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THE NEED FOR VIGOROUS ANTITRUST ENFORCEMENT

by

Willard F. Mueller

WP- 18

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## THE NEED FOR VIGOROUS ANTITRUST ENFORCEMENT

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Mr. Chairman, it is an honor and pleasure to appear before this Committee, and for me it also is a nostalgic appearance. I first testified before this Committee 18 years ago before Mr. Steed's Subcommittee examining problems of price discrimination in the dairy industry.<sup>1/</sup> The following year that great and kind man, the late Wright Patman, persuaded me to serve for a short time as the Committee's chief economist.

I also welcome the opportunity of sharing again the witness table with Professor John Kenneth Galbraith, one of the truly great political economists and public servants of our time. Nearly 11 years have passed since I was similarly privileged, when the Senate Small Business Committee held a special hearing the day before public release of Professor Galbraith's insightful book, The New Industrial State.<sup>2/</sup> On that occasion I was invited to play the role of critic, a role I played with greater enthusiasm than success. Those who expect me to replay that role this morning will be disappointed. Today Professor Galbraith and I agree about much more than we disagree. Some may infer my criticisms have softened because I no longer am, as Senator Long characterized me in 1967, "a high-level member of the FTC's technostructure."<sup>3/</sup> But my changed views do not reflect my changed station in life. The explanation

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<sup>1/</sup> "Small Business Problems in the Dairy Industry," Hearings before the Special Subcommittee of the Select Committee on Small Business, House of Representatives, April 6, 1960, Part V, pp. 739-77.

<sup>2/</sup> "Planning, Regulation, and Competition," Hearings before the Subcommittee of the Select Committee on Small Business, United States Senate, June 29, 1967.

<sup>3/</sup> Ibid., p. 3.

is simple. Experience has converted me, in part at least, to Galbraith's view that much of antitrust is, indeed, a "charade." By promising more than they can deliver, antitrusters mislead the public into believing economic power is being policed successfully. Thus a deluded public has come to believe that some industries are becoming more concentrated because the big are always the best and that the small are always the least efficient.

But having acknowledged my disenchantment with much antitrust, I still cannot embrace Galbraith's prescription that we concede the failure of the antitrust laws and "allow them quietly to atrophy."<sup>4/</sup> Galbraith urged this course in the expectation that having done so, "Then we would face the real problem which is how to live with the vast organizations--and the values they impose--that we have and will continue to have."<sup>5/</sup>

Professor Galbraith's recommendation that we permit the antitrust laws to atrophy assumes that they will be replaced with more effective instruments of social control. But what are these new instruments of social control and who are their champions? I am not at all confident that those who control "these vast organizations" will permit Galbraith's bright new day to dawn. Until viable alternatives exist, how will small and medium business fare in a world where holders of vast economic power can bring it to bear without any threat of government or private antitrust challenge. No, until an alternative is found we must retain and strengthen our antitrust laws and enforce them with greater vigor, while recognizing that they must be supplemented by other forms of social control.<sup>6/</sup>

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<sup>4/</sup> Ibid., p. 11.

<sup>5/</sup> Ibid.

<sup>6/</sup> Mueller, "The Social Control of Economic Power," in Bonello and Schwartz, Alternatives in Economic Policy, University of Notre Dame Press, 1978, pp. 125-151; Mueller, "Antitrust in a Planned Economy: An Anachronism or an Essential Complement?", Journal of Economic Issues, June 1975, pp. 159-179.

Time permits touching on only a few matters relating to the future of small business and what can be done to improve the environment in which it operates. I will discuss two areas in which I am currently doing some work relevant to these issues.

The Rise of Concentration and Fall of  
Small Business in Manufacturing Industries

In most of manufacturing, modern technology rules out highly fragmented industries occupied by vast numbers of companies. But this truism does not warrant the inference that imperatives of large scale dictate the emergence of "monopoly capitalism" and the demise of all but giant corporations.

Ominous trends have been underway for the past quarter century. The greatest damage to competition and small business in manufacturing has occurred in consumer product industries. (These are products manufactured for consumption by final consumers, e.g., canned goods and other grocery products.) Consumer-oriented industries generally require less sophisticated technology and smaller capital investments than do producer product industries (these are industries making products for use by other manufacturers, e.g., chemicals and electrical equipment).

The concentration trends in these two categories of industries differed markedly between 1967-1972.<sup>7/</sup> Whereas producer product industries as a group experienced virtually no change in average concentration, consumer product industries have experienced a persistent upward trend in

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<sup>7/</sup> I first reported on this emerging trend for the period 1947-1963 in testimony before the Senate Small Business Committee. Mueller, in hearings on the Status and Future of Small Business in the American Economy, Select Committee on Small Business, United States Senate, March 1967, pp. 447-95.

concentration (Table 1).<sup>8/</sup> The latter group may be further subdivided into three groups varying with the degree of product differentiation, which refers to real or perceived differences in essentially the same product, e.g., different brands of household bleach, dog food, or detergents. Today, such product differentiation is accomplished largely by advertising. Thus, the three classes of consumer products have significantly different advertising intensities (as measured by advertising-to-sales ratios). The greatest increase in concentration has occurred in the high differentiation industries, where advertising is most important (Column 6, Table 1).

As shown in Figure 1, the percentage of producer product industries experiencing declines in concentration (the share of the industry held by the top four firms) actually exceeded those with increases. An entirely different pattern existed in consumer product industries, where the percentage of industries with increases exceeded those with decreases in all product differentiation categories, especially so in industries with the heaviest advertising.

Figure 2 illustrates the percentage change in the number of companies in the 70 consumer product industries. The number of companies declined in 66 percent of all consumer product industries. Again, the toll was heaviest in the highly differentiated industries, where 81 percent of the industries experienced declines in the number of companies. Although not shown here, the total number of companies in these 70 consumer product industries fell by 12,134, from 49,909 to 37,775 between 1947 and 1972.

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<sup>8/</sup> Table 1, Figure 1, and Figure 2 are from a forthcoming study, Willard F. Mueller and Richard T. Rogers, "The Role of Television Advertising in Changing Market Concentration." It is based on 167 representative manufacturing industries. For an earlier study see Willard F. Mueller and Larry Hamm, "Changes in Industrial Market Concentration," Review of Economics and Statistics, November 1974.

