



# FOOD MARKETING POLICY CENTER

## NEWSLETTER

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Department of Agricultural and Resource Economics  
College of Agriculture and Natural Resources  
University of Connecticut

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### Mission

The Food Marketing Policy Center conducts research on food and agricultural marketing and related policy questions. It facilitates research within the land grant university system by organizing meetings and conferences, by maintaining large scale data bases and by distributing publications. The general intent is to provide information that can contribute to improved performance of the food production and marketing system. Key users include farmer and consumer organizations, agribusiness firms, public agencies, state legislatures, and the U.S. Congress.

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### Newsmaker Interview: Professor Bruce Marion, University of Wisconsin-Madison

*by Ronald W. Cotterill*

- **You and your co-authors, Willard Mueller and Maqbool Sial, published a recent article in the *Review of Industrial Organization* titled, “Price Leadership on the National Cheese Exchange.” It was based on a study that you did of the National Cheese Exchange that has had consequences for the pricing of manufacturing milk in the U.S. dairy market. I wondered if you could explain to us, briefly, what it was your study showed and what happened after its release?**

- The study was of a classical thin market, the National Cheese Exchange.

- **What do you mean by a “thin market”?**

- A thin market is a market in which a very small percentage of the total volume of the product is traded on that exchange. In this case, less than one half of 1% of the total cheese manufactured in the U.S. was traded on the NCE in most years.

- **If the market is that small, why do we care about it?**

- The NCE, although very tiny, was used to price about 95% of all the cheese in the U.S. It was the national reference price that was used for formula pricing. When a very thin market has that type of leverage we become concerned about the potential for it being manipulated. The NCA was also thin not only in percentage terms but also in volume. In most weeks less than 5 blocks of cheese were traded. There were many weeks when no blocks were traded, and formula prices were set on bid and ask prices.

- **In 1988 the NCE price series suddenly sprang to life when compared to the CCC block cheese prices. What happened at that point on the market?**

- The market, essentially, became market driven. The support price prior to that time had been high enough so that it largely set the price for cheese. As support prices declined from 1984, it became more and more market driven. Note that one of the consequences of being market driven is that prices also become much more volatile.

- **So when the government program disappeared, how did the trading behavior on the market change?**

- The big difference was that the ability and incentive to influence or manipulate prices became much greater. We documented a change in trading behavior by Kraft in August 1986 and in the cases of some of the large cooperatives in 1987. Kraft, which had been more frequently a buyer on the NCE than a seller prior to August 1986, became exclusively a seller and remained that way through 1996 and, in fact, until the NCE was closed in May 1997.

- **The fact that Kraft was a seller on this market, so what?**

- Kraft produces about a third of their cheese needs, and they buy the other two thirds. The price of all of the bulk cheese that Kraft buys is based upon the NCE price. That is the incentive for Kraft to want the NCE price to be low.

- **So Kraft is selling a small amount of cheese on the Exchange in the hopes of driving the price down?**

- That is correct, but more specifically, they are influencing the cheese price cycle to keep

prices as low as possible for as long as possible. If the NCE was used simply as a residual market in which companies were getting rid of surpluses or going there to buy for shortages you would expect the companies that make bulk cheese, like the cooperatives, would mostly be sellers on the Exchange, and cheese markets like Kraft and Borden that bought bulk cheese would largely be buyers.

- **So the exchange actually is a price discovery mechanism, not a cash cheese market. People are trading on that market not because they want cheese; they are trading to discover or influence the NCE price.**

- That's right. Since August of 1986, the leading traders have reversed roles. Kraft and Borden have been predominantly sellers on the NCE and the cooperative manufacturers predominantly buyers on the NCE. The \$64 question is whether any firm is powerful enough to be able to influence that market; or conversely, was there a balance of power between the leading buyers and sellers so that even though Kraft may have wanted the cheese prices to be lower, they might not have been able to make it happen.

- **What's the answer to the \$64 question?**

- Our econometric analysis of the data and our analysis of motives and conduct led us to the conclusion that Kraft was, in fact, able to manipulate cheese prices lower, and that they were successful in doing so at times and that the other firms who may have wanted to counter Kraft's behavior were not successful in doing so.

