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MANAGEMENT CHALLENGES: EMERGING COMPETITION IN FOOD DISTRIBUTION

Competitive Situation in the United States Food Industry, 2010 A.D.

by

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Introduction

It is an extreme pleasure for the author to embark upon this latest in a long series of intellectual journeys into the food industry future (dating from the late 1960s). Our approach will be a logical, time tested one. We will (1) choose a time frame, (2) identify the major elements of change (future shaping variables), (3) speculate about the varying impacts that changes in these variables would have upon the future situation, (4) draw some conclusions based upon our findings, and (5) pass along some implications of these findings to food industry management, policy makers, educators and the public at large.

We will use five major points of focus in this analysis. They are the combinations of products, services, and perceptions containing the nutrients for our citizens--(1) *meals*, (2) *lifestyle*, (3) the *operating environment* for the food indus-

try system, (4) the *nutrient delivery system* which will supply nutrition to our citizens, and (5) the *competitive situation* within and around the system.

Our journey will start with a TIME FRAME, a VISION, and a GOAL as all good journeys should. Then we will proceed into the meat of the discussion.

Time Frame — For this paper, we have chosen 2010 A.D. as our target date. Eighteen years is a short enough time so that most of us can grasp its significance and long enough to assess the impacts of major changes.

Vision — Cain sees food--nutritionally adequate meals--available practically anywhere, at any time, in any form, at a reasonable cost. Unlimited access to nutrition for all our citizens.

Goal — The following statement surfaced in the early 1980s and provides us with a comprehensive target:

“To provide adequate supplies of safe, nutritious food and food products, with desired service levels, at prices that reflect true value to U.S. consumers, at minimum total resource cost.”[1]

Normally, we would apply this to our total food industry system.

Meals — Nutrients fuel the growth, maintenance and activity in the human species. Commodities provide varying combinations of nutrients for people. Meals are groupings of commodities, variously processed, which can provide adequate total nutrition for the individual human being.

The “meal concept” was introduced in the early 1970s.[2] It provides a point of focus for (1) combinations of nutrients, (2) the idea of nutritional vehicles, (3) an easy way to trace movement of products and services through a complex food industry system. It also provides, for all parts of the system, a constant reminder of what is in the ultimate consumers’ minds when they think of food. In addition, if we can see where our commodity or service fits in the overall scheme of things, it tends to give meaning and purpose to our efforts.

Lifestyle

The way we choose to live, the role that food plays in our lives, the manner in which we choose to consume our food, and the types of food and food products we eat all affect the overall demand for food (meals) in our society.

Lifestyles change over time and at varying rates of speed. In the past, the U.S. food industry has largely found itself playing “catch-up” in terms of meeting the needs of changing lifestyles. It is very difficult to predict changes in lifestyles. This is especially true when concentrating on many of the subtle nuances of a complex society.

With the first 2000 A.D. paper[2], we made a series of lifestyle assumptions regarding (1) acti-

vities of the primary meal preparer outside the home, (2) this person’s involvement in meeting meal needs of the family, (3) place of the meal in the social structure, and (4) impact of speed and convenience (value of time) on feeding our people. These predicted lifestyle changes, which *came true in the 1970s and 80s*, brought forth the fast food, prepared food, and microwave era that we are experiencing currently.

We have experienced the “Go-Go 1980s” and are currently weathering a prolonged recession. Dramatic changes are exploding all around us, and we are wondering what sort of life style we can pursue for the last eight years of the twentieth century and the first ten years of the twenty-first.

Some people feel that the heavy borrowing (government, industry and consumers) during the 80s has masked the start of a decline in the level of living in the United States.[7] There are a number of environmental limits--water, energy, fresh air, poisonous elements--all around us that support such a theory. We will talk more about these limits under the section on operating environment for the food industry system. Suffice it to say, the free wheeling, resource-consuming lifestyle most of us have enjoyed for the past 20 years cannot reasonably be thought to continue into the twenty-first century.

There is dramatic evidence that people are scaling back in their food purchases--buying less, buying fewer services, buying down--as a result of the recession.[8] The pertinent question here is: How does this translate to longer range changes in lifestyle? If, in truth, we have had too much and must scale down our lifestyle, that is one set of questions. What do we do with the increasing segment of our society who views this talk of too much only as the cruelest of jokes? If there is to be a “great leveling,” how is it to be accomplished and when will it come?