Table 1. Average Unweighted Four-Firm Concentration Ratios by Degree of Product Differentiation for 167 U.S. Manufacturing Industries, 1947-1972

	Total Industries <sup>a/</sup> (167)	Consumer Goods: Degree of Differentiation					
		Producer Goods (97) A/S = 0.1% <sup>b/</sup>	All (70) A/S = 2.2% <sup>b/</sup>	Low (21) A/S = 0.3% <sup>b/</sup>	Moderate (33) A/S = 1.6% <sup>b/</sup>	High (16) A/S = 6.3% <sup>b/</sup>	
	(1)	(2)	(3)	(4)	(5)	(6)	
1972	42.4	42.8	41.8	28.3	41.4	60.6	
1967	41.4	42.6	39.7	25.2	39.2	59.9	
1963	41.1	42.5	39.2	24.6	39.6	57.8	
1958	39.9	42.5	36.3	22.4	36.7	53.4	
1954	40.3	43.4	36.0	23.7	35.9	52.3	
1947	40.9	44.7	35.7	25.9	36.2	47.7	

Change  
1947-  
1972

+1.6

-1.9

+6.1

+2.4

+5.2

+12.9

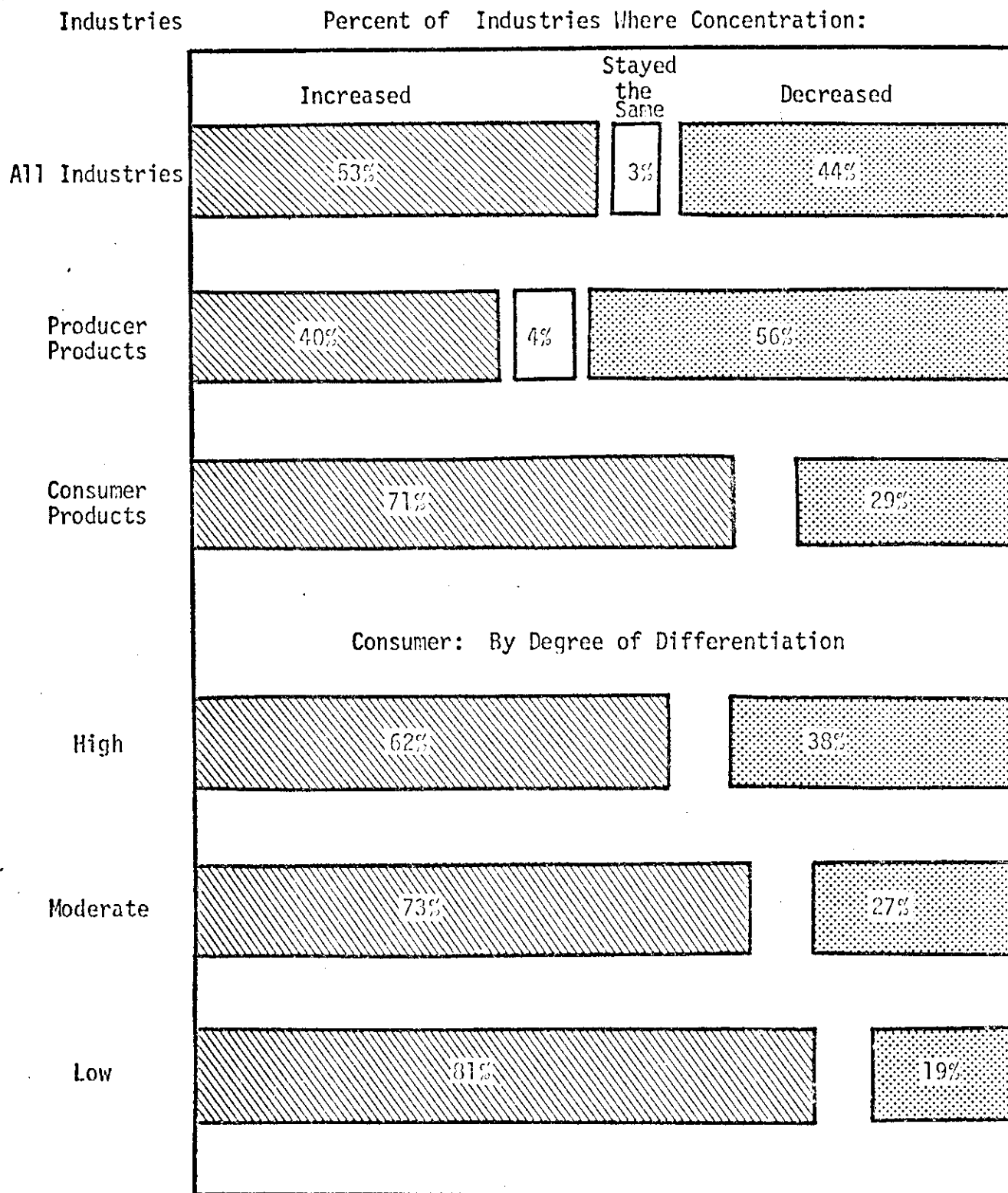
a/ These industries are all those manufacturing industries that had comparable data for the period 1947 to 1972.

b/ This is the average advertising-to-sales ratio for all industries in this group. This includes advertising expenditures for eight measured media in 1967.

Source: Mueller and Rogers, "The Role of Advertising in Changing Market Concentration," Unpublished Manuscript, 1978.

Figure 1

Change in Four-Firm Concentration in 167  
Manufacturing Industries, by Type of Industry, 1947-1972

