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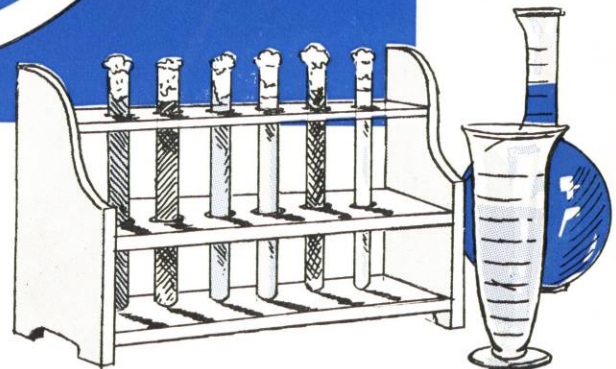
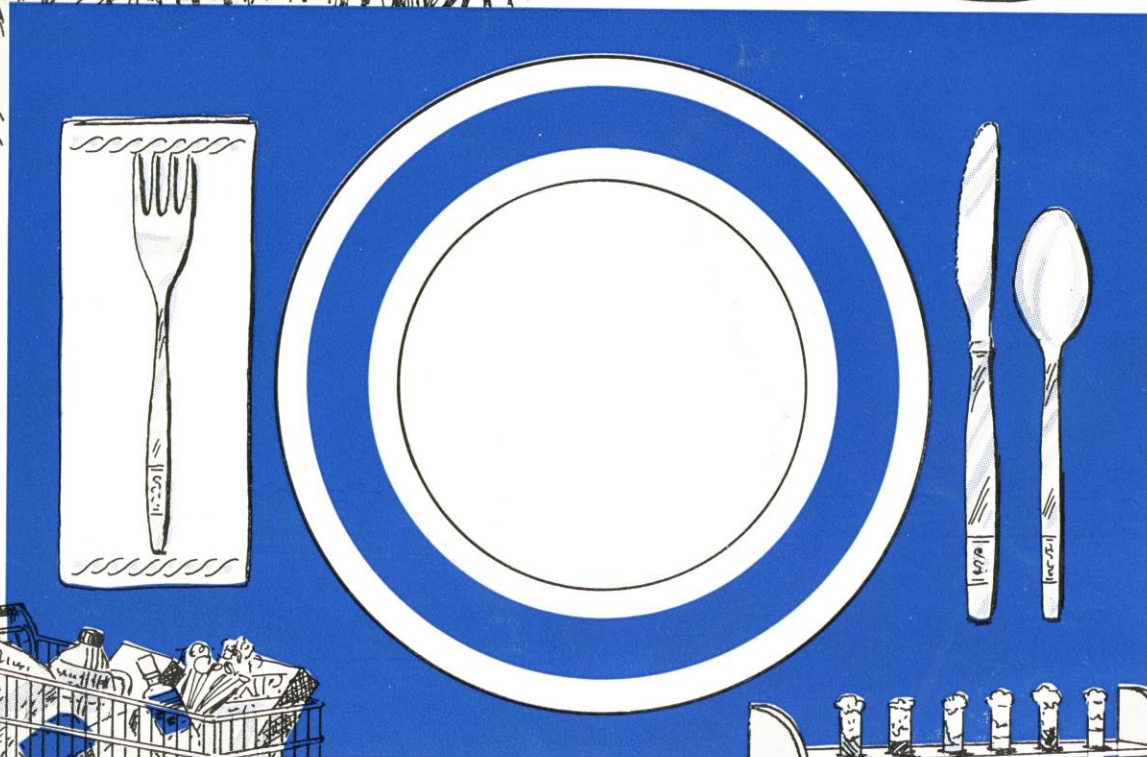
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management adviser

July-August, 1972

Food: A Review of the Industry



Pollution control: A corporate responsibility



Pollution and pollution abatement have become important aspects of every business. They affect budgets, profit and loss, position in the community, corporate image, even the price of stock in some cases.

Pollution is a now problem that is receiving now attention from astute businessmen. Water treatment plants, fume scrubbers and filtration systems, land reclamation, plant beautification, litter prevention, employee education programs, are all types of things industry is doing to help in the pollution fight.

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against
birth
defects...”**

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THIS SPACE CONTRIBUTED AS A PUBLIC SERVICE BY THE PUBLISHER

Neil Doppelt • Marketing Information: Three Squares a Day Required for the Food Industry p. 17

The internal pressures for cost control and the dynamic competitive activity of the food industry have convinced many marketing managers that improved information systems are well worth the investments

they require. Two modules in a marketing information system with payoff potential, salesforce utilization and promotion planning, are given as examples of what industry leaders are using.