At this point, the author’s “crystal ball” is extremely cloudy. One could write a series of scenarios from “doomsday — starvation” to “no change — full speed ahead.” In fact, that is what should be done to help provide valuable information for making policy choices. One fact is very

clear. We as a food industry and a people need to do a lot of serious *anticipatory thinking*, very shortly, to be able to even hope to deal with these problems satisfactorily.

The answer lies somewhere in how effectively and efficiently we can deliver those meals to all our citizens to accomplish the goal stated above. This will surely require some significant changes in the food industry system over the next 18 years. Before exploring the system, we need to look at its operating environment.

Operating Environment For the Food Industry System

There are a multitude of parts to this subject. We have chosen ten to comment briefly upon in this paper. No attempt is made here to be exhaustive with the list or comprehensive in our treatment of the subject matter. These parts, future shaping variables, are mentioned because they will all have major impacts on the food industry system between now and 2010 A.D. So they must be considered in determining what the competitive situation might be for the food industry in 2010 A.D.

1. *World Economy* — We have been, are, and will be operating in a worldwide economy. What will be important in 2010 A.D., as now, is the freedom of access to products, technology and people power. The optimist will hope and work for complete freedom of access to these items. The pessimist will cry and settle for the status quo. The realist will be working in the middle, ever pushing toward the free trade side. It's a tall order, but somehow we must learn to live and work with each other to sustain satisfactory life on the planet. Continuous fouling of the collective nest can only move us away from our stated objective.

2. *Information Systems* — One of the major elements in the fabric of our food system is an ever-increasing capacity to deliver more accurate, comprehensive, pertinent information anywhere in the world. The challenge is to use the capacity and output of future information systems to constantly improve the efficiency and effectiveness of the total food system.

3. *Technology* — As in the past, technological change will continue to fuel growth and development in the food system. Product, packaging, and systems technology will be critical areas of emphasis.

4. *Government* — Currently, some governments in the world are changing with lightening speed, or trying to. The U.S. government, thanks largely to special interests, entitlements, excessive bureaucracy, and ineffective leadership stands basically at a gridlock. Can the government make a significant positive impact upon the competitive situation in the food industry by 2010 A.D.? Based upon its track record and current state, there is scarce hope for an affirmative answer.

5. *Labor* — The power (numbers) of organized labor is dwindling in the traditional areas (steel, autos, trades) and growing in the government and institutional areas (state and local governments and the post office). As we move more into the service world, the future of organized labor becomes unclear. Where in the future food system will there be large aggregations of skilled or semi skilled workers that could benefit from group bargaining? More importantly, what would be the impact of increased activity in this area upon the food industry and its ability to successfully accomplish its objective?

6. *Debt* — Interest and principle repayment on our massive public and private debts rob current and future generations of potential investments in both human capital development and technological research and development. The principles of debt management are elementary. Essentially, you learn to live within your means. As individuals, many of us are learning this painful lesson. As a government, we have not started and apparently don't want to start to get our fiscal house in order. The longer we wait to "bite the bullet" on our fiscal situation, the greater will be the negative impact upon the food industry in 2010 A.D.

7. *Infrastructure — transport* — One has but to travel over an interstate highway in any major urban area to get a flavor for the potential problems facing our nation's transport system. The more one travels, especially by different modes, the more the enormity and urgency of the problem

sinks in. Our entire food industry system has been built based on cheap, reliable transportation. However, basic flaws in construction philosophy and failure to invest in proper maintenance and renewal of the system could leave this essential link in our food industry system in a shambles by 2010 A.D.

8. *Energy* — We survived the "energy crunches" of the 1970s, conserved slightly on energy in the early 1980s, fought a war over energy in the early 1990s, but the basic energy situation in this country has not changed. We are using more and more of a non-renewable resource-oil, with finite limits, major supplies of which we do not control. Worse yet, what passes for an energy policy translates into "pump the United States dry and minimize investments in alternative energy technologies." Dependence on foreign oil supplies increases daily.

Unfortunately, the food industry system is particularly vulnerable, since mobility is one of its key elements, and mobility depends almost exclusively on oil.

If we started to reverse energy dependence and develop alternative energy technologies from this day on, major inroads are achievable; but the problem won't be solved by 2010 A.D.

