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**DIRECT SELLING OF FRESH VEGETABLES
IN THREE OVERSEAS COUNTRIES**

by I.J. Bourke

SEPTEMBER 1971
NEW ZEALAND

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September 1971

Occasional Paper No.3
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PREFACE

This Report is the second of two publications by Mr Bourke on the marketing of fresh vegetables directly from grower to retailer. The first publication reported on the results of a survey on the practice of direct selling in New Zealand.^{1/}

This Report describes the systems of direct selling used in some overseas countries and evaluates their impact on overseas growers. The sources of information were published material and correspondence with overseas authorities.

The important conclusion that can be drawn from this Report is that there is very little evidence to support the contention that overseas growers have suffered financially as a result of direct selling. There is evidence that the growers' financial position relative to the rest of his society has deteriorated and that this deterioration has proceeded concurrently with the growth of direct selling. However, a decline in the real incomes of agricultural and horticultural producers is a trend which is largely explained by general economic forces. It is quite incorrect to attribute this decline to the growth of direct selling.

However, it should be emphasised that there has been very little overseas work which has attempted to isolate the financial impact of direct selling on growers. Indeed, it would be very difficult to obtain reliable information on

1. Bourke, I.J., The Direct Buying of Fresh Vegetables in New Zealand - A Survey, Occasional Paper No.2, Department of Agricultural Economics and Farm Management, Massey University, February, 1971.

this question. Nevertheless, this Report does give a considerable amount of factual information on the nature and extent of direct selling in some overseas countries. Such information provides useful background material for discussions on direct selling in New Zealand.

The work on which both this Report and the earlier publication is based was supported financially by the New Zealand Vegetable and Produce Growers' Federation (Inc). We gratefully acknowledge this support.

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September 1971.

SUMMARY AND CONCLUSIONS

Although overseas experience has been used as evidence of the major detrimental effects of direct selling nothing was found to support these views in authoritative publications or from correspondence with overseas marketing experts. This is not to say that the practice has had no effect on the grower, but that the effect is only minor. No definite evidence was found of growers having suffered financially as a result of direct selling. It is likely that factors such as price decline due to excessive total supply, increasing costs, and the general economic pressures on the small unit are the main contributors - not direct selling.

The extent of the practice would also appear to have been exaggerated. An estimate for the United Kingdom placed the level at 8 percent of total produce sold direct in 1967, while it is suggested that the maximum level likely to be achieved in the U.S.A. will be 40 percent. The New Zealand level has been estimated to be less than 5 percent. (See Massey University Occasional Paper No.2).

Direct selling has progressed much further in the U.S.A. than in any other country due to the size of its production units and the prevalence of large retail outlets. It is also here that direct selling is said to have shown major problems. Published studies do not support this view, and personal correspondence refuted it. Some of the "evidence" would seem to have been quoted out of context. Moreover, direct extension to the New Zealand situation is not valid since certain factors contributing to the features of the marketing system in the U.S.A. are not

present in this country.

No doubt, one factor which could be regarded as restricting the large retailer's bargaining power is the existence of cooperatives (both bargaining and general) marketing the produce of a number of growers. Here again the wrong conclusions have often been drawn - the main bargaining cooperatives, said to be evidence of the growers' need to achieve strength in bargaining, exist in the processing field - not the fresh market field.

Cooperatives of a more general nature are used in many sectors of overseas countries, and in addition to their functions of bulk buying of supplies for the grower, and carrying out packing and grading activities, they may also assist in price arrangement. It must be realised though, that cooperation need not be solely to offset the retailers' bargaining power, and therefore the presence of cooperatives cannot be taken as a priori evidence that the grower has resorted to them as a defensive mechanism.

From the experience of the overseas countries studied, the following points may be made about the future effects of direct selling in New Zealand:

- (1) Based on the available evidence there is nothing to support the view that direct selling is likely to be a major contributor to the New Zealand growers' troubles. Other factors such as excessive supply, and the general economic pressures favoring the larger production unit are probably more important.
- (2) Future growth in direct selling will be dependent on the growth of large scale retail outlets; the share of the fresh vegetable trade they acquire; the availability of growers capable and willing to meet the requirements of these retailers; and the extent to which existing channels adapt to the needs of the large buyer.
- (3) While direct selling does not deserve the main accusations laid against it, major growth in the practice could result in the

grower being placed in an inferior bargaining position, but the relative positions in bargaining will depend on the availability of alternative supply outlets and the total supply position at any particular time.

(4) An increase in decentralised marketing (i.e. outside central markets) results in price establishment becoming less obvious, and it is because of this, that growers become less effective in bargaining. To overcome this market intelligence is required.

Therefore, if growth in direct selling does occur in N.Z., growers could need to introduce a greatly improved system of market intelligence. This is not to suggest, however, that this growth will occur.

(5) To enable such an intelligence system to function effectively an improved grading system would also become necessary.

(6) If direct selling does expand considerably above present levels some form of coordination would be an effective method of improving the growers' bargaining position. This would allow the small grower to achieve levels of negotiating strength similar to those likely to be held by a large grower.

DIRECT SELLING OF FRESH VEGETABLES

IN THREE OVERSEAS COUNTRIES

I. INTRODUCTION

The method of marketing fresh vegetables by which produce is sold directly from grower to retailer has been strongly opposed in New Zealand, both by individual growers and the New Zealand Vegetable and Produce Growers' Federation.

The major arguments against direct selling are :

- (a) the domination of growers by the large retailers in the bargaining process, due to lack of negotiating strength;
- (b) an auction system at which competition is reduced; and, resulting from this -
- (c) a decline in the price received by all growers for their produce.

