Discussion of

Structural Changes in the Food and Fiber System

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Knowledge such as a basic understanding of the food and fiber sector, seems more like a dead fish in the creel than anything else. It ages quickly. This has been one of my recurring frustrations in economic research and teaching. Knowledge, once gained, grows stale.

I feel uneasy, for example, about my understanding of product differentiation and barriers to entry into food manufacturing, and of vertical integration into food processing by grocery chains. Just ten years ago, in 1966, I helped prepare chapters on these topics for the National Commission on Food Marketing. Now, Congress is considering legislation to establish another food commission. Such a research effort is sorely needed.

Economic history is important, of course. Without an understanding of structural changes in the past, our view of present changes lacks perspective. We are doomed to repeat past mistakes. It seems to me of critical importance that we understand the relationship between trends in structure and market behavior, between structure and performance, and between structure and policy. This is a large order. It seems that only a National Commission can muster the necessary resources to accomplish such a large research task.

It would be unfair to expect the participants in this program to fulfill the need for such basic economic knowledge. I am grateful for what they have done. They have given us an informative and up-to-date review of many trends which are important to managerial decision making in the food and fiber sector. For example, they review aspects of trends in efficiency, population, energy, capital, multinational corporations and commodity markets. Their unique knowledge and concern for these matters reflects their experience as corporate insiders, with access to the executive suite. It need hardly be said that most of their comments on the implications of recent trends for structural changes seem also to reflect their day-to-day contact with the corporate management point of view.

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Both Hammonds and Hayenga discuss elements of a kind of "Future Shock," as in Tofler's book by that title, which has beset the food and fiber sector in the past five years. Tofler's main thesis is that changes are occurring so fast that man and his institutions are unable to cope. The old knowledge is fast outdated; the old remedies do not work.

According to Hayenga, ". . . the *shocks*. . . have made investors and management in the food industry much more wary." He concludes that the overall economic environment of the food and fiber sector may be characterized as "more uncertain, with potentially greater price, supply and policy instability than was the situation five years earlier." Then, it seems to me he says that the conventional oligopolistic remedies have been applied. The results include *higher margins* – "to build larger risk premiums into product pricing decisions . . . and to *transfer or eliminate* some of (the) increased risks. . ." Thus, he acknowledges: "though the severe recession led to operating capacities less than 70 percent of capacity. . . price-cutting was definitely not in vogue as was the case in earlier recessions. Rather (the) *maintenance of margins* and internal cash flow probably became much more important motivations . . ." to both large and small firms.

Hayenga suggests that when concentration statistics become available for the past five years, they will show increases. He seems to favor the expected trend, wondering "whether the *competition* in individual markets by more viable, financially secure firms might not be more viable (and less sporadic) in the long run."

Hammonds concludes that: "the super market sector is in for a period of intense competition between now and at least 1980." He shows that this intense competition will be among larger stores with sales of more than $4 million annually. They are the most rapid growing segment of food distribution, increasing by one-third between 1974 and 1975. These 7,000 stores have total sales of nearly $42 billion annually. He expects that with the demise of inefficient operators, the number of super markets will decline from 32,000 today to about 25,000 by 1980.

To many economists, Galbraith for one, the expected economic result from these trends in number of stores, store sizes and competition, would be *increased efficiency*. However, the evidence Hammonds presents suggests the opposite. The *efficiency of capital employed* has declined about 4 percent annually. This is based on average sales per square foot of selling space, deflated by the food-at-home portion of the consumer price index. USDA data show labor productivity in food retailing stood at the same level in 1974 as it was in 1964, ten years earlier.

No information was presented at this session on the trends in food prices, the gross margins of food retailers, or the profit trends of food processors and retailers. The information on these trends currently available from other sources is also incomplete. However, in the past few years, consumer prices for food have increased by approximately one-half. We should know what proportion of this rise was due to farm price increases, and what proportion resulted from increased gross margins of processors and retailers. Other sources suggest that large food processors have received higher profits than the average for all industries. In the Western States, Safeway and Albertson's grocery chains also have had higher profits than all industries.

This is not the expected performance result from intense competition. It is the expected result of increasing concentration of economic power. The Joint Economic Committee of Congress has prepared data from the 1972 Census showing that profit rates *rise* in grocery retailing with increased market share of individual companies and with increased market concentration at the four firm level.

The 50 largest food manufacturing companies have increased their dominance. From 1950 to 1974, their share of total food sales increased from 41 percent to 56 percent. Over the same 25 years, their profits have also increased relative to the average of all manufacturing industries in the U.S., and are at higher levels today.

No information was presented in this session on anti-competition practices. Yesterday, the *Denver Post* reported the Federal Trade Commission has alleged the General Foods Corporation engaged in monopolistic practices to foreclose entry into the Northeast U.S. coffee market. Folgers coffee division controls 45 percent of that market.

The Seevers paper raises a number of important issues about the regulation of commodity futures markets. Probably, most important is his exploration of the benefits and costs of government regulation. The National Science Foundation recently awarded substantial research contracts to Pennsylvania State University and Colorado State University to develop measures of benefits and costs of regulating hamburger production and consumption from the ranch to the consumer. It is suggestive that in the case of possible reduced regulation of milk quality, it has been estimated that milk prices could fall to three-fourths of their current levels. The next decade may see more and more economists turn their attention to the important questions concerning the performance of regulations with respect to a number of food and fiber products. This may become a new direction for an applied institutional economics.