- **So that's the study. We can read it to evaluate your analysis. What happened after your study went public?**

- It's a fascinating example of political economy. For the most part, the industry, the big players particularly, circled the wagons and defended the NCE. There were some of the firms who contacted us and said we agree with your study, but they would not issue public statements. Nobody wanted to be an enemy of Kraft. Farmers got up in arms. For a long time they have believed that the NCE was thin and was being manipulated.

- **So what did farmers do?**

- They were given the ammunition that they wanted to push for change. Groups of farmers held meetings. They went to Washington to meet with Secretary of Agriculture Glickman and with their legislators who began to push for change. In Wisconsin, the governor organized a task force on cheese and dairy pricing to investigate what should be done. It was initially heavily tilted towards the big cheese companies. Many dairy farmers attended those meetings, protesting that the task force was doing a white wash job. They became such a strong force that the governor finally had to respond to them. He added two or three more farmer members to the task force. It changed the overall end product of the task force and the recommendations that were made. Ultimately, Congressional Hearings were held in Washington by subcommittees of the House Agriculture Committee. The National Agricultural Statistic Service now collects prices from cheese factories around the country on their actual selling prices for bulk cheese. At the USDA level, changes have occurred in the way milk is priced and the prices that are included in that calculation. The industry finally decided regardless of how they felt about the Cheese Exchange, it was so discredited and subject to so many criticisms that they closed it in May of 1997. An alternative cash market on the Chicago Mercantile Exchange opened up. Thus the

private unregulated NCE was replaced with a public exchange fully regulated by the CFTC.

- **Do you think it is an improvement?**

- At this point it's probably too early to know whether it's an improvement or not. I think it still may be thin; it still may be subject to some of the same problems that the NCE had.

- **Is formula pricing still being used?**

- Yes, 90-95% of cheese is being priced off the Chicago Mercantile Exchange price.

- **The USDA prices that are being collected, are they being used by anyone?**

- I believe they are being used mainly, at this point, for calculation of the basic formula milk price used in milk marketing orders.

- **So they are not using the Chicago Mercantile Exchange cheese price in the basic formula price?**

- Yes. That's my understanding.

- **But, in fact, those country cheese prices are priced off of the MERC, so the MERC still has influence?**

- That's the problem.

- **Is Kraft still a major seller on that Exchange?**

- We don't know. There's some positives and negatives with the Chicago Mercantile Exchange. One of the negatives is that trading is anonymous. There's no information provided on who is trading or how much. So we don't know whether Kraft accounts for 100%, 50%, 10% or what percent of the trading.

- **Then you don't know which side of the market Kraft is on?**

- No, we don't. The trading does have to go through a broker. One of the potential problems with the NCE, that firms could signal one another through their trading actions, may be more difficult now because trading goes through brokers. Making trading anonymous has some plusses and minuses.

- **What other option would you consider?**

- I think one of the potential alternatives that looks very attractive to me is a national electronic computerized auction. Given the nature of the product, the fact that the industry is accustomed to trading in standardized 40 pound blocks and 500 pound barrels, and given the growing geographic decentralization of cheese manufacturing, a national electronic exchange, to me, makes a lot of sense. I think it would have had a chance for increasing volume quite a bit. But it would have also been a much bigger change for the industry, and that may have been one of the reasons they didn't do it.

- **Thank you, Bruce.**

Editor's Note: When Willard F. Mueller, Bruce W. Marion and Maqbool H. Sial completed their multi-year study of the National Cheese Exchange at the University of Wisconsin, Philip Morris, the parent company for Kraft General Foods, threatened the authors with a libel suit if they distributed it to the public without first giving Kraft an opportunity to review and respond to it. When the University, and the state of Wisconsin who commissioned the study, supported their right to publish, Philip Morris backed down and subsequently hired Professor Bruce Gardner, University of Maryland, as a consultant to critique the study. As Oprah says, "Free speech rocks!"

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### AGRIBUSINESS JOURNAL TRANSITION

Ron has been selected as the editor of *Agribusiness* and is forming a new editorial board for the Journal. Harry Kaiser, Cornell University, and James MacDonald, ERS/USDA have agreed to serve as associate editors. Since the Journal is no longer associated with the International Agricultural Marketing Association (IAMA), it will renew its focus upon agribusiness economic and policy research. The Journal will retain its international scope.