This opposition is based primarily on New Zealand growers' beliefs concerning the impact direct selling has had on growers in other countries.^{1/}

This paper describes the direct selling of fresh vegetables in three overseas countries - the United Kingdom, the United States of America and West Germany. These are three countries where direct selling has been stated to be a problem.^{2/}

-
1. See, for example, "Some Dangers - But What Other Choice?", New Zealand Commercial Grower 25 (8): 1, January, 1970.
 2. Australia has been quoted as a source of evidence concerning the negative effects of direct selling. However, insufficient information could be obtained to justify its inclusion in the investigation.

This paper represents one part of a broader study into direct selling.^{3/} The information given is based on published material and correspondence with overseas authorities on fresh vegetable marketing.

The discussion falls into two parts; firstly, a discussion of trends in direct selling and the effects on growers; and then investigation of the measures taken by growers in the three countries to improve their bargaining position in relation to the buyers of their products.

3. Bourke, I.J., An Economic Investigation into the Direct Selling of Fresh Vegetables in New Zealand, Unpublished M.Ag.Sc. Thesis, Massey University, December 1969.

II. TRENDS IN DIRECT SELLING AND THE IMPACT ON GROWERS

(A) UNITED STATES OF AMERICA (U.S.A.)

Prior to World War II, most fresh produce sold in the U.S.A. was sent to terminal markets in the consuming areas where it was sold by auction or private treaty - mainly the latter, since auction has never been a common method of selling vegetables. Since World War II there has been a strong move to direct buying. Direct buying in the U.S.A. refers to purchase by the retailer or his agent at shipping points, or purchase from the grower himself. The predominant channel is from the shipping point. Growers deliver produce to these shipping points where firms known as shippers take it over, grade, pack and sell it. This produce is distributed both locally and nationally.

Despite this growth in direct buying, a majority of produce sold at the shipping points is bought by wholesalers, not retailers, although their share declined considerably between 1948 and 1963. (See Table 1).

Although this purchase from shipping points rather than from the grower represents an important difference between direct buying in the U.S.A. and New Zealand, the same arguments may be levelled against it. Sale to the shippers may result in the grower lacking bargaining power in price negotiation and also contribute to produce by-passing the auction system.

It may therefore be seen that the arguments used against direct buying in New Zealand relate to the quantity of produce by-passing the central markets, not just the quantity bought by the retailer. It is however the retailer - and the large retailer at that - who buys directly, and therefore the quantity by-passing auction in N.Z. is likely to be primarily accounted for by these.

TABLE I: PERCENTAGE DISTRIBUTION OF FRESH FRUIT
AND VEGETABLE ASSEMBLER SALES, BY KIND
OF BUYER

<u>KIND OF BUYER</u>	<u>YEAR</u>			
	1948 %	1954 %	1958 %	1963 %
Industrial, commercial	5.1	8.8	11.9	9.8
Consumers, farmers	2.9	2.6	3.0	1.9
Retailers	10.9	15.6	26.5	28.2
Wholesalers	80.5	70.1	55.9	57.0
Export	0.6	1.9	2.7	3.1
Federal Government		1.0		
	100.0	100.0	100.0	100.0

Source : National Commission on Food Marketing (N.C.F.M.),
Technical Study No.4, Table 3-29, p.92.

The Large Retailer and Direct Buying

The practice of direct buying in the U.S.A. dates back to the early 1920's. It began initially with national chain stores, and was quickly taken up by regional and local chains. Considerable evidence exists to indicate that direct purchase is of more interest to large retailers than to the smaller firms. This is because of the greater distance between the growing areas and the large stores located in the cities, and the fact that large firms are more able to support their own buyers in these markets. Direct buying is easier if purchase can be made in car-lots, thus favouring the large firm.

If the buyer's needs for a commodity are large relative to supplies available on local markets, the cost of inspecting many small lots and purchasing those of similar quality will be substantially higher than by purchasing a large quantity direct.

Views on direct buying and future trends were presented in a detailed study on vegetable marketing done in 1964. Although rather dated its predictions are of interest :

"Obviously, the controlling factor in the expansion of direct purchasing is the share of the total fruit and vegetable market controlled by chains - corporate, voluntary, and cooperative - which are large enough to buy economically direct from shipping points. To some extent the decision of expanding organisations to go into direct buying and how far to go into it, will be conditioned by the performance of the terminal markets. If adequate supplies of produce are available at competitive prices on the terminal markets, the incentive for smaller groups to buy directly will be much less.

While there is no basis on which to predict the precise nature of the structure of food retailing in the years ahead, a projection of the changes of the past thirty years seems to indicate further growth of buying groups of all types which are big enough to buy directly from the shipping point if they wish to do so. The outside limits of such growth seem to be set by the needs of at least three groups:

- (1) restaurants, hotels and institutions;
- (2) unaffiliated independent grocery stores; and
- (3) chains making some local purchases. A conservative estimate might be for direct buying to increase from a fifth to something like a third of total sales in the next 10 to 15 years". (1974-1979).^{4/}

This would take the time to 1974 or 1979 - that is about one third of total sales in the U.S.A. being bought directly by then. This situation would be dependent on the growth of large retail buyers. In fact, by 1967 supermarkets had achieved 72 percent of total grocery stores sales, but a distinct slow-down in the growth of market share had occurred. (Fig.1).