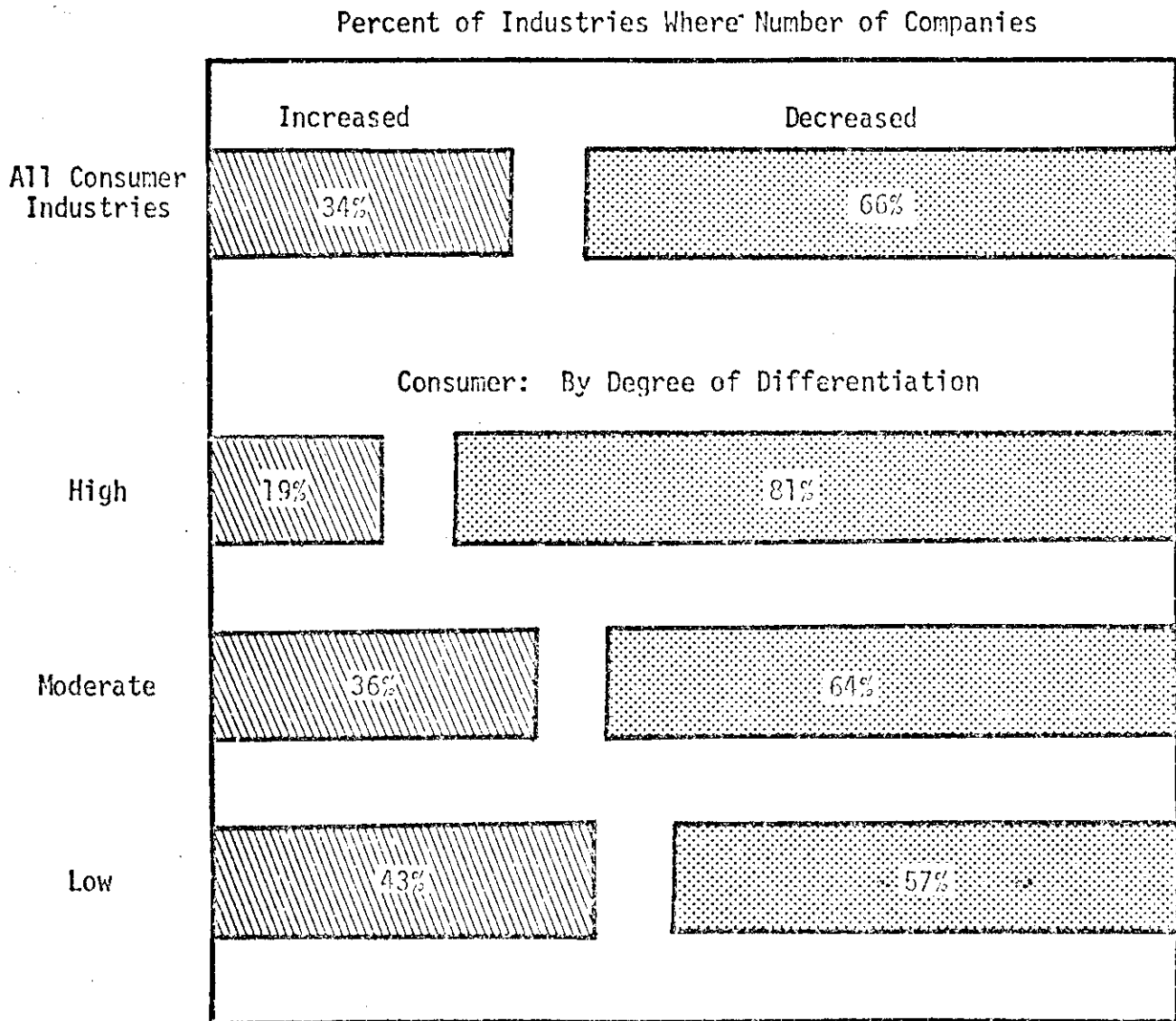


Source: Same as Table 1.



Figure 2

Change in Number of Companies in 70 Consumer Product Industries by Degree of Differentiation, 1947-1972



Source: Same as Table 1.

These contrasting patterns in concentration between producer and consumer product industries are surprising in one important respect. Producer product industries, where the requirements of large scale technology are greater than in consumer product industries, have not changed dramatically over this 25-year period. On the other hand, in consumer product industries, where technology generally is less sophisticated and capital requirements for plants generally more modest, concentration has risen persistently.

Some have argued that the developments in consumer product industries are simply a reflection of economies of large scale in advertising. If true, then the thousands of small businesses destroyed during 1947-1972 were simply the unfortunate victims of economic progress. In this view, all is well in a world where Adam Smith's invisible hand sorts out the efficient from the inefficient; and there is no stopping it, even if one cared and tried.

Perhaps it will not be stopped. But this is not to say nothing could be done to stop it, for there is much more involved than simple economies of scale in advertising.

Based on work done with my research associate, Richard T. Rogers, it is clear that TV advertising and its use by large corporations is at the root of the problem.<sup>9/</sup> Although various factors including scale economies impact on market concentration, our studies show TV advertising is playing a central role in restructuring consumer goods manufacturing. There are, of course, important economies of scale in certain types of advertising. But many small and medium size companies have often survived and prospered

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<sup>9/</sup> Unpublished paper, Mueller and Rogers, op. cit.

so long as they could get access to TV advertising on equal terms and if huge conglomerate rivals did not use massive TV and other promotional strategies in a predatory fashion.

Today, I'll discuss briefly a current example of the way large corporations may use advertising in ways that injure competition and destroy small business.

#### P&G's March to the Sea

Procter & Gamble is the nation's largest conglomerate manufacturer of grocery products with sales of \$7.3 billion and advertising outlays of \$429 million in 1977. Its acquisition of J.A. Folger & Company in 1963 illustrates the strategies a powerful conglomerate firm can pursue to increase the market share of an acquired firm's brand. After investigating this acquisition, the Federal Trade Commission issued a complaint, February 9, 1965, charging P&G with violating Section 7 of the Clayton Act.<sup>10/</sup> However, February 9, 1967, without a trial on the merits, the Commission issued a decision and order requiring P&G to divest its coffee plant, but permitting it to retain the important Folger brand.<sup>11/</sup>

Prior to its acquisition, Folger operated mainly west of the Mississippi. P&G did not immediately make a concerted drive to expand eastward

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<sup>10/</sup> In the Matter of Procter & Gamble Company, Docket No. C-1169, February 9, 1965.

<sup>11/</sup> The order also included several ancillary provisions effective until February 1972. One prohibited P&G from accepting discounts or reductions in media rates of any kind on its purchase of advertising for coffee products in any media used other than those resulting solely from P&G's coffee sales. Another provision prohibited P&G from engaging in price discrimination in the sale of coffee. This provision essentially represented a restatement of the law prohibiting certain kinds of price discrimination.

following the acquisition in 1963. By 1972, however, when it was "freed from the constraints of a consent agreement with the Federal Trade Commission,"<sup>12/</sup> P&G was already on the move. In 1972 it invaded Cleveland "where a horrible time was had by all."<sup>13/</sup> In early 1973 Folger moved into Philadelphia with a saturation advertising campaign. According to an advertising agency official Folger used daytime and nighttime TV ads on 14 stations and "sent 1.5 million six-ounce samples to 1.5 million homes and 25 cents off coupons to one million more. Additional coupons are running in full-page, four color ads in Sunday newspaper supplements."<sup>14/</sup> As a result, according to a smaller Philadelphia coffee roaster, "We're all bleeding to death."

The Cleveland and Philadelphia stories were retold in Pittsburgh. When in 1973-74 P&G decided it "should be in that market too,"<sup>15/</sup> a price war followed. Breakfast Cheer Coffee Co., a \$12 million Pittsburgh company, saw its market share dwindle from 18 percent in 1971 to 1 percent in 1974. Breakfast Cheer was forced to sell out because, in the words of James Deilly, formerly with the company, "We were raped."<sup>16/</sup>

Nor are these isolated examples. The Paul de Lima Coffee Co., a family-run Syracuse business founded in 1916, was another casualty of P&G's march to the sea. The president of de Lima recalled that when he

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<sup>12/</sup> "Bitter Brew: Tiny Firms are Losers in Coffee War Fought by Two Big Marketers," Wall Street Journal, November 3, 1977, p. 1.

<sup>13/</sup> "The Folgers are Coming," Tea & Coffee Trade Journal, May 1972, p. 18.