Harold W. Fox • Food Retailing Needs a Systems Approach. p. 24

The new complexities of modern supermarket retailing separate it more and more from the halcyon days of the small proprietor. While achieving record-high gross margins, the stores concurrently experience record-low net margins. Any relatively minor change

jeopardizes the net or, at least, makes it swing wildly. The author maintains some of the retailers' questions can only be handled via a systems perspective that views the problems encountered from manufacturing to final disposal as interrelated.

Robert M. Smith • Food: Its Past Victories, Its Current Problems p. 33

In the 30 years since World War II the history of the food industry has abruptly changed directions. A brief overview of the industry's history within that

period is given as well as discussion of the Government regulations that are becoming more and more important to its future growth.

Alfred N. Califano and Allen Weiss • The Turbulent Food Service Industry p. 38

In the restaurant business the profit squeeze induced by inflation is aggravated by three identifiable factors: consumer resistance to price rises, labor costs, and high rentals. Institutional feeding is affected by analo-

gous problems. Convenience foods are playing an important part in solving the food service industry's problems, in part because these products embody a systems approach, the authors say.

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management adviser

(formerly *Management Services*)

Louise H. Dratler • Food Manufacturing: Products, Problems, Protests p. 44

The food manufacturer has problems: Not only does he have to contend with the ordinary problems of business, but he has Mother Nature, the FTC, and

irate consumerists giving him gray hair. The manufacturers say they are facing their environment with better marketing, packaging, and products.

Michael H. Hagler • From Merchants to Merchandisers p. 48

This is a case history of how a CPA firm was able to help a client do what was formerly thought to be impossible, determine future demand in the food business. A small importing company was becoming a major

bridge between manufacturers abroad and food processors in this country; the only problem was the company was growing so fast it didn't know how to forecast demand for the goods it was importing.

Jerry H. Loyd • Marketing for Food Manufacturers: The Role of the Food Broker p. 54

Put the General Foods Corporate Vice President of Sales together with the Executive Vice President of M. W. Houck Corporation, food brokers, and see if it is possible to come out with a definition of what a

food broker does. That is exactly what this author did and the result was not only a definition, but a two-sided picture of the future of food brokers, manufacturers, retailers, and consumers.

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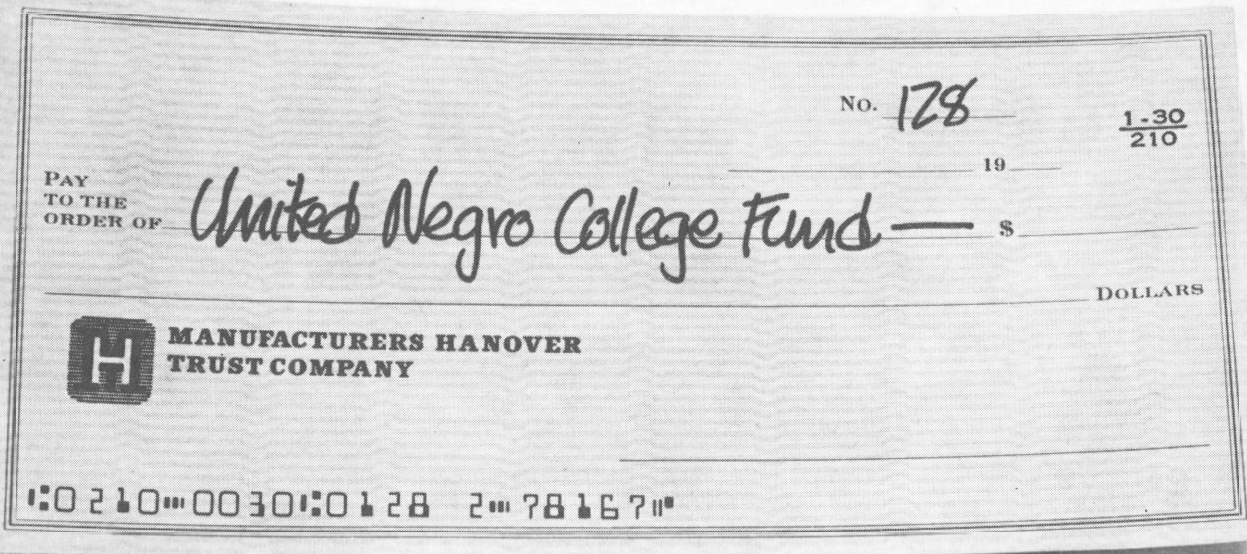
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people, events, techniques

Marvin Stone Suggests at Dallas Computer Conference that CPAs Publicize Their Specialties to Offset Competition from Commercial Firms

Services that have traditionally been offered by CPAs are now being offered by banks, finance companies, chain retailers, insurance companies, tax return preparers, and others, Marvin L. Stone, CPA, chairman of the AICPA committee on the nature of accounting services, said May 24.