Extent of Direct Selling

Despite the dominant position in the retail market held by large stores, and the prevalence of shippers, it is interesting to note the low percentage of total vegetables actually by-passing the wholesale markets. Prior to actual study of the wholesale markets in the U.S.A., it was believed that as much as 60 to 75 percent of fresh fruit and vegetables was by-passing the

4. A.C. Manchester, The Structure of Wholesale Produce Markets, Ag. Ec. Report No.45, U.S.D.A. 1964, p.viii.

FIG. 1

SHARE OF GROCERY STORE SALES BY SIZE OF STORE - U.S.A.

	Supermarkets	Superettes	Small Stores
1952	39%	22%	39%
1954	46	20	34
1956	52	19	29
1958	58	17	25
1960	65	15	20
1962	68	14	18
1964	70	13	17
1966	71	13	16
1967	72	13	15

Note: In 1967 a supermarket was defined as a store doing \$500,000 worth of business a year or more (previously \$375,000 or more); a superette as a store doing from \$150,000 to \$500,000 (previously \$75,000 to \$375,000); and a small store as doing less than \$150,000 (previously less than \$75,000).

Source: Allvine, F.C., "The Supermarket Challenged!", Business Horizons, Indiana Uni. Grad.School of Business, XI (5): 61, October, 1968.

traditional wholesale markets. On study in 1958 it was found that only 20 percent by-passed these markets as a result of direct buying. However, 50 percent of retail organisations' supplies came outside traditional wholesale markets. Within this figure national chains were obtaining 70 percent of their supplies direct from shipping points, regional chains 52 percent and local chains 28 percent, further reinforcing the view that it is the larger firms who show most interest in direct purchase.

It is important to note the distinction in the percentage figures relating to supplies by-passing the traditional wholesale channel - that is, that 20 percent of volume from shipping points by-passed central wholesale, but retailers as a group obtained 50 percent of their supplies direct from shipping point, and another 6 percent from local growers. Therefore, retailers obtained something like 56 percent outside the terminal wholesale system - but were the outlet for only 20 percent of what the shippers sold; the rest obviously went through normal channels or to such sources as institutions, the military etc.

In 1963, shippers sold 28 percent of their supplies direct to the retailer and 57 percent to wholesalers.^{5/}

Future Growth of Large Retail Outlets

The suggestion that the national chains would not obtain the same rate of increase in the market that they had previously achieved, and that growth of the medium sized chains would take

5. N.C.F.M. Tech. Study 4, op.cit., Table 3-29, p.92

place, was presented in 1966^{6/}, a view that is supported by a more recent statement, "The decline in the number of food stores over the past decade is expected to be reversed by a dramatic influx of convenience stores".^{7/}

Other forms of retail outlets, such as the discount store, superettes and convenience stores and food emporiums, appear to be providing stern competition for the supermarkets although these stores do not emphasise perishables in their operations. Manchester stated that specialty fruit and vegetable shops were growing in some areas and that they competed with supermarkets for produce business. Further, these stores were not in a position to buy much direct.

The present opinion held by Manchester and others is that direct purchases are not likely to exceed 40 percent of the total volume in the foreseeable future.

Effects of Direct Selling

None of the studies mentioned so far has indicated any effects of direct buying - they merely discuss its growth. A significant decline in the numbers of growers has occurred since early 1950, and increasing average size in vegetable farms is obvious. Whether or not this is an undesirable occurrence, however, is unknown. It is plausible to suggest that this type of move is part of the economic rationalisation process and should not therefore be halted. If it could be shown that it is only a result of power held by one sector, and no improvement is resulting, then attempts should be made to stop it.

6. N.C.F.M. Food Retailing, Tech. Study No.7, 1966, p.3.

7. U.S. Dept. Commerce, U.S. Industrial Outlook 1970, (Government Printing Office, Washington, 1969).

There is no evidence of the consequences of this trend with regard to the individual grower. It would be extremely difficult to determine what part of the blame for growers going out of production can be placed on direct selling, since this trend has taken place with all agricultural producers, regardless of whether or not direct selling has been a feature of their industry. Small growers will have been forced out for reasons other than the method of sale; for example, economies of size in production, low prices due to oversupply and shifts towards the use of vegetables in the processed form.

Evidence from other fields all tends to suggest that direct selling does not markedly affect growers' returns. A study on pigs considered direct marketing had not affected the price registering function of the auctions, nor caused interior market prices to be lower than if the increased in direct marketing had not taken place.^{8/}

The one publication coming out against direct selling is a Congressional report on food marketing.^{9/} This presents the usual arguments against direct trading - the difficulty of pricing, the lack of power held by the grower, the decline of auction, and the pressure on growers to become larger. No evidence is presented supporting these arguments, the conclusions having been drawn from the study on fruit and vegetables done for the Committee.^{10/}

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8. U.S.D.A., The Direct Marketing of Hogs, Bur.Ag.Econ. Misc. Publication No.222, March 1935.
 9. N.C.F.M. Food From Farmer to Consumer, (U.S.Government Printing Office, 1966).
 10. N.C.F.M. Tech. Study 4, op.cit.

This latter study discusses the organisation of the vegetable industry - both fresh and processed, but does not, however, draw many conclusions as to the effects of direct selling on the grower. Considerable discussion of shipping point trends and changes exist, but not particularly from the grower's viewpoint.

Features of competition at the shipping points - both between the shipper and the grower he buys from, and between the shipper and the buyer he sells to - are of interest to the grower since competition in the latter will affect the relation in the former.

Competition among the shippers for supplies takes the form of non-aggressive, non-price competition, since although the firms are trying to expand their supply source -

"....in the short run, shippers recognise the futility of engaging in aggressive price competition for a fixed supply of product. Such competition would raise product costs for all shippers without affecting immediate supply."^{11/}

The fact that small growers generally face large shippers, resulting in the grower being in the weaker position, is expressed:

"Short of integration, product quality and supply dependability are the only means for producers to ensure shipping point market outlets. However, these are necessary but not sufficient conditions for producer success. They are necessary to ensure the grower a market, but they cannot be relied upon to raise producer prices appreciably."^{12/}

Consequently the grower appears to be in a weak bargaining position.