<sup>14/</sup> Ibid., p. 19.

<sup>15/</sup> "Bitter Brew," op. cit., p. 1.

<sup>16/</sup> Ibid., p. 21. Deilly has filed a private antitrust suit alleging P&G's entry "devastated the small companies."

learned P&G intended to invade the Syracuse market in 1974, "We were quite alarmed, because we had heard about Breakfast Cheer."<sup>17/</sup> His fears proved well founded. P&G offered Syracuse supermarkets as much as 28 percent discounts off the wholesale price and mailed coupons giving 35 cents off the price on a one-pound can, and another coupon for 10 cents off was included with each Folger can placed on the shelf. These deals reportedly had the effect of reducing the price of Folger's coffee to less than 50 cents a pound, about one-half the price of de Lima's coffee.<sup>18/</sup> P&G then "swooped into stores," persuading supermarkets to provide adequate shelf space.

General Foods tightened the price squeeze when it counterattacked. As the market leader, General Foods was not about to yield the field to P&G without giving battle. It poured large amounts into local television advertising, and offered discounts and coupons, in GF's words, "to blunt Folger's introduction."<sup>19/</sup>

Advertising Age recently reported that it had examined General Foods documents revealing that in 1971 GF's advertising agency, Ogilvy and Mather, "urged key members of a Maxwell House group known as the 'Folger's defense team' to match advertising and promotion spending by P&G as it invaded Maxwell House strongholds in the East."<sup>20/</sup>

Small, single-line coffee companies were the main casualties in P&G's march from the Mississippi to the Atlantic seaboard. Small companies

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<sup>17/</sup> Ibid.

<sup>18/</sup> Ibid.

<sup>19/</sup> Ibid.

<sup>20/</sup> "FTC Files Reveal GF's Plan to Make Cora a Star," Advertising Age, April 3, 1978, p. 3.

struggled to survive in the accelerating battle between the two giant companies . The de Lima Company's reaction was typical. It cut prices to below its breakeven point, and began TV advertising for the first time. "We lost money," said company president David de Lima, "in hopes of staying in the market."<sup>21/</sup> But the effort failed, as the company's share fell from 15 percent in 1974 to under 7 percent in 1977.<sup>22/</sup>

In early 1978, P&G launched its long-awaited invasion of the big New York market.<sup>23/</sup> P&G opened its campaign in New York with a massive "direct mailing of 45¢-off coupons, couponed print ads and spot TV."<sup>24/</sup> Shortly thereafter one chain combined the coupon deal to cut coffee prices deeply.<sup>25/</sup>

Whatever the ultimate outcome of the battle for New York, P&G's past strategies teach that it has an awesome capacity for restructuring markets. In the words of a former P&G executive, it intends "to become a national coffee business, and after initial objectives are met, try to become the No. 1 coffee brand in the categories in which it competes."<sup>26/</sup> Says one Wall Street analyst, "They want what's rightfully theirs--50% of the market."<sup>27/</sup> P&G's pursuit of what it perceives as a divine right

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<sup>21/</sup> "Bitter Brew," op. cit., p. 21.

<sup>22/</sup> Ibid.

<sup>23/</sup> "P&G Tops Off Coffee Rollout with Attack on GF Turf," Advertising Age, February 20, 1978, p. 1.

<sup>24/</sup> Ibid., p. 63.

<sup>25/</sup> "New York Store First with Special Folger's Price," Advertising Age, April 3, 1978, p. 78.

<sup>26/</sup> "Bitter Brew," op. cit., p. 21.

<sup>27/</sup> Ibid. Emphasis added.

to a dominant position has left in its wake as casualties many smaller regional coffee companies, just as have its tactics in other industries.<sup>28/</sup> Between 1963 and 1972 the number of coffee roasters dropped from 261 to 162. One source estimates that there are only 40 coffee roasters today and predicts that within a few years P&G and GF will sell over 70 percent of all ground coffee in the U.S.<sup>29/</sup>

This experience demonstrates how a powerful conglomerate corporation can pursue strategies that enhance greatly the acquired company's position. The results are especially likely to be anticompetitive when many rivals are largely single-line firms that are unable to match the tactics employed by the conglomerate, as it selectively applies its power to individual submarkets. When, as in coffee roasting, a substantial firm (GF) already holds a strong market position, the struggle is intensified and the casualties increase when the established firm decides not to yield market share. Here, P&G is the hammer that destroys lesser companies on the General Foods anvil.

It is ironic that after giving its blessing to P&G's invasion via merger of the coffee business in 1967, the FTC challenged in 1975 only the practices of General Foods in the ensuing struggle between the two giants.<sup>30/</sup> It is not clear what the FTC expected GF to do in the face of P&G's stated objective of dislodging GF from its No. 1 position. What

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<sup>28/</sup> For example, in 1957 it introduced its Comet cleanser with a tremendous subsidized advertising push that yielded it a market share of 36.5 percent within 20 months. In the Matter of Procter & Gamble, Docket No. 6901 (1962), Opinion of the Commission, p. 12.

<sup>29/</sup> "Bitter Brew," op. cit. Between 1968 and 1976 Folgers' share rose from 18.0 percent to 21.4 percent of the national ground coffee market. Ibid. In 1974 General Foods accounted for 35 percent of the regular coffee packaged for sale at retail. Complaint In the Matter of General Foods, Docket No. 9085, July 14, 1976.

<sup>30/</sup> Ibid.

does seem clear, however, is that competition will not have been served should it come to pass that P&G and GF end up dominating the coffee industry. The demise of long-established smaller companies with strong regional brands will remove an important source of price competition, leaving the field to huge grocery products conglomerates that rely almost exclusively on nonprice rivalry once they have achieved a dominant position. Although the final act has not yet been played out, events to date seem to have borne out former FTC Commissioner Jones' prediction over a decade ago that the "coffee industry will be significantly less competitive...because of the majority's acquiescence of Procter's acquisition of Folger."<sup>31/</sup>

P&G-Folger's behavior is only one of many situations where conglomerate firms have destroyed small companies. P&G's strategies are so destructive of competition and small business because its huge size and conglomerate operations permit it to zero in on one product or market at a time, destroying competitors by cutting prices and/or elevating costs by massive advertising and promotional campaigns. These practices usually involve massive cross-subsidization--the practice of subsidizing losses in one market or product from profits earned elsewhere. When another conglomerate already is in the market, it responds in kind with the small businessman squeezed in the middle. Success or failure in this environment is not determined by efficiency but by sheer economic power. Surprisingly, most antitrust officials are completely indifferent to this behavior, apparently taking their cue from some of my fellow economists who see such rivalry as "hard competition," and who accuse anyone who

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<sup>31/</sup> Commissioner Mary Gardiner Jones' dissenting opinion in the FTC decision to permit P&G to retain the Folger name.



disagrees with them as favoring soft competition that protects competitors rather than competition. I am reminded of Congressman Emanuel Celler's harsh criticism of those who defended such behavior as hard competition. This perverse view of competition, said Celler, reminded him of the elephant that said, "every many for himself," as he danced among the chickens.