Mr. Stone, a past president of the AICPA, spoke about his committee's findings at the AICPA Annual Conference on Computers and Information Systems, held May 23-25 in Dallas. (A report on the conference proceedings will be carried in the next issue of this magazine.)

"The days ahead are murky for

CPAs," Mr. Stone said. "CPAs will be faced with a great deal of new competition. These competitors will be unhindered by ethical restraints against solicitation, advertising, competitive bidding, organizational structure, and non-professional associates.

"Some competitors, notably banks, will have a competitive edge because they offer a service package which includes loans, record-keeping, consulting services, and perhaps tax services as well."

Mr. Stone urged the profession to be responsive to its new competitive environment. One of the suggested changes in the profession that he believes deserves some

new consideration is the recognition of CPA specialties.

"Much consulting work goes to non-CPA firms partly because CPAs may not let their specialty be known," Mr. Stone observed. "Even other CPAs have no way of knowing where to turn for specialized help. Unless a CPA has accidentally read a paper or heard a speech by a colleague, he has no way of determining that colleague's area of expertise."

He pointed out that even the legal profession is taking tentative steps toward the recognition of specialties.

"The AICPA or an affiliate could accredit specialists. Without some

accreditation mechanism, specialists would be self-designated. Once the mechanism has been established by which specialists can be accredited, ethical rules should be amended to permit CPAs to disclose their specialties."

"The following benefits should be derived from the recognition of specialization," Mr. Stone explained, "1—Better service to the public; 2—More referrals among CPAs; 3—An improvement in the CPA's competitive position vis-a-vis non-CPAs."

Mr. Stone was careful to state that this was just one idea that needed thought and discussion, and should not be viewed as an official recommendation of his or his committee.

FEI Survey Shows Nearly Half of Manufacturers Use CPAs as Consultants

Forty-one per cent of the manufacturing companies answering a recent Financial Executives Institute questionnaire said that they employed their CPA firms for management services activities.

The survey's findings were presented in the April, 1972, *Financial Executive* by George Hobgood and Joseph A. Sciarrino of the FEI.

Of the 797 U.S. manufacturing companies studied, 26 per cent felt that a conflict of interest between the CPA firm's audit and management advisory services function existed or might exist. Thirty-two per cent felt there was no possibility of a present or potential conflict of interest. The other companies did not consider the question.

The FEI researchers point out that there is a significant relationship between the size of the company and the way it views the CPA's potential conflict of interest. Larger companies tended to have more confidence in the CPA firm's integrity.

Of those companies that felt there could be a conflict of interest, 80 per cent had sales of less than

\$500 million a year, 65 per cent had sales of less than \$250 million, and 47 per cent sales of less than \$100 million. In comparison, 90 per cent of the companies making over \$1 billion a year said they felt there was no conflict of interest.

Respondents were asked by the FEI questionnaire to explain why they felt the way they did about the CPA's potential conflict of interest. Some of the responses reported by Messrs. Hobgood and Sciarrino were:

"The question revolves on the integrity of our CPA firm, which we hold in high esteem. However, this integrity depends on how important each member of the audit firm's staff considers it to be, and therefore there does exist the possibility of weak links in this chain," one respondent wrote.

Another said, "Internal separation within the CPA firms in terms of specific engagements prevents conflict of interest. The increased knowledge of the client increases the firm's ability to perform its public auditing responsibility."

A third responded, "Anything that brings our auditors too close to us will tend to negate the all-important attest relationship."

The FEI survey also examined audit fees. They found the average audit fee paid by U.S. manufacturing companies in 1971 was .04 per cent of annual sales volume. A sampling of Canadian manufacturing companies found that for the same services they paid .02 per cent of their annual sales volume.

Another fact uncovered by the FEI survey was that only 10 per cent of the responding U.S. manufacturing firms had changed CPA firms in the last three years. Those that did change either wanted to go from a local to a national CPA firm or to consolidate all audits in one firm, the FEI reports.

Messrs. Hobgood and Sciarrino suggest a similar survey from the auditor's point of view might be useful in bringing about a dialogue that could improve management-auditor relationships.

IBM Launches Program To Protect Access To 'Sensitive' Data

IBM has embarked on a five-year \$40 million program to give the computer user the means to control access to sensitive data in his system.

Addressing the Spring Joint Computer Conference in Atlantic City, May 16, IBM Chairman of the Board T. Vincent Learson explained, "This access will be controlled by 'locks and keys' in the system. Users will be able to set their own thresholds according to their needs.