11. Ibid., p.97

12. Ibid., p.98

For the sale of produce, shippers regard retailers as an important outlet. In selling to them, the shippers engage in aggressive service and quality competition and a form of non-aggressive price competition.

Since large retailers are considered to exert power when buying, it might be expected that the prices they pay shippers would be lower than those paid by smaller buyers. Evidence on this question is sparse, but one study compared the prices paid at shipping points by the large national chains and those paid by smaller non-chain firms, for tomatoes in the Lower Rio Grande Valley. In the price comparisons no significant difference was observed, the study concluding -

"... there seems to be no basis for maintaining that national chains pay either higher or lower prices than other buyers."^{13/}

Another study, this time on lettuce, investigated the claim by farmers that direct buying had reduced the number of competing buyers at shipping point markets, and that because of concentration of buying, buyers were able to use oligopsony power to depress prices and affect growers' incomes. The hypothesis that the three principal buyers paid lower prices than other smaller buyers, was tested by comparing the prices paid by the principal buyers with average market prices, the conclusion being that -

"... the hypothesis that the principal buyer paid a higher average price than the reported average market price was accepted."^{14/} (underlining mine).

13. Podany, J.C. & Farrish, R.C.P., Tomato Prices and Market Structure in the Lower Rio Grande Valley of Texas, U.S.D.A. Marketing Res-Report No.588, 1963; p.171.

14. Miklius, W. & De Loach, D.B., "Do Lettuce Buyers exert Oligopsony Power?", U.S.D.A. Ag. Econ. Res. 17: 101, October 1965.

It therefore appears that little evidence exists of major detrimental effects being attributable to direct selling despite the higher level existing in the U.S.A. In fact, comments received personally are worth quoting in full -

"... as a result of these studies (Manchester and N.C.F.M.), the discussion of the adverse effects of direct buying has declined sharply in recent years. We might even go so far as to say that it is now a dead issue."

And further, (in relation to the fears that prices decline as a result of direct buying by retailers) -

"Considerable evidence suggests that this has not been the case in U.S. produce markets."^{15/}

Summary

Data is, as always, extremely sparse except for two major studies, one published in 1964 in which data generally refers to 1958, and one published in 1966. These must be used for the bulk of material, and obviously changes will have occurred since then.

It has been shown, however, that direct buying is very different in the U.S.A. from what presently exists in New Zealand. Although the growers have similar difficulties - namely power problems when negotiating - the wholesale markets by-passed in the U.S.A. are not auctions, and about 50 percent of their business in 1958 was not with retailers. This suggests

15. Personal correspondence with J.K.Hanes, Agricultural Economist with the U.S.D.A., December, 1969.

This evidence mentioned refers to : Podany, J.C. & Farrish, R.O.P. op.cit.; Miklius, W. & De Loach, D.B. op.cit.; and unpublished work on potatoes in Maine and the Red Valley of Minnesota - North Dakota.

that a high proportion of their buyers would still be present on the wholesale markets.

In terms of quantities, 33 percent of shipping point sales by-passed the wholesale markets in 1963, a relatively minor amount, and it is estimated that a maximum level of 40 percent will be reached. However, about 50 percent of retailers' supplies were bought direct. The fear is decline of the wholesale market, but this appears to be still carrying out a significant amount of business and should give growers an adequate indication of prices.

Little evidence has been found to support the contention that the growers' position has been seriously affected by the growth of direct marketing in the works studied, and this has been further supported by personal correspondence. While growers may have had difficulty when negotiating with retailers or shippers, it seems the wholesale markets have remained reasonable alternative channels. Large growers able to meet the quantity and quality requirements of the large retailers have undoubtedly been in a preferred position to the small grower and, if growth of this method of sale continues, could remain so. But large retailers might be expected to prefer to buy the lines of large growers at the wholesale markets also - and it might be misleading to place all the blame on direct purchases.

Pricing has shifted, for much produce, to the shipping points where transactions are carried out by a number of diverse firms. This means that prices are not known as readily as under wholesale markets, but while it is to be expected that some detrimental effects may have been felt, there is little detailed evidence.

It appears that the wholesaling function has shifted

from the retail areas to the growing areas, and the retailer is not negotiating directly with the grower in many cases, but with the shipper. This is more akin to a situation where retailers in New Zealand arranged supplies through auction firms by private treaty, rather than bidding at auction.

Significant differences therefore exist in the marketing channels of U.S.A. and New Zealand, and in the main form of direct buying, but even given these differences there is little evidence that the U.S.A. grower has suffered greatly because of the practice.

(B) UNITED KINGDOM (U.K.)

In the United Kingdom, the fact that the production centres are generally within easy reach of the main consumption areas where the major wholesale markets are situated has meant that growers consign their produce to the markets, rather than to an intermediary such as a shipper as occurs in the U.S.A. In this respect the British method bears more similarity to New Zealand.

Direct buying is of importance, and bears certain similarities to the U.S.A. in respect of retailer purchases. Middlemen, known as distributing wholesalers, provide a service to retail outlets selling produce they have previously bought. These wholesalers would seem to be somewhat similar to shippers in the U.S., except that they are not located in the growing areas and they buy a majority of their supplies from the wholesale markets. It has been estimated that of all fresh fruit and vegetables reaching retailers, about 20 percent by value and 40 percent by volume is handled by distributing wholesalers who have dealt direct with growers. In total, it seems that

about 28 percent of the retailers' supplies come outside the markets - although most of this is via a middleman in a similar manner to U.S.A. shipper sales (See Table II).