9. *Water* — Absolutely essential to the production, processing and preparation of food, this element is also critical to the survival of the human species. In some areas of the country, mainly the West Coast and Southeast, the competition between water for food production and processing and direct human consumption becomes more intense with each passing day. In general, water management has been poor at best. Lakes and rivers have been fouled, major aquifers have been drained excessively, runoff causes massive erosion of valuable top soil, and so on. This is another part of the infrastructure that will require massive investments to handle the needs of our society and the food industry in 2010 A.D.

10. *"People Limits"* — The last of these elements is an intangible one, but we feel it will become increasingly important over the next 18 years. Economic and social stress upon families

and individuals, crime, drugs, ineffective public and private institutions, increasing frustrations, stress, inability to make a difference, and loss of hope, all make an impact upon our lives. Somewhere there is a collective limit to all this stress where people say "enough--effective changes have to be made and made now." The Los Angeles riots of 1992 are the latest in a series of ever-escalating violent examples of people going over the limit.

Fourth on the agenda, we will focus upon the nutrient delivery systems in the United States--past, present and future.

Nutrient Delivery Systems

The concept of a functioning system which delivers nutritious meals to our citizens in some sort of loosely organized fashion was introduced in 1973.[3] The principle was relatively simple, but the application was and is extremely complex. The concept bounced around the industry with varying degrees of acceptance until 1986 when a three part series on "Total Food Industry Systems" was introduced in the Journal. The first article was designed to help food industry management better understand the concept and to get their firms prepared to successfully participate in the system.[4] The second article on market areas and the total system will be woven into the discussion later on in the paper.[12] The final article in the series put the total systems concept on a nationwide basis, looking to the future.[5]

The thoughts behind this discussion of nutrient delivery systems and Total Food Industry Systems are as follows: we had a system to deliver nutrients to our people in the past; we have one now and will have one in the future. Over time this system will change. Some of these changes will have a positive impact on competition in the food industry and some will have a negative impact. During the remainder of this paper, we will take three structural measurements to identify these major impacts. We will combine these impacts with the environmental impacts discussed earlier, comment on integration and power and arrive at a "bottom line" regarding the competitive situation in the food industry for 2010 A.D.

Competitive Situation

A. Structural Measurements

1. 1979 — recent past

In a keynote address to the 1979 F.D.R.S. annual meeting in Portland, Oregon, we took a look at elements of size, concentration and market behavior in the food industry; at organized labor; at the government; and at the consumer.[6] This was an initial and halting attempt to look at the total food industry system. Data were fragmented and disjointed since there was no common data system for the total industry and no consistent history on total industry characteristics and performance. Unfortunately, the same is true for the present day. Measurements have improved in both quality and scope. But there is still no comprehensive process for looking at the total system.

So, what were the results? We found some evidence of increases in size and concentration at retail, food service, wholesale, food processing, farm supply and production agriculture in the food industry. We also found some elements of size and power in organized labor, government and consumer organizations. The panel of expert reviewers generally acknowledged the potential growth in size, concentration, and power. However, the general consensus was that such conditions were not too serious and that competition in the food industry would not be significantly impaired. Also, each particular interest group was sure that if competition was to be impaired it would not be the fault of their group.

2. 1992 — the present

For the current period, we have a more comprehensive and detailed overview of parts of the food industry system than we did in 1979. Food Institute's "Food Retailing Review — 1992,"[7] USDA's "Food Marketing Review, 1991"[9] and the Marion book[10] provide a wealth of data on the pieces of the system. In addition, the industry standard Progressive Grocers "Annual Report of the Grocery Industry"[8] and selected Census data provide us with a sense of continuity over a considerable time period. Of

course, selected trade association data are extremely helpful as well.

What do these data tell us? In the area of *traditional concentration data* we find:

- (a) chains did 62 percent of grocery store sales, up from 49 percent in 1972;
- (b) on an S.M.S.A. basis at retail, the top four firms did 59 percent of sales, up slightly from 57 percent in 1972;
- (c) 20 top food service firms did 62 percent of sales;
- (d) 20 top fast food firms did 71 percent of sales;
- (e) at wholesale 1.8 percent of the grocery firms control 74 percent of the assets of that industry segment;
- (f) five top food service distributors did 82 percent of sales;
- (g) in food manufacturing the top 50 firms did 50 percent of the value added.

With regard to *existing players* in the marketplace:

C—store numbers leveled off at 52,000 for traditional units recorded, 32,520 petroleum company units and growing.