"In addition, of course, these systems will also include audit trails and the most advanced forms of authorization we can devise."

Four test centers

Four data security study centers are planned, three in "highly qualified user installations" and one in IBM, Mr. Learson said. The security system will be tested in actual working situations.

Some of the things the IBM researchers will try to find out are: What is a fair measure of how secure the system is against penetration? What logical and physical facilities should be taken into account? What difference does environment make (i.e., time sharing, data base, commercial or government users)? How can the levels of authorization be handled? What constraints will data security place on individuals working with the system? What will the security program mean to the cost and performance of the system?

High-end users first

"We want to give high-end users security options that are as near as we can come to the limit of the art," Mr. Learson said. "Where possible, we will incorporate these findings into the middle- and lower-end of the line and to program

products. Meanwhile, we shall maintain a custom security capability for special security needs."

The corporation intends to offer users as low or as high a threshold of security as they think they need.

"Obviously, we are never going to build a system that is absolutely crackproof," Mr. Learson acknowledged. "But just as banks have come a long way since the days of Jesse James, so can we go a long way, beyond where we are now—and at a cost that will make sense."

He said study sites will be free to share with others the understanding the researchers will reach on data security requirements.

Westinghouse Shows Minicomputer Process Control System

A minicomputer process information system has been developed by Westinghouse. The corporation says its Prodac Process Information System is a "do-it-yourself" system because it does not require a computer operator or technician to install or operate it.

Prodac can give the user a continuous record of production, quality, or environment by employing the plant's existing instruments and a Westinghouse 2500 minicomputer.

System price: \$23,000

Westinghouse says the system can warn of potentially dangerous situations before they occur; reduce the costs of raw material, energy, labor, and scrap; plan maintenance on a scheduled rather than emergency basis; monitor product and environmental quality; and help new employees operate as though they were experienced.

The purchase price of the basic Prodac Process Information System starts at \$23,000.

More information on the system is available from the Westinghouse Electric Corporation, Westinghouse Building, Pittsburgh, Pa. 15222.

Technical Problems Solved, Organizational Difficulties Remain in Large Data Base Systems, Says Diebold

Organizational, rather than technical, problems remain as the key issues to be resolved in the establishment of a large data base system, a recent study by the Diebold Research Program concludes.

The Diebold researchers found, "For many companies the 'total integrated common data base' approach of the 1960s has turned out to be a dramatic mistake! The concept involved a top-down design methodology embracing every information need conceivable. This technique has fallen into disfavor as organizations found it difficult, if not impossible, to implement."

Companies with highly autonomous divisions appear to the researchers to be poor candidates for data base systems that cross divisional boundaries. However, the Diebold group says this situation depends on the amount of interdivisional management cooperation fostered by corporate philosophy and management style.

Similar products important

"Companies whose divisions have common or similar products or overlapping customers appear to be better candidates for transdivisional product- or market-oriented data base systems than those with little interdivisional commonality," the Diebold study states.

"To attempt the design (let alone implementation) of any functional product data base that crosses divisional boundaries in a highly diversified company would be wasted effort," the study advises.

Centralized planning urged

However, this does not mean that individual corporate units should go their own way in EDP development. Diebold believes that data processing is a *corporate* re-

source and must support the entire corporation. For consistency of development efforts and cost-effectiveness of control, data base planning and coordination must be centralized, the study maintains.

Shared responsibility suggested

Funding for the data base can be divided so that development is financed on the corporate level and operation and applications on the division level but shared, where appropriate, among divisions and top management, Diebold states.

The report suggests that for each functional data base a user "Prime Responsible Authority" (PRA) and a "Data Base Administrator" (DBA) be appointed.

The PRA determines information content, identifies levels and privileged classes of users, and acts as the authority on the functional area to be served. Each PRA reports to his user management, Diebold explains.

The DBA is the technical feasibility adviser. The DBA creates and maintains the data base structure with its supporting library and documentation and ensures that security and backup provisions are made. Diebold advises that the DBA report to the management level above the data processing division since he has full and final responsibility for technical review of the data base system and all data processing personnel report directly to him on matters involving that system.

Through appointing a PRA and a DBA the responsibility is shared among user organizations and the EDP organization, Diebold believes.

The Diebold Research Program is an industry-sponsored study conducted by the professional staff of The Diebold Group, Inc., a management consulting firm.

Definite Milestones Essential for Software Development, ADL Says

At every stage of software development, identifiable milestones should be built into the project so that progress can be objectively reviewed, ADL Systems, Inc., suggests in a recent issue of its newsletter, *The Casebook*.