As is shown, 72 percent is obtained through the markets, but unlike New Zealand (and like the U.S.A.) most produce is sold in these markets under private treaty rather than auction.

In relation to the proportion of total supply which bypasses the market and its effect on the functioning of the price mechanism, it has been stated that there is little consequence as long as about one quarter of total supply goes this way.^{16/} However, no evidence is given to substantiate this statement. This supports the generally recognised view that a certain level of patronage is needed for effective price establishment, but little is known of what level this is.

Retailing Fresh Produce

Retail outlets in the U.K. have followed similar trends to those in the U.S.A. - namely an increasing share of the total food business being done by the large supermarkets and chain stores. In the fresh fruit and vegetable field, sales by the main types of business in 1961 were as shown in Table III.

Thus 73 percent was sold through greengrocers and fruiterers. Further, an estimate puts the retail fresh fruit and vegetable sales by the large retailers at between 10-15 percent

16. Ellis, P.G. and Kirk, J.H., The Selling of Fruit and Vegetables: A Comparative Study of Commission Trading, Wye College Mktg. Series No.4, October 1968, p.31.

TABLE II SUMMARY OF THE RELATIVE IMPORTANCE OF SOURCES
OF SUPPLIES FOR THE RETAIL TRADE

<u>To Retailers:</u>	<u>Percent</u>
1. Direct from growers	8
2. From growers (and importers) and thence direct through distributing wholesalers	20
3. Through market	
(a) direct to retailers	38
(b) through distributing wholesalers	<u>34</u>
	<u>100</u>

Source : Ellis, P.G., Hunter, C.S., Kirk, J.H., The Distribution
of Fresh Fruit from Markets to Shops.

Note: No date is given for this data, but it probably refers
to 1967.

TABLE III FRESH FRUIT AND VEGETABLE SALES BY MAIN TYPE
OF BUSINESS, GREAT BRITAIN, 1961

<u>Type of Business</u>	<u>Percent</u>
Grocers and Provision Dealers	19.6
Greengrocers, fruiterers	72.9
Other food retailers	1.5
Non-food shops	<u>6.0</u>
Total	<u>100.0</u>

Source : Ellis, Hunter, Kirk, op.cit., Table B, p.33.

in 1969.^{17/} This suggests that the large retailers are not as important for the sale of fresh produce as generally thought. One source predicted in 1963 that by the end of 1976 supermarkets would be doing 50 percent of food shop sales, and 66 percent by 1981. And, further, that -

"The supermarkets' proportion of the British retail trade in fresh meat and greengroceries is likely in the long run to lag only slightly behind their share of the total food trade."^{18/}

- that is, slightly below 50 percent by 1976, 66 percent by 1981. The prediction for 1976 appears to be highly optimistic since, as mentioned, 15 percent has been calculated as the level existing in 1969.

It is suggested that in 1968 supermarkets were responsible for about 61 percent of all food sales. Thus the predictions given in 1963 appear to have been conservative for the percentage of total food sales, and highly optimistic for the share of fruit and vegetable sales done by the supermarkets. This is not to dispute the increasing share being taken by these large outlets - only the extent of its growth.

The view is held that the large retailer finds it more difficult to obtain produce through markets than the small retailer. To overcome this, they attempt to contract with growers and cooperatives, but "... the supermarkets have not found it easy to find growers willing to grow for them on

17. Personal correspondence with P.G.Ellis, Research Fellow, Wye College, (University of London), December 1969.

13 percent for vegetables and 15 percent for fruit is given in UNCTAD-GATT. The Fresh Fruit and Vegetable Markets in Seven European Countries, Geneva, 1968, Vol.1, p.275.

18. McClelland, W.G. Studies in Retailing, (Blackwell, 1964), p.54.

the contract system."^{19/} To overcome this, the supermarkets have attempted to get supplies from cooperatives, but the majority of these are not prepared to allow themselves to become dependent on the large retailer. Upper limits of 20 percent of total supplies sold by cooperatives to supermarkets have been suggested.

Effects of Direct Selling

Problems of negotiating price exist. Both parties use the market price as a guide and the party with the strongest bargaining position is able to achieve a premium at the expense of the other. However, it would seem that the grower is not at a great disadvantage since other alternative outlets exist and hence the large retailer is not in a dominant position.

No information has been found which either supports or disproves the usual arguments against direct selling, and in particular, none relating to the extent to which direct marketing has forced growers out of business by lowering their prices. It does appear that any decline in the prices or fall in the number of growers is more likely to be the result of general conditions in the industry rather than the marketing system.

Summary

Produce bypassing the central markets has been estimated at 28 percent by value, but only 8 percent of this as going directly from the grower to the retailer. This is well below the levels inferred by statements in N.Z. trade journals.

The percentage of the fresh fruit and vegetable sales handled by the large retailers in 1969 has been put at 10-15 percent, considerably below what was predicted a few years ago.

19. Ellis, P.G. "Wholesale and Retail Fruit and Vegetable Markets", Proceedings of the Twenty-first A.G.M. & Conference of the National Association of British Market Authorities, September 1969, p.59.

Contributing factors have been the problem of acquiring large quantities of suitable produce, and also difficulties in getting suitable personnel to run produce departments.

No doubt growth in the share of the fresh produce market controlled by these large firms, and expansion of direct purchases can be expected, but the small retailer will have the major share of the produce market for some time to come.

