food&water watch

FOOD

Consolidation and Buyer Power in the Grocery Industry

Fact Sheet • December 2010

Food companies throughout the entire food chain are rapidly consolidating, leaving just a handful of powerful middlemen between 2 million American farmers and more than 300 million consumers. One of the most critical links in the food chain that has suffered the effects of this consolidation is the retail sector. A smaller number of grocery stores and supermarkets are exerting more and more control over which foods reach the mass market and the prices families pay at the checkout case. As food retail companies grow larger, so too does their influence on food processors and manufacturers, encouraging consolidation up the food chain, all the way to farmers growing crops and raising livestock.

Large grocery store chains claim to offer consumers lower prices by increasing business efficiency and offering discounts from bulk purchasing. But when these chains control the market, it can actually result in higher prices for consumers. According to the American Antitrust Institute, the concentration in buyers, processing and retailing has "undoubtedly contributed to the increased cost of food."[1] Consumers are especially vulnerable to the consolidated market power of food companies since food is an essential item.[2] Even worse for inner-city and rural consumers, retail consolidation contributes to food deserts, areas where healthy food is inaccessible due to a lack of grocery stores.

Consolidation in the Food Retail Industry

Throughout the 1980s, regional and local supermarket chains dominated the food retail landscape. In the 1990s, large grocery store chains merged or bought out other regional retailers, while large warehouse clubs and large discount general merchandise stores expanded into grocery products.[3] Over the last decade, grocery store chains have focused on consolidation, mergers and takeovers in an effort to compete with the giant food warehouses, such as Wal-Mart and Costco.[4] Between 1996 and 1999, there were 385 grocery mergers — nearly 100 each year.[5] Meanwhile, new national supercenters and discounters have emerged as grocery powerhouses. Wal-Mart, for instance, became the largest food retailer in the United States within a dozen years of opening its first supercenter that sold food products.[6]

The share of groceries sold by the four largest food retailers has more than doubled since 1997.[7] By 2009, the top four food retailers — Wal-Mart, Kroger, Costco and Supervalu — controlled more than half of all grocery sales.[8] Grocery store concentration can be considerably higher on the local level. Consumers spend time and bear travel costs to get to the store, which creates a kind of captive market if there are only a few stores nearby.[9] For example, in the largest 100 metropolitan areas, the four largest food retailers controlled 72 percent of sales by 1998.[10]

Consumers Pay the Price

Consumers have not necessarily benefited from the rapidly consolidating grocery industry. Grocery mergers may have increased chains' gross profit margins and some mergers improved efficiency, but even when the mergers increased efficiencies, the lowered costs were not passed on to consumers in the form of lower grocery prices.[11] Some academic studies have found that higher levels of local retail concentration are associated with higher grocery prices.[12] The majority of studies reviewed by the U.S. Department of Agriculture (USDA) in 2003 found that increased grocery chain consolidation contributed to an increase in consumer grocery prices, which suggests that further consolidation in the retail sector could cost consumers more.[13] A study of grocery store concentration in the United Kingdom found that retailer mergers increased grocery prices by as much as 7 percent, but breaking up big grocery store chains could reduce retail prices by 2 to 4 percent.[14]

Food retail consolidation also contributes to the existence of food deserts, inner-city neighborhoods and rural communities with few or no full-service supermarkets, making access to healthy foods severely limited. Rapid retail consolidation has pushed many of the grocery stores that served these areas out of business, but in many cases the national chains have not filled the void created by the loss of rural and inner-city supermarkets. A recent USDA study found that 2.3 million Americans, 2.2 percent of the population, live more than a mile from a grocery store and are without access to a vehicle.[15] According to USDA, urban food deserts "are characterized by higher levels of racial segregation and greater income inequality," while lack of transportation is the primary characteristic of rural food deserts.[16]

In the largest 100 metropolitan areas, the four largest food retailers controlled 72 percent of sales by 1998.