It is high time the antitrust agencies do something about such predatory behavior. Certainly Section 5 of the Federal Trade Commission Act grants ample authority to challenge such anticompetitive practices, and Section 7 of the Clayton Act permits challenging mergers by huge conglomerates. In December 1976 the Federal Trade Commission rescinded its Grocery Products Merger Guidelines without public notice.<sup>32/</sup> This enforcement policy statement indicated that, in 1968 at least, the FTC did not intend to tolerate further more mergers of the P&G-Folger type. Unfortunately, it abandoned this policy in 1976 without explanation.

Accelerating Concentration in Food Retailing  
and the Destruction of Small Business

Another industry in which consumers and small business have a common interest at this time is food retailing. Between 1955 and 1964 large food chains acquired numerous food retailers, resulting in substantial increases in concentration. This merger activity by large chains virtually ceased after the Federal Trade Commission issued complaints challenging mergers by six leading food chains and after the Justice Department won the famous Von's-Shopping Bag case in the Supreme Court in 1966. Additionally, in January 1967 the FTC issued food distribution merger guidelines declaring

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<sup>32/</sup> FTC, Enforcement Policy with Respect to Product Extension Mergers in Grocery Products Manufacturing, May 15, 1968, p. 2.

that any but very small acquisitions by large chains (defined as chains with annual sales exceeding \$500 million) would be carefully scrutinized.<sup>33/</sup> The guidelines apply to both horizontal and market extension mergers (i.e., mergers between chains that operate in different metropolitan markets).

These various actions sent a clear signal to large chains that the Commission would probably challenge substantial market extension mergers by large chains as well as horizontal mergers that violated the standards of the Von's case. For a decade these actions had the effect of virtually stopping acquisitions by large chains (Table 2). Not all mergers were stopped, however, nor was this the FTC's intent. Indeed, total acquisitions of food retailers actually rose in subsequent years, but practically all (85 percent) acquisitions were made by retailers smaller than the top 20, by wholesale distributors, or by firms not involved in food wholesaling or retailing. Thus, a salutary effect of the FTC actions was to channel mergers away from the leading chains, thereby slowing the trend toward growing local and national concentration.

By the mid-1970s, the FTC was at a public policy crossroads. As its consent orders (which prohibited acquisitions without prior Commission approval) with leading chains began expiring, the industry waited for signals indicating the direction of future policy. The FTC was given ample opportunity to indicate its policy during 1975 and 1976, when five substantial mergers occurred.

Time does not permit recounting in detail subsequent events. (I have placed in an appendix to my testimony several pages in which these events were discussed before the Joint Economic Committee.) Suffice to

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<sup>33/</sup> United States v. Von's Grocery Co., 384 U.S. 270 (1966).

Table 2 - Acquisitions of Food Retailers, 1949 to 1975  
(Millions of Dollars)

Year	By All Acquirers		By 20 Leading Food Chains <sup>d/</sup>			By 10 Leading Food Chains <sup>d/</sup>		
	Number of Acquisitions	Sales of Acquired	Number of Acquisitions	Sales of Acquired	Percent of Total Acquired Sales	Number of Acquisitions	Sales of Acquired	Percent of Total Acquired Sales
1949	5	\$ 66	1	\$ 47	71%	1	\$ 47	71%
1950	5	4	2	3	75	1	1	25
1951	12	28	6	25	89	5	19	68
1952	10	71	5	55	77	4	53	75
1953	13	88	4	77	88	2	61	69
1954	24	76	7	37	50	4	31	41
1955	55	559	23	465	83	15	267	48
1956	69	450	32	310	69	20	141	31
1957	52	319	20	194	61	14	170	53
1958	74	517	41	361	70	27	261	50
1959	63	319	34	136	43	14	24	8
1960	44	307	25	201	65	10	36	12
1961	50	518	30	407	79	16	292	56
1962	53	306	24	179	58	14	157	51
1963	51	568	27	463	82	16	416	73
1964	41	312	16	188	60	8	153	49
1965	28	558	5	61	11	3	35	6
1966	40	539	6	110	20	3	73	14
1967 <sup>a/</sup>	33	1,350	3	21	2	0	0	0
1968	51	1,155	12	314 <sup>e/</sup>	27 (12) <sup>f/</sup>	6	199 <sup>e/</sup>	17(2) <sup>f/</sup>
1969	45	715	14	41	8	6	13	3
1970	36	688	9	74	11	5	22	3
1971	27	435	2	28	6	2	28	6
1972	59	1,069 <sup>b/</sup>	6	242	20	1	3	<sup>c/</sup>
1973	27	206 <sup>b/</sup>	13	29 <sup>b/</sup>	14	3	11	5
1974	18	1,591 <sup>b/</sup>	4	30	2	3	14	1
1975 <sup>g/</sup>	29	255	5	99	39	3	84	35
Total	1,014	\$12,879	376	\$4,197	32%	206	\$2,611	20%

<sup>a/</sup> The FTC merger notification program did not require reports from food distributors until June of 1967.

<sup>b/</sup> Sales data not available for one firm in this category.

<sup>c/</sup> Less than 1 percent.

<sup>d/</sup> For 1949-1966, data are for largest chains of 1963. Subsequent data are for the largest chains of 1975.

<sup>e/</sup> Includes Lucky's acquisition of Eagle Stores, with estimated sales of \$175 million.

<sup>f/</sup> Percent excluding Lucky's acquisition of Eagle Stores, which was approved by the FTC.

<sup>g/</sup> Data for 1975 are not complete since pre-merger notification data were available only for the first months of 1975.

Source: Marion, Mueller, Cotterill, Geithman, and Schmelzer, The Profit and Price Performance of Leading Food Chains, 1970-74, a Study Prepared for the Use of the Joint Economic Committee of the Congress of the United States, April 12, 1977.

say that during 1975 and 1976 the FTC took a number of actions that suggested an end to its aggressive enforcement policy of the 1960s, both with respect to horizontal and market extension mergers. For example, in 1976, shortly after the expiration of its 10-year consent decree restricting further acquisitions without prior Commission approval, Winn-Dixie (1977 sales of \$4.4 billion) acquired Kimbell Stores, which had annual sales exceeding \$500 million. This acquisition was over twice as large as any market extension merger challenged in food retailing during the 1950s or 1960s. The FTC's failure to challenge this merger led many chains to infer that the Commission had abandoned its previous policy. As Supermarket News interpreted it, the "FTC looked the other way when Winn-Dixie swallowed Kimbell, Inc."<sup>34/</sup>

Other large chains recently announced they too intend to make acquisitions. Lucky Stores (1977 sales of \$3.9 billion) announced that when its consent decree terminates it also intends to resume making acquisitions. And just last month, the President of Grand Union (1977 sales of \$1.6 billion), which is owned by the large British conglomerate, Cavenham, Ltd., announced that it planned to hit the acquisition trail. Finally, in April, Jewel Companies (1977 sales of \$3.3 billion) announced an agreement to merge with Skaggs Companies, a western food and drug chain with sales exceeding \$900 million. If consummated, this merger will be the largest ever in food retailing. Significantly, it will involve both horizontal and market extension aspects.

