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Americans will allocate about 15 percent of their disposable personal income to food in 1985, the lowest percentage in U.S. history, about 4 percent will go to purchase raw agricultural products used in the food supply. The other 11 percent, over \$300 billion dollars, to pay for processing, transporting, storing, distribution, retailing, and servicing of the raw food supply. This intricate and interacting network of firms that market the food supply from the farm gate to the final consumer make up the food marketing system.

In total, there are over a million establishments within this system. These include over 250,000 retailers, about 700,000 food service establishments about 40,000 wholesalers, and 16,000 food processors. In terms of employment, the system is one of the largest in the U.S., generating approximately 12,000,000 full time equivalent jobs, more than one out of every 10 U.S. workers. These include 3 1/2 million workers in retailing, wholesaling and transportation, about 1 1/2 million in food processing, and 3 1/2 million in eating and drinking places. In addition, the food marketing system generated another 3 1/2 million jobs through other supporting sectors.

The performance of the four market sectors (processing, wholesaling, retailing, and servicing) is important to the overall functioning of the U.S. agricultural, consumer, and non-farm economies. In 1985, about 1,400 pounds of food per person (retail-weight equivalent) will leave American farms, a quantity virtually unchanged over the past quarter century. Over the years, however, major changes changes have occurred in the composition and final form of foods consumed.

- o Over the past decade less milk and eggs and more chicken, fish, fats, fats, and oils, soft drinks, and vegetables are being consumed.
- o Relatively less food is now purchased for at home use and more away from home. At home food expenditures declined from roughly 74 percent of total food expenditures in 1960 to an estimated 58 percent in 1985.
- o The form in which these 1,400 pounds of food have been sold has also undergone constant change. For many food products sold in grocery stores, the degree of processing has changed considerably, as shown by relative shifts in what is purchased (breaded chicken fillets rather than raw chicken). At the retail level, the number of products in the nation's supermarkets ranges from 12 to 25 thousand. Each year from four to six thousand new products appear on the nation's grocery shelves.

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- o The type of institution in which food is purchased is changing. The bulk of at-home purchases now take place in large supermarket chains; three decades ago, single store firms predominated. Fast food chains currently account for about 45 percent of eating place sales, up from 10 percent in the 1950's.

The food marketing system is the link between the farmer and the consumer. Shifts in the demand for agricultural products at the consumer level are transmitted by the food marketing system to the farmer. Consumer demand can be affected by changes in the sociodemographic composition of the population (including shifts in regionalization, median age, race, income, educational levels, and family characteristics) and by changes in technology, life styles and health concerns. In addition to providing consumer demand signals to the farmer, the food marketing system can be pivotal in stimulating demand for agricultural products via product innovation, advertising and promotion, and efficient distribution.

As agent for the agricultural economy, the food marketing system must deal with an unpredictable and highly perishable supply of raw materials. Crop output can not be closely controlled because of the vagaries of the weather. In some cases, there are long fixed lags between the decision to produce and actual production. These uncertainties mean that the food marketing system must deal with wide price fluctuations for some commodities, especially fresh fruits and vegetable, and animal products.

The U.S. food marketing system is essentially a slow growth industry compared to the nonfood economy. This can be seen from both income and production. Disposable personal income rose at a yearly compounded growth rate of nearly 5 percent between 1974 and 1984, while food expenditures rose at a yearly rate of less than 3 percent. Consequently, the portion of disposable income allocated to food fell from nearly 17 percent to about 15 percent during the decade. On the production side, the value added by the food marketing system rose at a yearly compound growth rate of 1 percent between 1976 and 1984, while the nonfood marketing system's sector rose 1.6 percent. Consequently the food system's share of total value added fell from about 10 percent to about 9 percent. The system's share of total U.S. employment fell from 10.7 percent to 10.1 percent.

While on the demand side the food system is characterized by slow growth, on the supply side the industry is shaped by several basic economic characteristics. The industry is labor intensive, rather than capital intensive, especially in food service and food retailing. Second, the cost of raw products amounts to about a third of domestically produced foods, so that vacillations in farm prices can impact prices at retail. Third, about a sixth of the U.S. food supply is imported by the U.S. food marketing system. While exports constitute a large portion of U.S. raw agricultural products, the export market accounts for only a small portion of U.S. manufactured food products.

Given its stable but moderate growth and inherent supply characteristics, the food market system benefits by an overall economic climate of stable growth and wage and price stability. During the 1980's, the food system has essentially operated in such a climate, substantially different from the

1970's. Stable or falling farm prices have been the rule rather than the exception. Between 1980 and 1985, the index of prices received by farmers for food commodities, rose only 5 percent. By comparison, farm prices rose nearly 40 percent between 1975 and 1980. Wages account for another third of food marketing system costs. Rapidly rising wages had been prevalent during much of the period from 1970 to 1982. Average hourly earnings rose from \$3.35 to \$8.49 during that period. Since 1982, increases in wage rates have slowed markedly, and in a number of instances food marketing firms have negotiated wage concessions. Inputs, other than, labor, are of lesser, but significant importance to the industry's costs. Energy and intercity transportation costs account for about a tenth of the industry's cost structure. Oil prices rose over 600 percent between 1972 and 1982, but fell almost a fourth between the early and mid 1980's. Real interest, however, rose considerably during much of the 1980's. The nominal prime rate of interest reached nearly 16 percent in 1982, while the inflation rate was only 6 percent. In contrast, during much of the 1970's the inflation rate was higher than the interest rate. However, because much of the food marketing industry is not highly leveraged, the impact of higher rates has been minimal. Interest costs for instance, accounted for 2 percent of the marketing bill in 1984.