Many grocery store chains left the inner city during the latter half of the 20th century, as supermarket brands merged and closed unprofitable stores. New, bigger supermarkets were built in the suburbs, creating a model difficult to replicate in city neighborhoods.[17] During the 1980s, cities lost supermarkets, even as more grocery stores opened than closed nationally. By 1995, "the poorest 20 percent of urban neighborhoods had 44 percent less retail supermarket space than the richest 20 percent."[18] The loss of retail stores typically forces low-income consumers to travel farther to reach a grocery store or to shop at a convenience store with fewer, more expensive, less healthy options.[19] Several studies have demonstrated that low-income consumers buy less healthy food, in part because of lack of access to supermarkets.[20]

Advocacy groups, local elected officials and the federal government are leading initiatives to encourage supermarket chains to invest in inner-city neighborhoods and convenience stores to increase healthful food offerings.[21] Nonetheless, the trends toward bigger, suburban supermarkets and closures of urban stores continue, worsening the public health crisis of limited food access in food deserts.[22]

Retailers Exert Buyer Power over Suppliers

Consolidation has given the largest retailers considerable purchasing power as wholesale buyers of groceries. These retailers can exert their influence over food manufacturers, meat processors, produce shippers and other suppliers to reduce their prices and require specific packaging and manufacturing practices. Retailers can also charge suppliers fees to ensure their products receive prime shelf space or promotional efforts. These suppliers, in turn, pressure farmers to lower their prices and workers to lower their wages.

Wal-Mart's supply chain management, logistics and data sharing cut the store's costs, as does its requirement that suppliers manage their own inventory.[23] Wal-Mart's competitors quickly adapted to ratchet down their own costs by requiring grocery manufacturers and suppliers to lower prices.[24] Large, traditional grocery chains have improved their inventory and shelf space management, entered into exclusive supplier arrangements with volume discounts, and developed streamlined distribution chains from the food manufacturers to the retailers.[25]

Larger food manufacturers can also afford to pay shelf space and promotional fees to retailers, creating a barrier for smaller firms that cannot afford the fees, furthering consolidation up the food chain. Many food-processing firms justify their own mergers as an effort to create stronger bargaining power with large retailers.[26] Smaller food processors and manufacturers may leave the industry after determining they cannot get fair prices from dominant grocery buyers.[27]

Food processors, meat packers and other suppliers cannot sacrifice their sales to major retailers, but the retailers can easily switch to alternative suppliers.[28] Large retailers can represent between 10 and 30 percent of a food processor's sales, which gives a retailer significant bargaining power over its suppliers.[29] Retailers often have long-term contracts with food processors and manufacturers. An estimated 50 and 80 percent of meat and poultry are delivered to retailers under long-term contracts between grocery chains and meat processors.[30] An empirical USDA study found that retailer market power enabled supermarkets to push the prices paid to produce shippers for grapefruit, apples and lettuce below the prices they might receive in a functioning competitive market. The study also found that consumer retail prices were higher than purely competitive prices for apples, oranges, grapefruit, fresh grapes and lettuce.[31]

Shelf space and merchandizing fees can reduce competition by increasing the net cost of wholesale groceries — retailers may be willing to pay higher wholesale prices if they are compensated with other payments.[32] Manufacturers that can afford to pay fees can effectively pressure rivals to match or exceed payments to access retail shelf space, which can be a barrier to entry and may raise consumer prices. These fees effectively discriminate against smaller firms since larger firms are more able to pay higher fees for shelf space.[33] One study estimated that these fees can cost consumers about $10 million more annually, when food manufacturers use their profits to pay fees rather than to offer lower prices.[34]

Recommendations

Food retail consolidation allows grocery chains to exercise considerable market power over consumer food choices and prices, as well as contribute to the often-precarious economic condition of farmers and workers. USDA, Congress, the Department of Justice and the Federal Trade Commission (FTC) have allowed concentrated supermarket and agribusiness power to reach these unprecedented levels. They can take concrete actions to restore fairness in the food retail industry. Food & Water Watch recommends:

- **Stronger Horizontal Merger Guidelines to Account for Buyer Power:** The Department of Justice should reform the guidelines it uses to evaluate proposed mergers and include the level of concentration the merger would create nationally and at the local level. It should also consider the impact on consumer access to food and on suppliers.

- **Coordination with the FTC on Grocery Retail Consolidation:** Dividing the antitrust enforcement of retailers between two agencies can create confusion and delays. Having the FTC oversee food manufacturers and supermarkets but the U.S. Department of Justice oversee meatpackers is an outdated model. The U.S. Department of Justice and FTC must coordinate their investigations and antitrust enforcement efforts over the retail grocery industry.

The Department of Justice and FTC should also place a moratorium on any proposed agricultural and food company mergers by the top four firms in any industry. Send your concerns about consolidation, concentration and monopoly power in the food and agriculture sectors to agriculturalworkshops@usdoj.gov.

