

*Outputs: Impacts of Nontraditional Food Retailing Supercenters on Food Price Changes,* by T. Sharkey and K. Stiegert, FSRG monograph 20, February 2006. “**Food Pricing, Competition, and the Emerging Supercenter,**” by K. Stiegert and T. Sharkey, *Agribusiness* 23(3), in press.

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## **SUPER (MARKET) PRICES**

### ***Impact of supercenters and supermarket mergers on food prices***

Over the past 150 years, grocery retailing has undergone numerous major structural adjustments and technological changes. In the mid-1800s, chain grocery stores typically were 500-600 square feet and contained a limited assortment of goods. By 1941, thousands of chain grocery stores were replaced by supermarkets with very large floor designs (more than 5,000 square feet) and new advances in store shelving. Supermarkets consolidated power through mergers and strong barriers to entry. Antitrust cases brought against the industry attempted to redirect it to more competitive practices. Driven in part by economic recessions and energy crises of the 1970s, the warehouse supermarket format emerged, deemphasizing quality design and atmosphere. In the late 1970s, wholesale clubs and hypermarkets were introduced. Targeting customer clientele and combining wholesale and retail functions were key cost controls.

The latest major structural adjustment has been the advance of the supercenter. In 1988, the rise of the supercenter format began when Wal-Mart opened its first supercenter, which combines food retailing with general merchandising and pharmacy under one roof. Up to 40% of floor space is devoted to grocery items. Shortly thereafter Kmart and then Target opened supercenters, which meant that the nation's three largest general merchandisers had entered into grocery retailing. By the end of 2005, the number of non-traditional food retailing supercenters in the United States had increased to over 1,600 stores. Meanwhile, as supercenters took market share from traditional supermarket retailers, the supermarket industry responded with large mergers and acquisitions, creating fewer but larger firms.

### **PROFITS AND PRICES**

Researchers used data from 1993-2003 for 23 major urban areas to analyze the impact of supercenters and supermarket consolidation on food prices. Findings show that the marginal impact of the rise of supercenters and the time series effects of increasing supercenter market share did not have a significant impact on food prices in the metropolitan areas analyzed. This is significant in light of so many claims that supercenters raise the level of competition in retail markets and therefore should bring prices down. Findings also show that increased market concentration led to higher food retail prices. Only the rental rate was found significant in affecting prices among the major cost variables used in the study. It appears supermarkets do not change prices when other, perhaps less permanent, cost shocks occur.

In response to the emergence of supercenters, supermarkets may have regarded mergers as a way to increase buying power and achieve economies of scale. The project findings suggest that if supermarkets did obtain merger induced efficiency gains (i.e., scale economies), they did not pass the cost savings on to consumers. Analyzing data from the period of intensive merger activity (1998-2003), the researchers estimated a significant economic effect on households as a result of the mergers. Based on the average increases in competition over the study period, the econometric model showed the potential for an approximately \$5.9 billion increase in operating profit each year for food firms, while a typical family of four could expect an \$85 a year increase in home food purchases. The analysis shows that the increasing concentration of supermarkets leads both to higher profits *and* higher prices. If higher food at home purchase costs tend also to raise the costs for food purchased away from home, then the total impact of the mergers on food prices is likely to be even higher. Furthermore, the did not account for the added time and transportation costs of traveling longer distances to reach fewer supermarkets.

The study suggests that policymakers must pay closer attention to the alarming and increasing level of concentration in food retailing. This study indicates that imperfectly competitive price impacts are already present even while supercenters continue to enter and grow their market shares. Future studies should monitor the role of supercenters in the food retailing sector. Once the U.S. market becomes saturated with these stores, firms such as Wal-Mart will have to rely on same-store sales to demonstrate growth to stockholders. The temptation to exercise market power will likely be very strong, and prices could increase in ways not justified by costs. A trip to the grocery store could get expensive for families, and even a small rise in prices can be a heavy burden on poor families.

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**ISSUES:** The impact from non-traditional food retailers entering the food retail market through supercenters. The effect of supermarket mergers on profits and prices.

**FINDINGS:** Recent changes in the industry have muted competition effects. The rise of supercenters does not seem to increase competition nor have a significant impact on prices. Supermarket mergers increase supermarket profits, but prices to consumers also rise.

**OTHER MATERIAL:** Mayo, J.M. 1993. *The American Grocery Store: The Business Evolution of an Architectural Space*. Westport, CT: Greenwood Publishing Group, Inc. Foer, Albert A. 1999. "Food Retailing: The Two Faces of Supermarket Mergers." *American Antitrust Institute* 8-26-1999. Balto, D.A. 2001. "Supermarket Merger Enforcement." *Journal of Public Policy & Marketing* 20(1): 38-50.

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