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**General Announcements**

Li Yu Ma, a recent Ph.D. in Agricultural and Resource Economics at the University of CT who worked in the Policy Center, has been accepted in the MBA program at Yale University.

The Japanese are translating chapters from four NE-165 books; *The Economics of Food Safety, Valuing Food Safety and Nutrition, The Economics of Reducing Health Risks from Food, and Strategy and Policy in the Food System: Emerging Issues*. Also, Cotterill, R.W. "The Food Distribution System of the Future: Convergence Towards the U.S. or U.K. Model?" *Agribusiness* 13(2): March/April has been translated into Turkish.

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**Food Marketing Policy Center on the Web**

Don't forget to check out our ever-expanding Policy Center Home Page at:  
<http://vm.uconn.edu/~wwware/FMKTC.html>

Our web site contains a continuously updated list of publications available through the Policy Center. Some publications may be printed directly from the web site. In addition, we are currently producing an archive of the Food Marketing Policy Center Newsletters. These archived newsletters will be available in PDF format for printing directly from the web site. Consult the web site for details and availability.

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**NE-165 Conference Announcement**

NE-165 will hold an international conference on "The Economics of HACCP, New Studies

of Costs and Benefits" June 15-16, 1998 in Washington, D.C. This conference is organized by the NE-165 Regional Research Committee on Private Strategies, Public Policies, and Food System Performance. It is sponsored by Farm Foundation, the Department of Resource Economics at the University of Massachusetts and the Food Marketing Policy Center in the Department of Agricultural and Resource Economics at the University of Connecticut. Research will be presented on new approaches to evaluating the costs and benefits of HACCP in food industries, including choosing cost-effective points of intervention, managing risks and transactions in the food chain, and applying HACCP to food retailing. In addition to firm and industry level studies, new research on the distribution of costs and benefits from HACCP will be presented. Papers include experiences from the U.S., Europe, Latin America, and Japan. Dr. Catherine Woteki, USDA Undersecretary for Food Safety, will make the keynote address. For more information and registration materials, please contact Barbara Talenda, Conference Administrator, Dept. of Resource Economics, Box 32040 University of Massachusetts, Amherst, MA 01003-2040, Tel (413) 545-5732, email [talenda@resecon.umass.edu](mailto:talenda@resecon.umass.edu).

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**Activity Report****Julie Caswell**

(University of Massachusetts)

Julie presented an invited paper on "Valuing Food Safety and Nutrition" at the Annual Conference of the Australian Agricultural and Resource Economics Society, Armidale, Australia, January 1998. She also consulted on food safety issues with the New South Wales Department of Agriculture.

Julie is currently chairing the Awards Committee of the American Agricultural Economics Association.

Julie organized, served as chair, and was a speaker at a mini-symposium/discussion group (3 sessions) on "Food Quality Regulation in International Markets," Triennial Conference of the International Association of Agricultural Economists, Sacramento, CA, August 10-16, 1997.

Julie presented a seminar, "The Regulatory Environment in Food Markets" at the Seminar on Economic Policy for the Agribusiness Sector in the Transition Economies, Economic Growth Center, Yale University, July 24, 1997.

#### **Ronald W. Cotterill**

*(University of Connecticut)*

Ron provided economic analysis for the milk workers unions in New York City and northern New Jersey who are defendants along with the leading milk processor, Tuscan and other milk processors in an antitrust case that charges them with conspiring to monopolize the NY/NJ milk processing market. The plaintiff is Farmland Dairies.

Ron is providing economic analysis for American Media-Retail Marketing Network, the plaintiff in a monopolization law suit against Actmedia, a subsidiary of News America. The case centers on in-store coupon distribution.

Ron took the lead on revising and expanding a paper, jointly authored with Bill Putsis (London Business School) and Ravi Dhar (Yale) on national brand private label pricing for the *Journal of Business*.

Ron attended and delivered a plenary session paper at the "International Conference on

Vertical Relationships and Coordination in the Food System," Piacenza, Italy, June 1997.

#### **Michael Lubatkin**

*(University of Connecticut)*

Michael continues research on strategic management issues in the food system. Bill Schultze, assistant professor of Management, and Avinash Mainkar, Ph.D. candidate, are collaborating with him.