Documenting and reporting on small-unit achievements also makes system development more "people-independent," ADL says.

"By breaking tasks into identifiable segments—no one of which represents more than 2-4 per cent of the total—you can avoid the trap of thinking that because 80 per cent of the budget has been expended, 80 per cent of the work has been done," the newsletter says.

Another important technique in software development is the involvement of the user department, or departments, with the data processing department while development is in progress. "It is crucial that the data processing department finds out exactly what the user wants, specifies it to his satisfaction, and gives it to him," ADL advises. "In this process, user involvement is mandatory. Have him review specifications, look at sample outputs, and stay informed."

ADL maintains that software has matured as a discipline and, therefore, is as manageable as any other production system. Good program development should not be treated as a miracle, as some senior managers seem to believe, but should be expected.

"A preferred attitude is one in which performance to stated standards is expected, and that deviation from those standards is a cause for concern and not an expectation," ADL states.

Two of the most challenging areas for software management, ADL believes, are data communications and data management.

The principal problems in data management software center around file structuring, devising updating and retrieval modules, and in throughput and recovery needs, ADL finds.

In data communications, clients have expressed their concern to ADL about the extravagantly high cost, in terms of resource requirements, of software for message handling and support functions.

ADL Systems, Inc., is the software subsidiary of Arthur D. Little, Inc. ADL is located in Cambridge, Mass.

Raising Productivity To Be Theme of Munich Work-Factor Conference

Increasing productivity is the theme of the Fourth International Work-Factor Conference to be held in Munich, Germany, October 26-28. The conference is a post-congress activity of the Sixteenth CIOS World Congress, to be held October 23-26 in Munich.

The productivity conference draws its name from the Work-Factor System of productivity improvement which was developed by Joseph H. Quick, chairman of Science Management Corporation, Moorestown, N. J.

"The Work-Factor Conference is planned to come to grips with the problems of and the solutions to productivity more effectively than any other conference of which I'm aware," Mr. Quick said. "The program has been planned to give participants practical solutions that they can take home and put to use in their facilities."

The conference will be simultaneously translated into German, French, and English. The registration fee is 300 Deutsche Marks, or approximately \$100. More information about the Work-Factor Conference is available from: Work-Factor Associates of the East Coast, Fellowship Road, Moorestown, N.J. 08057.

Missouri City Police Use Computer Terminals In Squad Car Fleet

Kansas City, Mo., police recently completed a successful field test of a squad car message terminal designed by IBM.

"Our four years of computer experience have shown us the officer in the field is safer and more effective when we give him more information quickly and clearly," said Clarence M. Kelley, chief of the 1,300-man Kansas City Police Department.

A patrolman who spots a suspicious vehicle can type its license number on the IBM squad car terminal. The terminal is linked to an IBM System/370 or 360 which searches its files to see if the car has been involved in a crime. If it has, the terminal can flash a "proceed with caution" warning and print out a message if the car's driver is believed to be armed and dangerous. If the patrolman needs assistance he can call for it with a single keystroke.

The terminal also frees the patrolman from taking notes, such as missing child descriptions, and instead transmits information in computer-usable form.

Efficiency vastly increased

According to V. R. Macdonald, vice president of public sector industry operations for IBM's data processing division, "The test system at Kansas City quickly produced the vital information a policeman needs to do his job efficiently. More importantly, this same data helps insure his personal safety.

"At the same time, the system releases police dispatchers from handling inquiries by radio. The dispatcher can then concentrate on taking telephone calls from the public for police service."

In Kansas City it was found that squad cars with the test terminals averaged 200 inquiries per day during a 19-day test period. The

police department's other 325 cars averaged less than 20 inquiries daily.

The Kansas City police department has also been using IBM's Law Enforcement Manpower Resource Allocation System (LEM-RAS) that helps project when and where police will be needed within the city.

"We know that metropolitan police solve two-thirds of the crimes in progress they can respond to within two minutes," Police Chief Kelley said. "But when response is delayed five minutes or more, police solve less than one crime in five.

"The LEMRAS program helps us deploy our patrol cars so they can respond to crime reports as soon as possible."

The mobile terminal system for a police department with 300 squad cars will cost about \$1,270,000.

Supervisor—Personal Relationships Filmstrips Offered by Publisher

"The Supervisor and Interpersonal Relations," a filmstrip series, is available from Addison-Wesley Publishing Company, Inc., Reading, Mass. 01867.

The series consists of five color filmstrips designed to "help supervisors recognize the causes of interpersonal conflict and to provide them with some proven techniques for reducing and overcoming the conflict situation," Addison-Wesley explains.