This unchecked merger spree poses a serious threat to competition and to small businesses. Studies done with my research associates indicate

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<sup>34/</sup> Supermarket News, May 24, 1976, p. 12.

that not only do horizontal mergers increase concentration in metropolitan areas, but market extension mergers also tend to increase market concentration.<sup>35/</sup> This occurs because large food chains, which possess conglomerate power because they operate across many markets, tend to increase concentration in the same way as that described earlier in the case of P&G. When a large chain enters a market by acquiring an established retailer, it can subsidize its subsequent expansion with profits earned in other markets. This, in turn, often triggers established large chains in the market to respond by cutting prices and/or increasing advertising. Caught in the middle of the ensuing escalating competitive warfare are the independent and small chain retailers whose success and survival depend on how they fare in a single market.

Given this Committee's historic interest in preserving competition in food retailing, I urge it to examine closely the antitrust agencies' recent failure to enforce Section 7 in food retailing consistent with the Supreme Court's decision in Von's, the FTC's decision in National Tea,<sup>36/</sup> and the FTC's food distribution merger enforcement policy guidelines of 1967.<sup>37/</sup>

These matters are important to consumers as well as to small business. In a study prepared for the Joint Economic Committee, my colleagues and I found that the prices of large food chains are significantly higher in

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<sup>35/</sup> Marion, Mueller, Cotterill, Geithman, and Schmelzer, The Profit and Price Performance of Food Chains, 1970-1974, a Study prepared for the use of the Joint Economic Committee of the Congress of the United States, pp. 19, 122-125, and forthcoming study.

<sup>36/</sup> Commission Decision in the Matter of National Tea Co., FTC Docket No. 7453, March 3, 1966.

<sup>37/</sup> FTC, Enforcement Policy with Respect to Mergers in the Food Distribution Industries, January 3, 1967.

very concentrated markets, especially when they are dominated by one or two large chains. For example, after adjusting for other factors, during 1970-1974 large food chain prices were about 5 percent higher in metropolitan areas where four chains controlled 70 percent of sales than in those where four chains controlled 40 percent of sales.<sup>38/</sup> Prices of a dominant chain in such highly concentrated markets tended to be even higher. Thus, consumers have a big stake in the growing concentration in food retailing. Whereas in 1954 the top four retailers in each market controlled 60 percent or more of the sales in only 5 percent of all metropolitan areas, by 1972 the top four held 60 percent of the market in 25 percent of all markets; moreover, this trend toward higher concentration has continued since 1972.

Smaller retailers also are affected by these developments because they often are disadvantaged in markets dominated by a few chains. They have trouble getting preferred store sites--especially in shopping centers--and are likely to be caught in periodic massive advertising battles and other kinds of nonprice rivalry as the large chains struggle for market position. Large chains, from time to time, also have engaged in selective geographic price discrimination, even within a city, to retard expansion of existing firms or entry of new ones.

All of the above practices can be anticompetitive. The American antitrust agencies have done nothing in these areas in recent years except to challenge some restrictive lease arrangements. Perhaps, they should take a lesson from our Canadian neighbor, which in recent years has become more aggressive in dealing with various types of predatory behavior in food retailing. In 1973 the Attorney General of Canada initiated an

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<sup>38/</sup> Marion, op. cit., p. 3.

antitrust action under the Canadian Combines Act challenging Canada Safeway Limited for alleged "actions directed toward its competitors which limited the expansion of its competitors and created barriers to entry of other competitors to the market."<sup>39/</sup> One provision of a consent order in the case provides that for a period of six years,

The Defendant shall not knowingly charge a price for any grocery item in any one or more of its stores in Calgary for the purpose of meeting or undercutting the price of a competitor, unless the price so charged by the Defendant is applied uniformly and simultaneously by it, for the identical grocery item in all of its Calgary grocery stores.<sup>40/</sup>

The order also recognized that entry barriers and a new entrant's costs can be raised by massive advertising. Another provision of the decree prohibited "Safeway for five (5) years from engaging in market saturating advertising policies."<sup>41/</sup>

Selective price cutting and massive advertising that injures rivals and discourages entry also probably violate the Robinson-Patman Act, the Federal Trade Commission Act, and perhaps even the Sherman Act. If so, the antitrust agencies should challenge such practices. If these practices cannot be challenged under existing laws, the Congress should consider strengthening them. Indeed, I believe the FTC should consider issuing trade regulation rules regarding all or some of the above-mentioned practices. High officials of the "new" FTC have announced their intention to enhance their enforcement impact by promulgating trade regulation rules prohibiting restraints of trade as well as unfair and deceptive advertising.

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<sup>39/</sup> Statement by the judge in summarizing the prohibitions contained in a consent order in Regina v. Canada Safeway Limited, Alberta, Canada, October 5, 1973, as reported in the Antitrust Bulletin, Volume XIX, No. 1, Spring 1974, p. 61.

<sup>40/</sup> Ibid., p. 63.

<sup>41/</sup> Ibid., p. 63.

I hope this committee agrees that strict enforcement of the antitrust laws in this area is essential and that trade regulation rules should be seriously examined as a means of curbing discriminatory and predatory practices in this and other industries.

In conclusion, vigorous antitrust enforcement continues to be essential to create an environment in which all business is given a fair opportunity to compete. I am sure Professor Galbraith, despite his many reservations concerning antitrust, will agree that every business--small or large--has a right to expect the enforcement of legal rules necessary to insure such an environment.



## APPENDIX

Excerpt from Testimony of  
Bruce W. Marion and Willard F. Mueller  
before Joint Economic Committee,  
Congress of the United States,  
March 30, 1977

*Merger policy*

In the 1960's, the Federal Trade Commission entered agreements with six food chains prohibiting future grocery store mergers for 10 years without prior FTC approval.<sup>6</sup> Additionally, in January 1967 the FTC issued its food distribution merger guidelines which said that any but very small acquisitions by large chains (defined as chains with annual sales exceeding \$500 million) would be carefully scrutinized. The guidelines applied to both horizontal mergers (those between direct competitors) and market extension mergers (i.e., between chains that operated in different metropolitan areas).

