROPRIETARY FIRMS

Chain stores or large processing firms are good examples of integration or coordination that can be achieved. They may integrate through ownership or contracting the various stages of production, processing, and distribution. Some protection of the public has proved to be necessary where extensive integration under private management has developed. More regulation will be forthcoming unless management of these large firms finds ways of operating that protect them from monopolistic tendencies or accusations of the same.

WHO WILL CONTROL THE COORDINATION?

In evaluating the changes that are occurring and which will likely occur with respect to business coordination, farmers raise many questions, such as:

1. Where will the control rest? Will it be with the farmer-producers or with retailers?
2. How will the benefits of coordination be distributed among the important segments coordinated?
3. Will producers, processors, and distributors be affected in the same or different ways relative to profit maximization?

These are only some of the questions that could be raised. Thus, we may say that business coordination can be a threat or a promise for the farmers. Much depends on who is doing the coordination and who is being coordinated.

The problem of working out a fair sharing of the food dollar among producers, processors, manufacturers, and distributors will call for a cooperative attitude and a degree of future-mindedness which is not afraid of change.