#### **Everett Peterson**

*(Virginia Tech)*

Everett and Ron are working on oligopoly price reaction models. They also are commencing work on milk price transmission models with an empirical focus on the Northeast Dairy Compact.

#### **William Putsis**

*(London Business School)*

Bill continues work on a project with Ron and Larry Haller (USDA) on private label modeling strategies in food industries.

Bill Presented "Category Expenditure, Promotion and Competitive Market Interaction: Can Private Labels Really Expand the Pie?" at INFORMS, Dallas, October 1997.

Bill presented "On the Competitive Interaction Between Private Label and Branded Grocery Products," at Columbia-NYU-Wharton-Yale Annual Conference, May 1997.

Bill presented "The Competitive Interaction between Private Labels and Branded Grocery Products: Can Private Labels Expand the Pie?" at the Marketing Modeler's Meeting, BBDO, New York, April 1997.

**Kellie Raper***(University of Massachusetts)*

Kellie presented "Testing for Monopsony Power in Multiple Input Markets: A Nonparametric Approach" in a selected paper session at the American Agricultural Economics Association annual meetings in Toronto, Canada, July 27-30, 1997.

Kellie received Honorable Mention in the American Agricultural Economics Association's Outstanding Ph.D. Dissertation contest for her dissertation, "Empirical Measurement of Market Power". The award was announced at the American Agricultural Economics Association meetings in Toronto, Canada, July 29, 1997.

Kellie continues work on research project, "Empirical Measurement of Monopsony Market Power Exertion in the Beef Packing Industry" with H. Alan Love, Diana M. Burton, and C. Richard Shumway of Texas A&M University. This project is funded by USDA Grain Inspection, Packers and Stockyards Administration.

**Richard Rogers***(University of Massachusetts)*

Richard is assisting Andy Jermolowicz of the U. S. Department of Agriculture/Cooperative Marketing Division in updating their popular publication on "Cooperative Brands." A survey of agricultural marketing cooperatives is being done to gain information on how they market their processed products.

Richard and Jeff Royer, University of Nebraska, have been busy editing a book based on our June 1995 conference on "Vertical Coordination in the Food System." They have signed a contract with Ashgate Publishing Limited, and the book is now

being type-set and should be available by early spring 1998.

Richard presented a co-authored paper (with Jennifer Lewis, a former graduate student, and Rich Sexton of UC-Davis) on "A Comparison Between the Advertising Strategies of Agricultural Marketing Cooperatives and Investor-Owned Firms in Food Processing," at the AARES Annual Conference at the University of New England, Armidale, NSW, Australia, January 1998.

Richard is working with co-authors Tihomir Andonov and Bernie Morzuch on revising their paper on "Market Share, Retail Price, and Cooperatives in the Margarine Industry, 1992," which was accepted, subject to revisions, by the *Journal of Cooperatives*.

**Kathy Segerson***(University of Connecticut)*

Kathy recently completed a research report on "Mandatory Versus Voluntary Approaches to Food Safety."

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**Data Corner****Recent acquisitions include:**

The Food Marketing Policy Center has purchased additional ready-to-eat breakfast cereal scanner data from Information Resources, Inc. (IRI). The data consists of monthly observations, 1993 through 1997, for 15 market areas and for the entire U.S.

Trade Dimensions 1998 *Marketing Guidebook*.

Progressive Grocer 1997 *Market Scope and Mid-Year Update*.

Contact Andrew Franklin (860) 486-2826 for a complete listing of data and reference works available.

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### **Food Marketing Policy Center Publications Catalog**

We have updated the list of the publications that are available through the Center. Call (860) 486-1927, write for a copy, or print it from our Home Page:

<http://vm.uconn.edu/~wwware/FMKTC.html>

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### **Recent Publications and Papers**

Barrett, James and Kathy Segerson. "Prevention and Treatment in Environmental Policy Design." *Journal of Environmental Economics and Management*, June 1997, 33(2):196-213.

Caswell, Julie A. "Rethinking the Role of Government in Agri-Food Markets." *American Journal of Agricultural Economics*, May 1997, pp. 651-656.

Caswell, Julie A. Rapporteur's Report for Discussion Group/Mini-Symposium on *Food Quality Regulation in International Markets*. XXIII International Conference of Agricultural Economists (International Association of Agricultural Economists), Sacramento, California USA, August 10-16, 1997.