Growth of direct selling will, as usual, be related to the growth of large retailers and the extent to which they are able to increase their share of the total fruit and vegetable trade. It seems most likely that the large outlets will increase their share of trade, but growth of direct selling will also depend on their ability to induce suitable growers to supply them. Thus the growth of large growers or cooperative organisations will play an important part. If U.S.A. experience is followed sale by large retailers is not likely to go above the present level of 60-70 percent of total food sales. Therefore, while direct selling will expand, it should remain limited and not of the major significance that has been attributed to it in trade journals.

To quote:

"Although some estimates forecast a large increase in the total share of trade likely to be passing through supermarkets eventually, it is not thought that direct sales from grower to retailer are likely to rise to a level in the foreseeable future when they might challenge the traditional wholesale horticultural markets. Considerably more than half the fruit and vegetables sold in this country is expected to continue to pass through the markets. Buyers for supermarkets and chain stores

may well be attracted back to the wholesale markets when they are modernised and are handling standardised produce in greater volume; at present they are less inclined than other retailers to suffer the delays and inconveniences inevitably experienced in the older markets. When allowance is made for further increases in population and for such increases in per caput consumption as may result from rising standards of living, it is clear that the throughput of the wholesale horticultural markets as a whole should, even on unfavourable assumptions, maintain something like its present level for the next twenty or thirty years."^{20/}

(C) WEST GERMANY

West Germany has been selected because it appears to be one of the European countries exhibiting a significant degree of direct marketing.

Retailing trends

Again investigation is hindered by lack of data. However, the increase in self-service shops in Germany illustrates the important position these types of stores hold. The number of self-service shops rose from 17,000 in 1959 to 63,000 in 1966, a 270 percent increase.

20. O.E.C.D. Production of Fruit and Vegetables in C.E.C.D. Countries, United Kingdom and Ireland, (Paris, 1968)
Para.27, p.24.

That the importance of the large retailer has increased since that time is borne out by the statement -

"Retailing outlets of the calibre of supermarkets and chain stores are becoming of increasing importance, especially in the larger cities."^{21/}

Distribution

Briefly, the distribution of fruit and vegetables is generally producer/exporter to importer/wholesaler to retailer.

Auction selling predominates in the large consuming and producing area in the north-west, while being of lesser importance elsewhere. Home-grown produce is largely sold by auction, only about 25 percent of what passes through wholesalers' hands being sold on commission. Produce sold at these auctions is, however, largely sold to wholesalers, these merchants reselling later. Direct selling in West Germany may refer to three different situations - (a) many smaller growers have their own stalls in some wholesale markets and sell to retailers, wholesalers and consumers from these; (b) procurement from auction by the larger retailers has been called direct buying; and finally (c) the aspect this study is considering, namely, retailers arranging for growers to supply them is called direct buying. Obviously, with these variations, care must be taken to determine which is being spoken of when discussing direct marketing. A possible reason for regarding point (b) above as direct is that, in certain of the auctions, retailers are prohibited from buying - only wholesalers are able to do so.

21. UNCTAD-GATT, op.cit., p.135.

Effects of Direct Selling

Although no reliable statistics appear to be available on the importance of the different methods of selling, it has been stated that a great deal of direct selling takes place (both from producers' stands in wholesale markets and from the growers property to chains and supermarkets). However, most of the sales to large retailers are probably handled by the cooperatives. Once again no studies have been found on the effect on the grower of this direct selling, but it might be reasonable to suggest that their bargaining position has not been affected greatly since cooperative action exists as a balancing power.

An important difference between vegetable marketing in West Germany and other countries studied is the place of imported produce. West Germany is very dependent on imports (Table IV). In fact, over 50 percent of the fresh vegetables consumed is imported.

These imports are largely handled by brokers or agents, about 80 percent being done on commission, a much higher level than exists for locally produced produce.

An estimate of the clientele to which the importers sell is shown in Table V.

The preferred outlets are the wholesalers and integrated firms since the transactions are larger. Some importers, especially those buying for the chains and supermarkets try to get closer to supply sources such as cooperatives and individual producers, and sometimes buy standing crops in other countries. However, they are unable to buy directly from the producers in Holland since only shippers or dispatchers are permitted to deal with producers and producer associations.

TABLE IV IMPORTS AND EXPORTS OF FRUIT AND VEGETABLES
WEST GERMANY
 (mill. D.M.)

	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>1968</u>	<u>1969</u>
Imports	3,787	4,777	4,651	4,642	4,752	5,534
Exports	110	126	144	185	224	232

Source: The Europa Year Book, 1971, Volume 1.

TABLE V IMPORTERS SALES : BY MAJOR BUYERS

	<u>Percent</u>
Retailers	10
Integrated buyers (chains, supermarkets etc.)	20
Wholesalers	<u>70</u>
	<u>100</u>

Source : UNCTAD-GATT, op.cit., p.135

The Netherlands as a Source of Produce

Since Holland is an important source of supply for West Germany it is of interest to note the effects of Germany's procurement methods on the Dutch auction system. Most produce in Holland passes through auction, a great deal of the produce being for export, thus produce is bought at these auctions by buyers from other countries as well as local buyers. The growth of supermarketing in Germany, and the formation of chain organisations which do their buying in Holland, has had significant effects on the auction system in Holland and there has been concern that competition has been declining because of a lack of buyers. Concentration of buying has been occurring due to the changes in retailing and has resulted in 80 percent of the trade with the United Kingdom being in the hands of five firms, while a few Germany Organisations are in a dominating position in trade with that country.

While no evidence has been given on these effects, they highlight the fact that the decline of competition in the auctions is not just a result of buyers bypassing the auctions - it is affected by the concentration of buying power in the hands of a small number of large buyers.