These various actions sent a clear signal to large chains that the Commission would probably challenge any substantial market extension mergers by large chains as well as horizontal mergers that violated the standards established by the Supreme Court in its 1966 decision in the *Von's Grocery Co.* case.<sup>7</sup> For a decade these actions had the effect of virtually stopping acquisitions by large chains (see Table 5). Not all mergers were stopped nor was this the FTC's intent. Although *total* acquisitions of food retailers rose in subsequent years, practically all (85 percent) acquisitions were made by retailers smaller than the top 20, by wholesale distributors, or by nonfood conglomerate firms. Thus, a salutary effect of the FTC actions was to channel mergers away from the industry leaders, thereby slowing the trend toward growing national concentration.

By the mid-1970's, the FTC was at a public policy crossroads. As its consent orders with leading chains began expiring, the industry waited for signals indicating the direction of future policy. The FTC was given ample opportunity to act during 1975 and 1976, when five substantial mergers occurred.

<sup>6</sup> Consent orders involved Grand Union (1965 and 1968); National Tea (1966); Winn Dixie (1966); Consolidated Foods (1968); H. C. Bohack (1968). An Affidavit of Voluntary Compliance was entered with Lucky Stores in 1968.

<sup>7</sup> *United States v. Von's Grocery Co.*, 384 U.S. 270 (1966).

In 1975, Lucky Stores requested premerger clearance of its proposed acquisition of Arden-Mayfair's grocery stores in Seattle and Tacoma. This horizontal merger, which involved sales of \$10 million, increased Lucky's market share in both markets. The FTC approved Lucky's request and the merger was consummated.

In 1976, shortly after its 10-year consent decree restricting acquisitions expired, Winn Dixie expanded into the southwest by acquiring Kimbell Stores headquartered in Texas. This market extension merger was the largest acquisition in Winn Dixie's history.<sup>19</sup> Kimbell operated 135 food stores and a wholesale division serving 1,500 independents in the southeast. Its total sales exceeded \$500 million in 1975.<sup>20</sup>

Allied Supermarkets' purchase in 1976 of Great Scott Supermarkets reportedly tripled Allied's share of the Detroit market—from 8 percent to over 20 percent, making Allied the market leader.<sup>21</sup> The top four chains held 50 percent of the Detroit market in 1972. Allied, the acquiring chain, reportedly had financial difficulties prior to the merger.

A&P purchased 62 National Tea Co. stores in Chicago in 1976. This merger increased A&P's share in this market from about 4 percent to 11 percent, making it the second or third largest chain in the market.

In early 1976 two regional North Carolina chains—Food Town and Lowe's Food Stores—announced their intention to merge. In 1975 Food Town had sales of \$130 million and Lowe's had sales of \$76 million. The two chains were actual competitors in several markets and potential competitors in others.

The only merger challenged during 1975-1976 was the Food Town-Lowe's merger. Following this challenge, the FTC won a temporary restraining order by the Court of Appeals, after which the chains abandoned the merger.

The failure of the FTC to challenge other mergers, especially the horizontal merger involving Lucky and Mayfair and the market extension merger involving Winn Dixie and Kimbell, evidently has led some large chains to infer that the FTC has abandoned the policy adopted in the 1960s. As Supermarket News put it, the "FTC looked the other way when Winn-Dixie swallowed Kimbell, Inc."<sup>22</sup> In recent months, both Lucky Stores and Grand Union have announced that they intend to resume making acquisitions.<sup>23</sup> Other chains apparently are unclear as to the FTC policy.

Based on our analysis of the impact of market extension mergers by large food chains, we believe abandonment of the FTC's past policy will result in further centralization of food retailing in local and national markets. Prior to initiating a strict policy toward market extension mergers in the mid-1960s, the top 20 chains acquired 55 chains with combined sales of \$2.1 billion. These mergers were largely responsible for these chains' increased share of food store sales between 1948 and 1964.<sup>24</sup> Our analysis strongly suggests that when a large food chain or large nonfood firm makes a market extension merger an increase in concentration in the market involved can be expected. Thus, there is persuasive evidence that competition in food retailing will be injured if the FTC abandons the policy toward market extension mergers adopted in the 1960s. Additionally, our analysis warrants extending this policy to acquisitions of food retailers by large, powerful firms not engaged in food retailing.

Since the Supreme Court's 1965 decision in *Von's*,<sup>25</sup> both antitrust agencies have pursued a relatively strict line on horizontal mergers. However, during 1975-1976, they permitted three substantial horizontal mergers by large companies (Lucky, Allied, and A&P). Each of these acquisitions was made by one of the nation's largest food chains and resulted in greater combined market shares

<sup>19</sup> Supermarket News, January 3, 1977, p. 16.

<sup>20</sup> Supermarket News, May 19, 1976, p. 26.

<sup>21</sup> Supermarket News, May 24, 1976, p. 12.

<sup>22</sup> *Ibid.*

<sup>23</sup> The president of Lucky was quoted as saying that the FTC's failure to challenge recent acquisitions "gives us the idea that the FTC will look more kindly on acquisitions." Supermarket News, November 22, 1976, p. 1. He reportedly stated Lucky would accelerate acquisitions shortly after its consent agreement expires in late 1977. *Ibid.*

<sup>24</sup> Federal Trade Commission Staff Report, "Structure and Competitive Behavior of Food Retailing," January 1966, pp. 164-167.

<sup>25</sup> In addition to the FTC's *Food Town-Lowe's* case, the Department of Justice in 1974 challenged the acquisition by Albertson's, Boise, Idaho, of Mountain States Wholesale Co., also of Boise. This case was recently settled with a consent decree requiring Albertson to divest Mountain States and to refrain for five years from acquiring any grocery wholesalers in Idaho or Eastern Oregon without prior approval.

than those in the *Von's-Shopping Bag* case.<sup>17</sup> In addition, four-firm concentration was much higher in each of these cities than in *Von's*.<sup>18</sup>

Time permits examination of only one of these mergers in some detail, Lucky's acquisition of Arden-Mayfair in 1975. The failure to challenge this acquisition is particularly significant because Lucky had previously signed an "Assurance of Voluntary Compliance" (AVC No. 895) in connection with another matter which requires Lucky to secure Commission approval prior to acquiring food stores. By permitting the merger in 1975 the Commission gave explicit approval of a merger of this type, thereby providing precedent for the large horizontal mergers made by Allied and A&P in 1976.