Endnotes

1 American Antitrust Institute. Transition Report on Competition Policy: Chapter 8 Food. 2008 at 281.
2 Domina, David and C. Robert Taylor. "The Debilitating Effects of Concentration in Markets Affecting Agriculture." Organization for Competitive Markets. September 2009 at 8.
3 Barkema, Lan, et al. Federal Reserve Bank of Kansas City. "The new U.S. meat industry." *Economic Review*. Second Quarter 2001 at 34.
4 Martinez, Steve W. USDA Economic Research Service. "The U.S. Food Marketing System: Recent Developments 1997-2006." Economic Research Report Number 42. May 2007 at iii.
5 Richards, Timothy J. and Paul M. Patterson. USDA ERS. "Competition in Fresh Produce Markets: an Empirical Analysis of Marketing Channel Performance." Contractors and Cooperators Report No. 1. September 2003 at 1.
6 Martinez at 6.
7 Kaufman, Phil. "Consolidation in Food Retailing: Prospects for Consumers and Grocery Suppliers." *Agricultural Outlook*. USDA Economic Research Service. August 2000 at 20; "*Supermarket News*'s Top 75 Retailers for 2009." *Supermarket News*. June 2009.
8 "*Supermarket News*'s Top 75 Retailers for 2009."
9 Sexton, Richard, et al. USDA ERS. "Grocery Retailer Behavior in the Procurement and Sale of Perishable Fresh Produce Commodities." Contractors and Cooperators Report No. 2. September 2003 at 2.
10 Martinez at note 11 at 18.
11 *Ibid.* at 19-20.
12 Cotterill, Ronald W. University of Connecticut Department of Agricultural and Resource Economics, Food Marketing Policy Center. "Antitrust Analysis of Supermarket Retailing: Common Global Concerns that Play Out in Local Markets." Research Report No. 88. July 2005 at 7 and 9-10.
13 Sexton, et al. at 3.
14 Cotterill at 10.
15 USDA Economic Research Service. "Access to Affordable and Nutritious Food: Measuring and Understanding Food Deserts and Their Consequences. Report to Congress." June 2009 at iii.
16 *Ibid.* at iv.
17 Eisenhauer, Elizabeth. "In poor health: Supermarket redlining and urban nutrition." *GeoJournal*. Vol 53. 2001 at 127-128.
18 *Ibid.* at 128.
19 USDA Economic Research Service at 71.
20 *Ibid.* at 78.
21 See U.S. Department of Health and Human Services. [Press release] "Obama Administration Details Healthy Food Financing Initiative." February 19, 2010; The Food Trust. "Pennsylvania Fresh Food Financing Initiative Encouraging the development of food retail in underserved Pennsylvania communities." Available from http://www.thefoodtrust.org/php/programs/fffi.php. Accessed October 15, 2010.
22 Eisenhauer at 128.
23 Martinez at 6-7.
24 Foer, Albert A. American Antitrust Institute. "Mr. Magoo Visits Wal-Mart: Finding the Right Lens for Antitrust." Working Paper No. 06-07. November 30, 2006 at 5.
25 Barkema, Lan, et al. at 39.
26 American Antitrust Institute at 307.
27 Foer at 19.
28 *Ibid.* at 5.
29 *Ibid.* at 4.
30 Domina and Taylor at 75.
31 Dimitri, Carolyn, et al. USDA ERS. "U.S. Fresh Produce Markets: Marketing Channels, Trade Practices, and Retail Pricing Behavior." Agricultural Economic Report No. 825. September 2003 at 4.
32 U.S. Federal Trade Commission. Staff Study. "Slotting Allowances in the Retail Grocery: Selected Case Studies in Five Product Categories." November 2003 at 3.
33 Hendrickson, Mary, William D. Heffernan et al. Department of Rural Sociology, University of Missouri-Columbia. Report to the National Farmers Union. "Consolidation in Food Retailing and Dairy: Implications for Farmers and Consumers in a Global Food System." January 8, 2001 at 12.
34 Rennhoff, Adam D. University of Connecticut Department of Agricultural and Resource Economics, Food Marketing Research Center. "Paying for Shelf Space: An Investigation of Merchandizing Allowances in the Grocery Industry." Research Report No. 84. October 2004 at 2.

For more information:
web: www.foodandwaterwatch.org
email: info@fwwatch.org
phone: (202) 683-2500 (DC) • (415) 293-9900 (CA)