Caswell, Julie A. "What Labels Tell Us About How Foods are Produced." University

of Connecticut, Food Marketing Policy Issue Paper No. 16, October 1997.

Caswell, Julie A. and Ronald W. Cotterill, eds. *Strategy and Policy in the Food System: Emerging Issues*. University of Connecticut, Food Marketing Policy Center, 1997.

Caswell, Julie A. and Spencer J. Henson. "Interaction of Private and Public Food Quality Control Systems in Global Markets." In *Globalization of the Food Industry: Policy Implications*, ed. R. J. Loader, S. J. Henson, and W. B. Traill, 1997, pp. 217-235. Reading, UK: Centre for Food Economics Research, University of Reading.

Caswell, Julie A. and Jaana K. Kleinschmit v. L. "Using Benefit-Cost Criteria for Settling Federalism disputes: An Application to Food Safety Regulation." *American Journal of Agricultural Economics*. 79 (February 1997): 24-38.

Connor, John and Everett Peterson. "Market-Structure Determinants of National Brand—Private Label Price Differences of Manufactured Food Products: Reply." *Journal of Industrial Economics*, June 1997, 45(2):225-226.

Cotterill, Ronald W. "The Economics of Private Label Pricing and Channel Coordination," plenary session paper presented at the International Conference on Vertical Relationships and Coordination in the Food System, Piacenza, Italy, June 12-13, 1997.

Cotterill, Ronald W. "The Performance of Agricultural Marketing Cooperatives in Differentiated Product Markets," *Journal of Cooperatives*, 1997, 12:23-34.

Cotterill, Ronald W. and Lawrence E. Haller. "An Econometric Analysis of the Demand for

RTE Cereal: Product Market Definition and Unilateral Market Power Effects." University of Connecticut, Food Marketing Policy Research Report No. 35, September 1997.

Hooker, Neal H. and Julie A. Caswell. "International Trade Impacts of Quality Management Systems for Food." Poster paper presented at the Institute of Food Technologists Annual Meeting, June 1997.

Lewis, Jennifer. "A Comparison Between the Advertising Strategies of Agricultural Marketing Cooperatives and Investor-Owned Firms in Food Processing," a thesis submitted August 1997. Jennifer's committee was Richard Rogers (chair), Kellie Raper, and Cleve Willis.

Mainkar, Avinash. "Analysis of Market Power in the Food Industry." Paper presented at the Eastern Academy of Management, 34<sup>th</sup> annual meeting, New Jersey, 1997.

Mojduszka, Eliza M. "Manufacturers' Responses to New Nutrition Labeling Regulations." Ph.D. dissertation, University of Massachusetts at Amherst, 1997.

Putsis, William, "An Empirical Study of the Effect of Brand Proliferation on Private—Label National Brand Pricing Behavior," *Review of Industrial Organization*, 12(3), June 1997, 355-371.

Putsis, William and Ravi Dhar. "Private Labels vs. National Brands: The Many Faces of Competition," accepted, *Marketing Letters*.

Roberts, Tanya, Roberta A. Morales, C.-T. Jordan Lin, Julie A. Caswell, and Neal H. Hooker. "Worldwide Opportunities to Market Food Safety." In *Government and the Food Industry: Economic and Political Effects of Conflict and Cooperation*, ed. T. L.

Wallace and William R. Schroder, 1997 pp. 161-178. Dordrecht, Netherlands: Kluwer Press.

Rogers, Richard. "The Role of Cooperatives in Increasingly Concentrated Markets" in *Proceedings of a Symposium on Cooperatives: Their Importance in the Future Food and Agricultural System*, edited by Cook, Togergson, Sporleder, and Padberg, sponsored by National Council of Farmers Cooperatives and the Food and Agricultural Marketing Consortium, 1997, p. 49-65.

Rogers, Richard. "Broilers, Differentiating a Commodity" in *Industry Studies* edited by Larry Deutch, M. E. Sharp, 1998.

Steahr, Thomas E. "An Estimate of Foodborne Illness in the Elderly Population of the United States, 1987-1993." *International Journal of Environmental Health Research*, Vol. 8, 1998, forthcoming.

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