Supers experienced growth in the larger format sizes and decline in traditional format except for Food Lion; foreign ownership at retail and food manufacturing continues as does U.S. investment overseas in fast food and food manufacturing.

Labor unions represent 42 percent of clerks in chain stores, down from 62 percent in 1977.

Labor productivity declines at retail and food service.

Food manufacturers' sales are divided:
40 percent—direct to consumers—branded

60 percent--unbranded and undifferentiated--sold to rest of food system

Information system technologies are growing rapidly.

Investment in R & D--both product and human capital--is almost embarrassingly small.

Regarding *new players* in the marketplace:

Wholesale clubs emerge; mass merchandisers and deep discount drug stores as factors in the grocery industry are documented and widely discussed.

Petroleum companies are a growing force in the C-store industry.

Although the "merger-mania" of the 1980s has slowed dramatically, the trans-nationals are moving to consolidate their holdings, reduce their debt, and focus upon their market targets for the rest of the 1990s and beyond.

The current recession has had an impact on prepared and gourmet food sales. Major appeals to price and ways to save money are now paramount.

3. 2010 — structural estimate

A wag recently commented: "one of the troubles with the future is that there is no historical data on it." We can, however, get data on the future. We can take advantage of a myriad of trend projections (if conditions fit the time frame) and use scenario writing, modeling and other techniques to provide us with data. In addition to these data, we can add some intuition, best guess, and just plain "gut feeling" to assist us with our analysis of any time period.

What you get in this segment of the paper is Cain's perception of structure of the U.S. nutrient delivery systems in 2010 A.D. Later we will discuss the competitive situation of the period.

The U.S. nutrient delivery system in 2010 A.D will:

1. Have *better information systems*, tying the food system closer together and helping it to perform more efficiently.
2. Use *meals* as the prime nutrient vehicle, be more *universal* and more *basic*. *Simplicity* will help to adjust to the movement toward lower standard of living.
3. Break the "*to market, to market*" syndrome and increase sales of food away from home.[13]
4. Be more *concentrated* due to:
 - Global marketing
 - Better information systems
 - More centralized financing
 - Improved product and packaging technology
5. Have *new players*
 - (A) City and area market concept as discussed in the inner city paper[11] and the marketing system paper.[12]
 - (B) "Flexi-mart" — combination fast food and C-store[11]
 - (C) Delivery — not new but will fit certain densely populated markets[13]

In order to expand upon this structural estimate for 2010 A.D., we will proceed with a discussion of *integration, concentration, and power*.

B. Integration

We normally talk about four types of economic integration--horizontal, vertical, conglomerate, and transnational. As we move forward along the time continuum toward 2010 A.D., there will be changes in the U.S. food industry system at all four levels of integration.

At the *horizontal* level, we can see these areas of change:

- (1) Mass merchandisers and wholesale clubs.
- (2) Petroleum companies--C-stores.

(3) "Flexi-mart" — new retail institution, part C-store, part fast food

For *vertical* integration, we see changes at the city or area market portion of the system. Specifically, we can look at localized meal or perishables preparation in central facilities for distribution to retail or food service units.[11]

At the *conglomerate* level, one can see a relative pause in activity following the "merger mania" of the 1980s. There will probably be a sort of "shake down cruise" to get the firms ready for operation in the late 1990s. For the first decade of the 21st century, there could easily be increased activity in the non-food firms which have varying degrees of interest in the food industry.

Closely related is the *transnational* level. Activity here will have the greatest impact upon the food manufacturing segment. On the standard meal components, worldwide competition could be quite fierce. There will also be selected activity at retail and specialty wholesale. The expansion overseas of fast food outlets will continue up to 2010 A.D.

C. Concentration

When looking at concentration, there are two major areas of focus. First is size of unit. Through the 1980s and early 90s we have experienced a proliferation of changes in retail grocery formats, largely to increase the size of units. Expected gains were (1) economics of size in operation, and (2) increase in share of specific market areas. If we were to look at strictly the food portion of these larger formats, we are not sure that the hoped-for gains have been realized. Have the gains come from the non-food portion of the market?

When we start to put the meal concept, the breaking of the "to market, to market" syndrome and the tightening of the nutrient delivery system together, this puts pressure on the food portions of all super formats. Logic says the larger the food unit the greater the pressure. This same logic applied to the general line grocery wholesale segment of the food industry.