Throughout the 1980's, the U.S. dollar has been very strong against all other currencies. By the late 1970's, gold prices had reached nearly \$900 an ounce; by the mid 1980's they had fallen to \$350 an ounce. The value of the dollar compared to nearly all currencies rose very sharply. The decline in exchange rates has been beneficial to importers of foreign agricultural products. Exports account for only a small portion of U.S. processed foods. On the foreign investment level, the strengthened dollar has made foreign investment in U.S. food processing, processing, wholesaling, retailing, and food service less attractive.

While producer prices and wages remained relatively stable during the 1980's so did food prices. Between 1980 and 1985, retail food prices rose at an average annual compound rate of 3 percent, compared to 8 percent during the decade of the seventies. Thus, wage and price stability on the cost side has been translated into slow price increases in margins at the retail level.

The 1980's have been characterized by a sharp increase in mergers and acquisitions throughout American industry and food manufacturing, retailing, wholesaling, and food service have all taken part in this process. Because of stable growth and strong financial position, many food marketing firms are a prime target for acquisition.

Much of the same environment prevails in 1985, but several differences exist which can impact on the food system. Farm prices have been declining in 1985. Among meat products, prices received for poultry and eggs will show nearly a 15 percent drop from the levels of 1984. The indexes of prices received by fruit farmers likely will average 6 percent lower, while those for commercial vegetables will be 7 to 10 percent lower than in 1984. Second, the dollar weakened relative to other foreign currencies, thus rising prices of imported food products.

The weakening of the dollar, reflected not only continued trade deficits, but a sharp drop in U.S. interest rates, thus decreasing the demand for U.S. dollars. Interest rates during most of 1985 were considerably below a year earlier, mirroring not only a slowdown in the economy but an accomodating Federal Reserve policy as well.

Economic growth slowed considerably during the first half of 1985. Real GNP growth grew only a third as fast as a year earlier. Real per capita disposable income, which rose nearly 6 percent in 1984, rose at a seasonally adjusted annual rate of slightly above 2 percent during the first three quarters of 1985. Aided in large part by the slowdown in the economy, wages and prices rose at an even lower pace than in 1984 during the first half of 1985. The producer price index averaged a 2 percent increase in 1984, while during the first half of 1985 it averaged less than 1 1/2 percent higher. In 1984, retail food prices advanced less than 4 percent, and the increase in 1985 appears likely to be even less, reflecting both a drop in farm prices and modest increases for nonfarm inputs.

In 1985, significant developments include a wave of mergers as well as divestitures; continued pressure for wage concessions and work rule adjustment and new store formats as firms compete to maintain their share of a slow growth market. The share of the total food dollar allocated to food at home, which dropped from 74 percent in 1960 to 58 percent in 1984, continued its fall in 1985. But within both food retailing and food service, significant changes continued in terms of formats. In food retailing, while the bulk of all sales continued to be captured by conventional supermarkets, this format is giving way to increased penetration by warehouse stores, super stores, combination food and drug stores, and convenience stores. In the faster growing food service industry, franchised outlets, chains, and fast food outlets continued to gain at the expense of single unit and full service eating places. In food processing, the share of total shipments by highly processed products constitute an increasing share of total shipments, offset by a declining share for processed fruits and vegetables, milk, and sugar.

The structure of the food marketing industries also continued to change. The number of food processing establishments, which declined from 42 thousand in 1947 to 21 thousand in 1982, continued falling as many small firms were absorbed into larger firms. The number of food retailing firms increased for the first time in 46 years, but average local concentration in local markets continued to rise. Only in foodservice did the number of establishments continue a longterm increase. Many large wholesalers are integrating forward by acquiring or building retail stores which they operate. The top ten wholesalers operated about 300 grocery stores in 1984.

Amidst all of these changes, the overall pace of food industry acquisitions and mergers increased in the 1980's. The average number of transactions per year was 607, compared to 474 per year between 1975 and 1979. In food processing, slow but steady growth makes many food processing firms inviting targets for acquisition. Intra-industry mergers among food processors allow for more clout in acquiring shelf space in a highly competitive market. Over 40 mergers took place in food retailing in 1984, while over 90 occurred in foodservice.

Current U.S. government forecasts of restrained wage and price inflation for the rest of the decade are somewhat tempered by predictions of moderate growth in overall economic activity. Moderate growth in disposable personal income would impact the most on food service which is highly dependent on increases in DPI. The market for food away from home may be expected to continue growing through the 1980's but at a slower pace. The food retailing system, less dependent on changes in DPI is likely to experience inflation-adjustment growth that closely matches the rate of population growth.

Under these economic conditions for the remainder of the decade, a continuing experimentation in types of retail and food service formats appears likely. In competing for scarce shelf space in the Nation's supermarkets, continued new product introduction appears likely. Changing store formats and products likely will be accompanied by a continued change in industry structure for food processing, wholesaling, and retailing. Part of this change will come from individual mergers, but forward and backward integration may result as all four segments of the industry attempt to gain control both the source of supply and the final retail market. A long-term decline in employment in retailing, wholesaling, and processing appears likely as attempts are made to hold down costs in this labor-intensive industry.