This point has particular significance to New Zealand, as it illustrates the fact that even should direct buying be limited, competition may be reduced by the growth of large retail firms dealing at auction - it may not be sufficient to stop direct selling since the effects can arise despite it. However, it must be stressed again, that no knowledge exists on how many buyers are needed on an auction to ensure adequate competition.

Summary

West Germany represents a country where large scale retailing is very important in the sale of fresh fruit and vegetables, the supplies coming from other countries as well as locally. Again, little can be said about the effects of direct buying other than that it is relatively common and has the unusual feature that some of the supplies arranged direct are from overseas producers.

Concentration of buying power by large German retail outlets has been given as a contributing factor in the decline of competition on the Dutch auctions, indicating that elimination of direct buying need not necessarily solve the problems of competition.

However, even though the large retailers may be tending to bypass the wholesale markets to a degree, it is interesting to note that -

"... although some observers have concluded that the wholesale markets have had their day, the statistics of their turnover (in physical quantities) show that they have held their own and even increased their business in some cases. Moreover, the large retail concerns have not made an unqualified success in the realm of direct purchases. Some have even experienced considerable losses in buying produce outside Germany at firm prices, having not unnaturally misjudged the market. These experiences have tended to drive them back into the markets for their purchases."^{22/}

22. Ellis, P.G. & Kirk, J.H., op.cit., p.46

III. MEASURES TAKEN BY GROWERS TO PROTECT THEIR POSITION

Since it has been suggested that direct selling has detrimental effects on the grower, it is of interest to see if any measures have been taken by the growers to protect their position. From the discussion of individual countries, it has been suggested that very little evidence exists to prove the growers have in fact suffered due to direct selling. It seems likely that many of the growers' problems are due to the nature of the product, and the general economic pressures favouring amalgamation of units and a general increase in average property size.

For these reasons it is difficult to see that moves taken by the growers in these countries have been solely the result of direct selling. However, those measures which may relate to the practice will be discussed.

(A) U.S.A.

First, it must be stated that most activity has been associated with process growers, not fresh. Organisation has been the suggested answer to the problem of bigness of the buyer - that is, for the growers to attempt to achieve countervailing power. Methods used have been the formation of general cooperatives, bargaining cooperatives, and the use of marketing agreements and marketing orders.

Cooperatives

These have been in existence since the late 1800's, and at present are important in the fresh produce field. They may carry out functions such as grading, packing, shipping, and selling the produce of their members. Many perform production services as well and may even arrange purchases of farm requisities. However, by and large, the cooperatives centre their activities upon the handling and marketing of the produce of their members.

The cooperatives, along with the trend in farm size, have tended towards handling larger volumes of business while having fewer members. But it is interesting to note:

"In general, cooperatives are less important as first marketing firms for major vegetable crops than for major fruit crops."^{23/}

Further, the percentage of the total U.S. crop handled by cooperatives is in the main fairly low. Celery is the main vegetable marketed by cooperatives, 32 percent of the total U.S. crop being handled in 1964/65 (Table VI). The other main vegetables using this method were potatoes, tomatoes, lettuce and watermelons, the percentages being as shown.

It should not be thought that these are the only vegetables handled since most cooperatives handle a number of products. In those cases where intermediary agents are not used, the cooperatives used direct selling as the predominant method of moving the crop handled. The cooperative seldom buys the produce from the grower, and further, the grower is seldom paid directly by the buyer. In the few cases where the grower was paid by the buyer the cooperative arranged the general terms of sale, but specific conditions were established by the grower and the buyer.

Thus, cooperatives are an important method by which growers have become organized, and it would appear that direct selling is the preferred method of sale by these, suggesting they have enabled the grower members to achieve a degree of countervailing power in direct negotiation with the large retail firms and shippers.

23. N.C.F.M. Tech. Study 4, op.cit., p.128.

TABLE VI

PROPORTION OF U.S. SALES OF SPECIFIED FRESH
VEGETABLES MARKETED BY COOPERATIVES, 1964/65

	<u>Percent</u>
Potatoes	10
Tomatoes	7
Lettuce	6
Celery	32
Watermelons	4

Source : N.C.F.M. Tech. Study 4, op.cit., p.128

Bargaining Cooperatives

This method of organisation is used as a means of increasing bargaining power. The cooperative may negotiate in general terms or establish specific prices and pricing formulae.

These bargaining cooperatives are not without their problems and the power to negotiate effectively is related to the volume of the produce controlled and the degree to which buyers are willing to recognise the cooperative. The second will be related to the first, since control of a significant proportion of the crop will ensure a willingness to negotiate. A further controlling factor will be the extent to which the cooperative has alternative outlets for its produce.

To obtain substantial gains for its members the cooperative needs:

- (1) Unity and strength among its members;
- (2) To market a large percentage of the supply;
- (3) An alternative market or storage facilities;
- (4) To influence the supply in total and seasonally;
- (5) To take account of the price elasticity of demand and the possibility of discrimination in selling the product;
- (6) To be aware of the assistance possible from legislation.^{24/}

Bargaining cooperatives are considered to be useful, but not to have achieved their full potential since they are voluntary as

24. Adapted from Johnson, S., "Collective Bargaining in Milk Marketing", Can. J. of Ag. Ec. 15 (2) : 1378, 1967.

to membership, and

"... the major limitations have their origins in the individualistic nature of farmers and their reluctance to forego the necessary decision-making freedom required to gain the full measure of bargaining power possible."^{25/}

It is important to note that bargaining cooperatives are found almost completely in negotiations connected with processing crops. In these circumstances, the buyers are a relatively small number of processors, and the individual growers would be faced with a much more concentrated buying sector than exists in the fresh produce field. A small number of buyers taking large individual quantities of produce lends itself to the organisation of growers into bargaining cooperatives to establish countervailing power; and further, to direct marketing as the channel used. The fresh vegetable field does not lend itself so readily to this type of organisation.