The salient facts are these. With sales of \$2.9 billion, Lucky was the fourth largest food retailer in 1974, and with sales of \$649 million Arden-Mayfair was the 20th largest food retailer. Lucky and Arden-Mayfair each operated stores with annual sales of about \$33 million in the Seattle metropolitan area,<sup>19</sup> resulting in a combined share of about 10 percent.<sup>20</sup> The combined shares in the Tacoma market appeared to be somewhat higher.<sup>20a</sup>

Based on its analysis of the probable competitive effects, the Commission staff recommended that the proposed acquisition not be approved. But, according to then FTC chairman, Louis A. Engman, "The Commission after careful consideration, approved the acquisition, with Commissioner Hanford dissenting."<sup>21</sup> Engman stated that important in the Commission's decision was "the distinct possibility that Lucky and Arden-Mayfair would leave the Seattle and Tacoma markets if the acquisition was not permitted." Arden-Mayfair, whose Seattle-Tacoma operation allegedly had suffered a loss in the first quarter of 1975, told the Commission it was withdrawing from these markets. Lucky informed the Commission it also would leave the market "because of below-normal profits unless it could strengthen its operation by the proposed acquisition."<sup>22</sup> Engman stated that "departure of Lucky and Arden-Mayfair would likely result in Safeway becoming more entrenched. Therefore, although the acquisition would combine the operations of two competitors, disapproval of the proposal could have a very substantial adverse effect on the state of competition in the relevant markets."<sup>23</sup>

The Commission's justification for its action was questionable at best. The merger made Lucky the second largest chain in both Seattle and Tacoma; in each market the top four firms made 49 percent of sales. Although the merger may well have improved Lucky's profit and growth prospects, this is not sufficient public policy grounds for approving the merger. It is incorrect to infer that what is good for Lucky is good for competition. Insofar as the merger improved Lucky's position vis-a-vis Safeway, it presumably also improved its position vis-a-vis smaller retailers. Indeed, by permitting the merger the Commission may have fostered the emergence of two dominant firms instead of one, as well as contributing to an increase in four-firm concentration. Our economic analysis indicates that under these circumstances consumers in these markets are likely to pay higher prices.

Many independent retailers in the Seattle and Tacoma market expressed fears that FTC approval would result in adverse competitive effects. Mr. F. N. McCowan, Executive Director of the Washington State Food Dealers Association, which represents about 1,000 retail grocers in the State of Washington, told the FTC that after the merger: "the market would be controlled by three chains [Safeway, Lucky, and Albertson's]."<sup>24</sup>

Mr. Morrie Olson, owner of a number of small stores in Seattle urged the Commission to "withhold" its approval because:

"The monopoly resulting from this transaction would intensify the growth and dominance of these three chains in the Seattle area, as well as enabling them to

<sup>17</sup> In *Von's*, the merging retailers had a combined market share of only 9 percent of the Los Angeles market. In 1968 the FTC disapproved a proposed merger where the acquiring company's market share was 18 percent and the proposed acquired retailer operated three supermarkets with about 1.5 percent of the market. Federal Trade Commission, advisory Opinion Digest No. 214.

<sup>18</sup> In 1978 the top four firms had only 24.4 percent of the Los Angeles market.

<sup>19</sup> Letter from Lewis A. Engman, Chairman of the Federal Trade Commission to Congressman Edward Mezvinsky, December 30, 1975.

<sup>20</sup> This is an estimate. Metro Markets estimates the shares of Lucky and Arden-Mayfair as 6.1 percent and 4.7 percent, respectively.

<sup>20a</sup> Metro Markets estimates the respective shares as 12.8 percent and 2.6 percent.

<sup>21</sup> Engman, *op. cit.*

<sup>22</sup> *Ibid.*

<sup>23</sup> *Ibid.* Emphasis added.

<sup>24</sup> Letter from F. N. McCowan to FTC, May 21, 1975. The FTC requested public comment on the proposed merger. Four grocery retailers, a food wholesaler, and the executive director of a retail grocery association opposed the merger. (The retailers operated from two to ten stores each.) Two Mayfair stockholders wrote in favor of the merger.

expand this dominant control into the outlying communities of western Washington".<sup>25</sup>

Mr. Richard C. Rhodes, owner-operator of three supermarkets observed the irony that Lucky and Mayfair "got their start" in the market by acquiring successful small businesses but were now asking to merge with one another rather than giving small businessmen a chance to buy Mayfair's stores. He wrote:

"It is interesting that Lucky and Mayfair got their start in this market through acquisition of successful small companies who couldn't turn down the lucrative offers made by these two chains.

"The independent retailers' position is not being jeopardized because of his skill or ability to compete price-wise or management-wise, but because of the lack of opportunity for growth. If the opportunity to purchase the Mayfair stores were presented to the independent grocers, I doubt that Mayfair would have difficulty in disposing of their stores—providing the price was fair".<sup>26</sup>

Since neither Lucky nor Mayfair were failing firms, they could not rely on the failing company doctrine. And while Mayfair-Arden evidently was intent on leaving this market, Lucky merely threatened to do so (unless the Commission permitted the merger) because it was earning "below normal profits."

In rejecting its staff view that the merger not be permitted, the Commission traded off lower market concentration and the probable increased competitive viability of several small chains (that would have purchased the Mayfair-Arden stores) for increased four-firm concentration and the hope that increasing Lucky's market share would increase competition. This was a dubious trade-off. It was based on the assumption that competition is more likely to be enhanced by a merger leading to a market dominated by two or three chains than a merger that would lessen concentration and strengthen the competitive position of a number of small chains. We believe that not only did the Commission's decision have an adverse effect on the Seattle and Tacoma markets, but that it set an unfortunate precedent for other mergers, specifically the two large horizontal mergers permitted by the FTC in 1976 (Allied and A&P).

In sum, we believe the Commission should not abandon the merger policies it pursued in the 1960s. With respect to horizontal mergers it should enforce the law as strictly as enunciated by the Supreme Court in its *Von's* decision. With respect to market extension mergers, it should not abandon the policy expressed in the *National Tea* decision<sup>27</sup> and FTC's 1967 food distribution guidelines, which state:

"... whereas mergers by retail firms with annual sales in excess of \$500 million may contribute to further concentration of buying power, in addition to any adverse effect that they may have at the retail selling level, it is unlikely that the prohibition of mergers by such companies would have an adverse effect on efficiency. Moreover, insofar as economies of scale require fairly large scale operations, the goal of promoting efficiency might be better achieved by channeling mergers away from the largest firms to those whose efficiency would be enhanced by further growth."<sup>28</sup>

<sup>25</sup> Letter from Norrie Olson to FTC, May 15, 1975.

<sup>26</sup> Letter from Richard C. Rhodes to FTC, May 19, 1975.

<sup>27</sup> FTC Opinion Docket No. 7453, *National Tea Co.*, March 4, 1966.

<sup>28</sup> FTC, "Enforcement Policy with Respect to Mergers in the Food Distribution Industries," January 3, 1967.