The titles of the filmstrips are: "General Problems of Interpersonal Conflict"; "Improving Relationships Between Peers"; "Improving Attitudes Toward Subordinates"; "Improving Attitudes Toward Supervision"; and "Reducing Conflict in the Organization."

Filmstrips, narration records, and a leader's guide are \$225. Individual filmstrips are available at \$50 each.

Most Small Companies Misuse Human Resources, J. H. Cohn Suggests; Recruiting Policies Faulted

The typical small company under-utilizes its human resources, observes J. H. Cohn and Company, a Newark CPA firm, in a recent issue of its newsletter, *Time and Tide*.

"Though many of these [personnel] problems are thought to stem from a genuine inability to attract or afford top talent, it is far more likely that they stem from the traditional adherence of small business managers to the view that manpower must be bought as cheaply as possible," the firm states.

"The evidence is now fairly complete that the small firm will profit by spending money wisely on good personnel at every level," Cohn advises.

Some of the reasons for the personnel problems in small businesses are: Small companies must deal with most of the functions big ones do, but they have less people to handle them; small companies tend to invest less of their resources in development of technical and managerial skills; small companies have comparatively low managerial turnover; small companies are more easily dominated by one strong personality, often the founder.

Cohn suggests that small businesses get to know the capabilities of their employees. "Correct employment and manning is, in the last analysis, strictly a function of adequate knowledge of the jobs to be filled and the people available to fill them," the firm states.

"Three measures capable of reducing the risks in running out of talent in small firms are: (1) to develop and maintain accurate job specifications for each of its key positions; (2) to commit as many of the company's formal procedures to documentary form as practical and (3) to identify, give recognition to, and lay plans for raising the level of under-utilized talent."

The CPA firm does not claim these measures will solve the retention/replacement dilemma of small companies, but it says they will aid in forestalling the departure of high-potential employees and breaking in executives.

A body of clear-cut recruiting and hiring policies should be developed by the small business and kept at hand. In doing this, the company should reconcile standards, biases, and myths that vitally affect recruitment, Cohn says.

The tendency to search for hirables on the basis of how long they will stay with a company is one of the standards that should be done away with, the firm says. "This prejudice should be junked; people should be hired because they are truly needed, and can produce the results desired, not because they can be expected to stay forever."

Turning to the matter of training, the CPA firm states that lower echelons should be allowed to make operating decisions within stated policy guidelines, to prepare them for increased authority. In-house training conducted by outside specialists is also advised.

Executive Attrition Causes Half All Mergers To Miss Financial Goals

Fifty per cent of all mergers and acquisitions do not realize their anticipated profits within originally projected time spans, a recent survey conducted by Einstein Associates, a New York management consulting firm, finds.

One reason for this is a frequent resignation of key members of the company that is being taken over, says Kurt Einstein, the consulting firm's president.

Mr. Einstein explains that it is the "nature of the beast" to have anxiety and insecurity plague the staff changing hands while acquisition negotiations are in progress. Consequently, he maintains, it is of paramount importance to set a tone of security and reassurance at the start of the transition period.

Personnel study essential

To conduct the transition period in a tranquil and orderly fashion, a working knowledge of operational problems and of the strengths and limitations of the key personnel is needed.

This knowledge will allow for the establishment of a smooth integration plan to bring the new unit into the corporate entity. The plan can go into effect on the day following the purchase, Mr. Einstein maintains.

Operational and staff strengths and weaknesses should be examined as closely as financial statements are in planning mergers and acquisitions, the consultant advises.

IBM Offers New Management Game, New Training Programs

A computer-based management game is one of the new educational offerings being made by IBM. Three others give on-the-job training to programmers, computer operators, and terminal users.

Interactive Business Game Simulation, the management game computer program, can demonstrate, for example, how a major, short-term investment in a new product can affect market resources. There is a monthly charge of \$435 for 12 consecutive payments for this program.

Another IBM educational product, the Interactive Training System, allows a customer to use his teleprocessing network to teach employees how to use terminals for

data entry and inquiry into computer files. It will be available in October at a monthly charge of \$225.

Three DOS Console Simulation Drills are programs designed to give an operator experience, through simulation, in communicating with an IBM System/370 or System/360 operating under DOS. Charges for the drills, which will be waived after the first license payment, range from \$205 to \$235 each.

IBM is also offering independent study programs for assembler language coding and ANS COBOL coding. The programs include videotapes and audio lectures, texts, and exercises for hands-on computer programming. Course materials are priced from \$2,400 to \$3,660.

Minority Enterprises Still Lack Adequate Funding, Michigan Economist Says

Despite all the recent talk about promoting minority enterprise, there are still not enough sources of capital for minority-owned businesses, a Michigan State University economist says.