Marketing Orders and Agreements

These are another means by which the horticultural industry in the U.S. has attempted improvement in production, marketing, demand and price.

A marketing agreement is a purely voluntary arrangement between the Department of Agriculture and individual handlers of a commodity. It is therefore only binding on those who sign it.

On the other hand, a marketing order can be issued only with the approval of a specified majority of producers. But

25. N.C.F.M. Tech. Study 4, op.cit., p.283.

once approved and issued, its terms and conditions are binding on all relevant producers and handlers in the industry. Obviously, therefore, Orders are a much more powerful weapon than Agreements.

"Marketing Orders and Agreements differ from the major crop control programmes in that they do not include provisions for government payments to growers and they do not control directly the amount any farmer may produce. They enable an industry to manipulate supply and demand in such a way as to bring about a balance at a level which yields a higher net return (to farm producers) than would otherwise result. The approach includes -

- (1) Some concerted effort to stimulate demand, and
- (2) Quality improvement, quantity adjustment, and activities to facilitate the marketing of supplies already produced. In addition many orders provide for some type of research as an aid to administrators of the programmes and members of the industries affected."^{26/}

The main aspects controlled under these arrangements are grading and quality standards, packs and containers, price intelligence, research and quantity restriction. Of these, the most frequently used provisions relate to research and quality regulation. While supply restriction (regulation of

26. Foytik, J., Agricultural Marketing Orders, Calif. Ag. Expt. Station, Giannini Foundation Research Report No.259, November, 1962, p.17.

production) would be the most powerful tool available, it has rarely been used to any degree. Therefore, where excess supply is a major cause of producers' problems, little real progress is likely to be made. In fact:

"There is reason to suspect that marketing orders may have contributed to the development of excess capacity and supply-demand imbalance in a few instances. There is no evidence to suggest that marketing orders, by themselves, have been adequate to re-dress the economic problems of producers in an industry characterised by excess capacity and chronic economic surpluses."^{27/}

The conditions under which marketing orders are most effective are:

- (1) Informed, effective leadership;
- (2) Limited number of distribution channels so that effective control is possible;
- (3) A high proportion of the total supply of the product under the order;
- (4) An inelastic demand so that supply limitations will increase incomes;
- (5) A weak or inelastic supply response so that any gains achieved are not lost by increased supplies from existing or new growers.
- (6) Strong member interest.

In order to work effectively, this form of organisation requires control over much of the produce, and therefore is

27. N.C.F.M. Tech. Study 4, op.cit., p.305.

most suited to products where production is limited to concentrated areas, since an order of national coverage is much more difficult to control. It seems that in the field of fresh vegetables factors contributing to the limited usefulness of marketing orders are : the widely separated production areas; the limited number of alternative marketing outlets; and the perishability of the products. Of the 90 Orders in existence in 1964/65 27 were for vegetables and 11 of these were for potatoes, an indication of the minor extent to which most fresh vegetables use this system.

(B) UNITED KINGDOM (U.K.)

Little effect of direct selling has been evidenced and few actions have been taken by the growers.

Cooperatives

The formation of cooperatives appears to be the only action taken by growers which could be regarded as a measure of protection against direct selling. Cooperatives have, however, been a common feature of British agriculture and horticulture for many years. They are therefore not solely a result of direct selling. The cooperatives carry out the functions mentioned under the U.S.A. discussion, and handle a wide range of vegetables, although in the case of peas and beans for canning and processing (70 percent) and cucumbers (31 percent) do they handle a significant proportion of England's total production.^{28/}

They are a means of providing the grower with countervailing power when dealing with large buyers, but are generally unwilling

28. Ellis, P.G., Hunter, C.E. & Kirk, J.H., op.cit., p.9.

to commit a major proportion of their produce to one large buyer, thus restricting the ability of the large retailer to buy direct. Their major advantages are related to other functions, such as economies in handling and grading.

(C) WEST GERMANY

Cooperatives again appear to be the only measure used, and yet again their popularity and usefulness is not solely related to attempts to protect the grower from direct selling difficulties. Some 200 horticultural cooperatives are present and handled about 30 percent of all West German grown vegetables.

SUMMARY

Measures used in the countries covered were cooperatives (both general and bargaining) and marketing orders and agreements. The latter are only used in the U.S.A. They attempt to improve the price the grower receives, but the price levels cannot be blamed on direct selling. As with all countries, excess supply can often be given a major share of the blame.

The cooperatives generally provide the grower with a degree of countervailing power when dealing with large buyers, but their prime activity seems to lie in the other functions they are capable of carrying out. They do, however, present a united front in negotiations, particularly in the processing field where the buyers are fewer and larger than in the fresh produce field.

Marketing orders and agreements are primarily aimed at improving the growers' financial situation by improving grading, supply rationalisation, price intelligence, and general research.

It is interesting to note that cooperatives often engage in direct supply of vegetables to the buyers. This would suggest

that this type of organisation is much more capable of dealing effectively with the large buyers, and that since they have a large quantity of produce to dispose of, they are attracted to large buyers. The two things appear to be related - large buyers prefer dealing with large sellers - when buying direct. Therefore, the growth of large producers is a factor encouraging direct selling, rather than the generally suggested direction of relationship - namely, that direct selling forces growers to become larger. The general economic forces favouring larger production units may also be favouring direct selling.
