Farm to Retail Price Spreads

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The difference between the farm value and the retail cost of farm-food products has long been a sore point with both consumers and producers. Whenever food prices rise noticeably consumers are inclined to believe that farmers are receiving the benefit. Farmers look at prices in the towns and cities and then at the prices they are paid and wonder who gets the difference.

Higher consumer incomes and prices paid to farmers during recent war years have let the controversy die down somewhat, but now that prices are declining old queries are urgently renewed.
The "Market Basket"

The difference paid by consumers and the amount received by farmers is called "marketing charges." It includes all costs, profits and taxes of processing, transporting and distributing farm-food products.

In order to get the full picture of price spreads and marketing charges we need to examine what has been happening over the long run. The Bureau of Agricultural Economics has computed the costs for what it calls a "market basket" of food consumed by an average family of three consumers per year in the U.S. for each year since 1913. The chart on the cover shows the trends and movements of the retail cost, the marketing charges and the farmer's share of the market basket since 1913. Also shown is the share of the consumer's food dollar that is received by farmers. An examination of this chart gives an indication of where we stand now in relation to past periods.

In 1952 farmers received 48 cents from each dollar spent for food. This is down from the high of 54 cents received in 1945 and is eight cents above the 1935-39 average. The low point of 32 cents was received in 1933. This indicates that the part that gets back to the farmer changes from year to year. Normally the pattern is like this: when retail prices are high the farmer's share of the food dollar is more than when retail prices are low.

The farmer's share varies for the different foods that make up the market basket. For example in 1952 the farmer's share for meat was 63 cents, for poultry and eggs 62 cents, for dairy products 55 cents, fruits and vegetables 37 cents and grain products 20 cents. Variations in the farmer's share reflect the difference in costs of transportation, processing and other marketing services for the individual food items.

Marketing charges also vary from year to year but are more stable and slower to change than are either farm prices or retail prices. Marketing charges change more slowly than prices because some of the elements of cost such as transportation, store rentals, taxes and labor change slowly over a period of time.

Processors Costs Increasing

Many people are astounded when they discover how much of the consumer's dollar it takes to cover the costs of distribution. They feel something must be wrong when it costs more to get a product from producer to consumer than it did to produce it. What is the situation? Are there excessive wastes or inefficiency or large profits being taken along the line? And, is the trend towards higher marketing charges likely to continue?

Marketing charges for the market basket follow rather closely the trend in labor cost and wage rates, since nearly half of the total food marketing costs are made up from the labor bill. Wage rates have continued to rise since World War II and in most lines were up 10 to 15 per cent above pre-Korean levels. Further increases are anticipated in 1953.

The cost of moving food by common carriers has also seen steady increases. Since World War II there have been 12 increases in freight rates. As a result, transportation costs on agricultural products now average about 70 per cent higher than at the end of the war.

Taxes also have a bearing on marketing costs and especially the tax on transportation. The tax rate on freight charges, now at 15 per cent, has two effects. First it tends to increase the cost of commodities that farmers buy and second it tends to reduce the prices he receives for what he sells. Since the tax is a fixed percentage the increase in rates has been accompanied by an increase in tax.
Rail passenger revenues have also been reduced by the federal excise tax on transportation of persons. This increases the passenger service deficit which must be borne by freight shippers in the form of increased freight rates.

**Profits in Marketing**

As in other forms of business, profits are necessary in the marketing process to provide enough incentive for the necessary services to be performed and to cover the risk involved. Our economy is based on the profit system. The question is, however, how much profit is necessary. Are exhorbitant profits being taken?

The notion is frequently held that large profits are largely responsible for the present width of the spread and that the solution is merely to force middlemen to relinquish or reduce their profits.

It is true that at certain times on certain goods profits may constitute a large item. In some past years, for example, profits of the big tobacco companies and some dairy companies were very large.

In a period of declining farm prices there is normally a time lag before declines in farm prices are reflected in lower retail prices. For beef this time lag has usually been around three to five weeks in past periods. The recent decline however has seen a longer time lag than normal, although sizeable adjustments have now been effected in retail prices. The use of price controls may have been responsible in part for the abnormally long time lag as retailers in many cases tended to maintain higher average base period prices in case controls remained in effect.

But for every example of profits like these there are many other cases where profits have been very small or negative even in good years. Profit rates of food proces-
sors in 1951 ranged from an average of 1.4 cents per dollar of sales for the meat packing companies to 7.5 cents for the baking companies. After payment of income and excess profits taxes, these rates were reduced to 0.8 and 4.0 cents respectively.

Profits per dollar of sales is the means most companies use to report profits to the public. There is another way of reporting profits that should be recognized and this is the profit per dollar of investment. Although the rates of profits per dollar of sales for most firms were lower in the post-war than the pre-war period, increased sales have raised the ratios of profits to investments. Therefore the amount returned to stockholders for every dollar they have invested has increased above the pre-war period.

Estimates are made taking all goods into account, which indicate that the total profits all along the line from producer to consumer normally amount to about three to five cents out of the consumer’s dollar.

**Services Raise Charges**

A good many of the reasons for the high cost of distribution, about which consumers complain, lie pretty close to home in the buying habits of the consumers themselves. Many consumers are willing to pay higher prices in stores having an atmosphere of quiet elegance and luxury including air conditioning in the summer; some misuse the credit and return privilege; most consumers want a wide variety to choose from although real differences in brands may not be great. Consumers seem to desire buying in small lots, frequent delivering, hand-to-mouth ordering and more processing and packaging. Each one of these items may be small, but together they add up to a large portion of the total costs.

**Can Costs Be Reduced?**

The fact that middlemen’s profits are normally small shows that most of the intervening charges between producer and consumer are not profits but costs. Even if profits were entirely wiped out the margin would be reduced only between three and five cents. It would appear then that the best place to look for ways to reduce the width of the spread between farmer and consumer would be in a reduction of costs and an increase in the efficiency with which food is marketed and distributed. Although high marketing costs do not necessarily mean inefficiency or a poor distribution system, the field of cost reduction offers the best prospects for decreasing margins.

One of the plans offered to reduce marketing margins is an overall reorganization of the vast marketing structure with an eye to increasing efficiency and avoiding duplication of services. Although this idea has some merit it is not generally considered feasible as some control and administration would be required by a central authority. In a way competition would also necessarily be restricted.

Offering more promise in reducing margins is an examination and study of the individual segments of the market structure. Much progress has been made in increasing efficiency in the marketing chain through the findings of research. In this field lies the means of providing more and better ways to reduce costs.