John P. Johnson, a research assistant at MSU, writes in a recent university publication that, while minority loans by the Small Business Administration did rise from \$1 million in 1967 to \$100 million in 1970, it would take \$40 billion to raise the number of minority-owned businesses to a level representative of their share of the population.

"As it stands currently, the linkup of the banks and the SBA represent the largest source of financing for minority firms although in fiscal year 1971 there were only 7,776 loans made through the SBA to minorities," Mr. Johnson writes. While commercial banks have cooperated in SBA-guaranteed loans they are slow to lend to minority firms on their own merits.

The minority-owned banks do

not have sufficient assets to supply a significant part of the capital demand. Mr. Johnson writes, "Most of the black-owned banks are less than ten years old. Their average size is \$10.4 million and they are little different from most other minority-owned businesses in being marginally profitable or undercapitalized."

The recent restructuring of the Small Business Investment Corporation to include an emphasis on minority enterprises has not had time to show its effectiveness yet, Mr. Johnson notes.

"Most of the proposals for increasing the flow of funds to small businesses and to minority businessmen in particular involve opening the capital markets to allow for free participation in secondary placements of long term debt and equity capital.

"Whatever the changes in policy or structure in financial markets that do occur, it is clear that minority-owned businesses will be needing large capital infusions to become viable in the business mainstream," Mr. Johnson concludes.

Census Breakdowns via Computer Network Offered by N.E. Firm

Population and housing information contained in First Count, File A, of the 1970 national census is now available on a time-sharing basis through National CSS, Inc., Stamford, Conn.

Included in File A are 409 items of population and housing data for 258,000 small areas in the United States, known as "block groups and enumeration districts."

Some of the information items contained in the file are population and housing counts, age, sex, race, and family relationship profiles; housing conditions; and dollar values of housing and monthly contract rent.

The data are accessed through

an interactive computer network called CENSAC. Users obtain a machine-readable file that can be directly input and processed by user-written programs, National CSS states.

More information on the data service is available from National CSS, Inc., 460 Summer St., Stamford, Conn. 06901.

GE Offers Technical Article Reprints as New Monthly Service

Technical article reprints of special interest to those in manufacturing are available to subscribers of a new General Electric Company service.

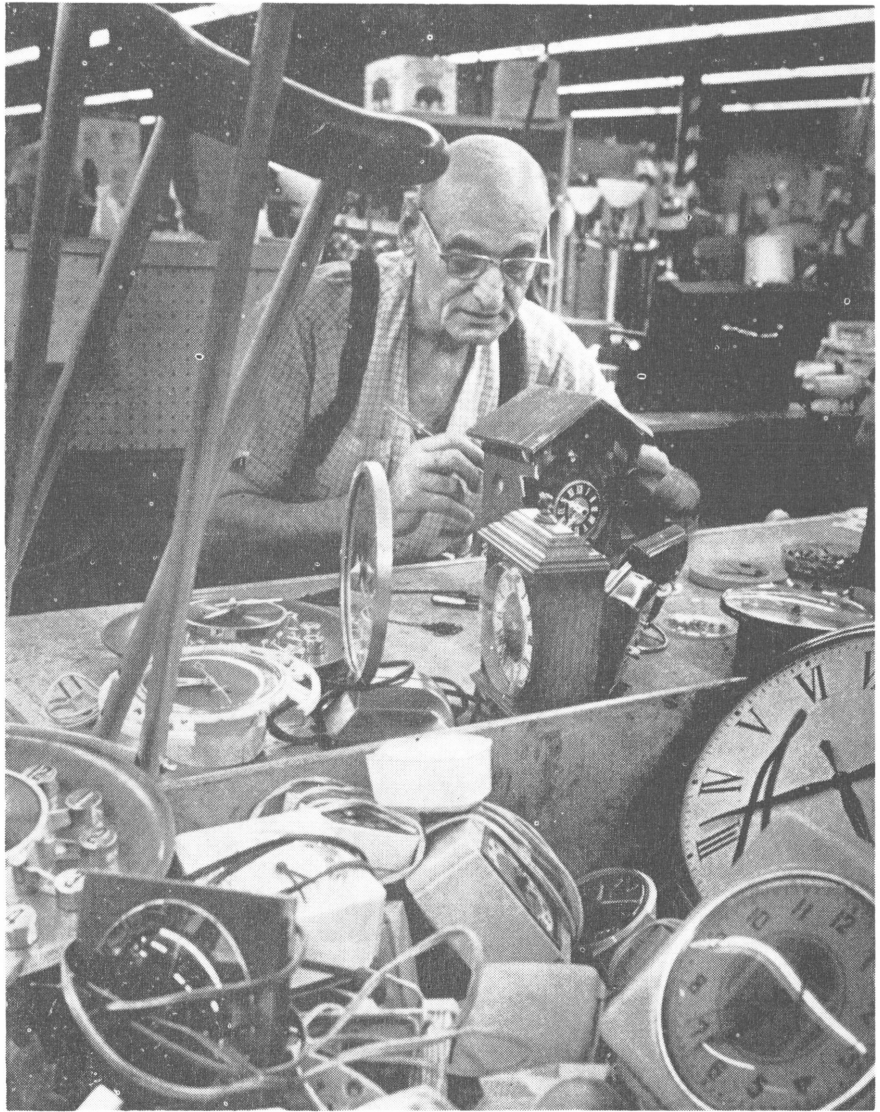
TIPS (Technical Information Periodicals Service) sends its subscribers a monthly catalog listing about 150 technical article abstracts aimed at those in charge of production and productivity. The abstracts are made from approximately 100 different manufacturing publications each month.