The second aspect of concentration is ownership. By owning a larger portion of units in a given market, there are economies in purchasing and operating, as well as marketing strengths to be gained. As most of the other areas are pretty well concentrated, we can look for more concentration in some areas of food manufacturing--worldwide and the grocery business at retail.

D. Power

In this section power is defined as the ability to influence price, product quality, product offerings and availability. We will look at power in the food industry, government, organized labor, and the consumer movement.

For the food industry at *retail*, the large format grocery stores and the food sections of the non-food retailers will lose ground to the food service and fast food segments under the "meal concept" nutrient delivery system. If we are dealing with meal components, then the ultimate fate of the institutional unit is determined by how efficiently and effectively it meets the specific needs of the market. This is a condition which leads to increased concentration of power within the retail segment of the food industry. In a nutshell, it means a smaller number of meal retailing firms, a smaller number of food service firms and fast food firms, with a number of specialty retailers to complete the square. In the author's view, this is a condition that we have been moving toward for some considerable time.

As for food wholesaling, both the general line grocery wholesale and, of late, the food service wholesale have experienced high degrees of concentration in their segment of the food industry system. There are a small number of specialty wholesalers who, in a sense, are quite concentrated in their market niche.

The appropriate question for the wholesale segment of the food industry is *not* "will it become more concentrated?" The *key question* for the general line grocery wholesalers, in particular, is, "will they, by either vertical integration or by-passing, have their functions absorbed by the food manufacturer, the retail segment or some conglomerate arrangement?"

In the *food manufacturing* segment, as originators of a significant portion of the meals for this nutrient delivery system for 2010 A.D., the natural tendency would be to grow in size to enjoy economies of scale as well as market power. This is indeed what has happened. What will be new here, over the next 20 years, will be the growth in transnationals and the increasing of conglomerate power, with control being outside of the United States. This has already started.

In *production agriculture*, the trend toward smaller numbers of commercial farms and larger farm units will continue its seemingly inexorable march through time. The real power impact will be producers from other countries in the world who can compete successfully with our farmers. This will be especially true in the seasonal, perishable items.

Bottom line on power for the food industry!!
We can see increased concentration at all levels.

For *government*, the author can visualize a unit with tremendous latent power. However, political "gridlock" and unmanageable debts make it virtually impossible for the government to exert anything more than "special interest power." It's the old story "you either lead, follow, or get out of the way." In this case, without dramatic changes the government will largely be "in the way."

For *organized labor*, with declining numbers in the trades and the changing composition of the service-oriented work force, the outlook for the effective power is on the decline.

For *consumers*, as they are poorly organized and not centrally funded, the outlook for general interest power is no better than it has been in the past, and probably worse. As members of special interest groups, consumers will be able to help affect specific changes in the food industry system. But unless there are dramatic changes in our political system by 2010 A.D, general interest changes are largely pipe dreams.

Summary

Regarding impacts of the *operating environments* for the nutrient delivery system upon the competitive situation in 2010 A.D., we would offer: (A) two areas with definite positive (+) impacts--information systems and technology, (B) two with mixed impacts (\pm)--world economy and people limits, and (C) the other six areas--governments, labor, debt, infrastructure, transport, energy, and water with negative (-) impacts.

Within the nutrient delivery system, we have indicated increasing (+) power to the food industry and declining power (-) to the other three groups--government, organized labor, and consumer movement.

E. End Results

The bottom line here is a potentially diminished food component in a perceived lower quality of life in 2010 A.D. which can mean:

Limited Availability
Lower Quality
Less choice--ethnic diversity notwithstanding
Higher prices--no more "cheap food"

For the consumer, a decrease in the level of competition means less attention to the food component of their lives.

For the food industry, different levels of competition mean a "harder way to make a buck" in 2010 A.D.

F. What to do about it?

Always the optimist, the author wants to end on a positive note, if possible. The suggestions that follow seem almost like "truisms," but they will work.

For the *consumer*, get yourself aligned with the "special interest" groups that will fight for changes in the system which will best meet your individual needs. Given the general situation,

which will not change completely in 20 years, this is the only way to fly.

For the *industry*, look ahead and pick the "niche" where you can maximize the benefits from your given set of resources.

For the *system*, someone will be around to worry a bit about the food industry system over the next 20 years. Maybe Cain? Maybe someone else?

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