The monthly TIPS catalog is classified into approximately 40 categories (such as automation, inventory control and design analysis, testing, and reliability). TIPS was developed by GE's Manufacturing Engineering Consulting Service and has been used within the company for more than a decade.

GE says that it will mail out requested reprints to TIPS subscribers within 48 hours after receipt of an order.

The TIPS subscriber can either pay a flat rate of \$325 per year, which entitles him to up to 250 reprints without additional charge and then 50 cents per reprint beyond that amount, or \$165 per year plus \$1 per reprint regardless of the length of the reprint.

Information about and subscription to TIPS is available from Business Growth Services, Building 5, General Electric Company, 1 River Road, Schenectady, N.Y. 12345.



Handicapped worker repairs clocks at Wisconsin facility.

Goodwill Industries Uses Computer to Aid in Evaluation of Training Services

Goodwill Industries of Wisconsin is using a computer to help it determine the effect of its training, counseling, and other services on the more than 500 physically and mentally handicapped persons working in its rehabilitation center.

Goodwill is creating an information base on its clients including their individual characteristics, as well as the services each receives.

"Ultimately," said Jerome R. Lorenz, associate executive director for human resource management at Goodwill, "we will be able to develop a statistical analysis that tells us that a person with a certain type of handicap and other characteristics, given a certain type and

amount of counseling, training, and other services, is likely to advance to a certain level of rehabilitation 'progress.'"

The computer system has also cut the number of reports the Goodwill counselors have to fill out for each client.

A detailed cost/analysis computer program has also been started at Goodwill. This program will provide the basis for reporting procedures and cost analysis of the rehabilitation research information, officials say.

"For the first time we will be able to tell the cost per client. We'll know more accurately where our money is being spent. We will

not be guessing," said Dennis Pastana, associate executive director of fiscal management for Goodwill Industries of Wisconsin.

Associate Executive Director Lorenz pointed out, "For a long time people have been asked to donate to institutions such as ours and yet they never know how effectively that donation has been used. With the computer we will be able to tell them."

Goodwill Industries of Wisconsin is using a small IBM System/3 computer. All of its computer operators are handicapped persons.

Builder Schedules All Physical Aspects of Work By Electronic Computer

One home builder is not only using its computer for traditional financial applications but also to coordinate the scheduling of equipment, sub-contractors, craftsmen, and materials during the construction process.

The Larwin Group, Inc., a subsidiary of CNA Financial Corp., is based in Beverly Hills, Calif. It builds single- as well as multi-family dwellings. The company also has divisions in recreational communities development, mortgage banking and finance, real estate investment trust management, and commercial development.

Cuts construction time

According to Michael I. Kewton, treasurer of The Larwin Group, "By using the computer as a scheduling device, we can cut weeks off the average new-home construction span. The computer, therefore, benefits both the housing producer and the prospective buyer by allowing more efficient construction, and better quality and cost control, which is ultimately reflected in lower prices to the home buyer."

William T. Mercado, Larwin's director of management informa-

tion services, said, "As many as 80 to 100 vendors must be scheduled efficiently at every home site. Delays of just a few days, even hours, can severely inflate the cost of construction. Better scheduling means fewer idle hours for craftsmen and equipment."

Larwin anticipates using its computer to further its position in the modular housing market.

MIS Director Mercado explained, "Modular housing is a process by which housing components or entire homes are built in the factory and transported to the site of assembly.

"Advanced data processing capabilities are essential to efficient modular home construction. With the scheduling function of the IBM 370/145, Larwin might well offer the home buyer a sort of housing supermarket. The buyer can select various house plans, elevations, options, and financing alternatives, and have a completed home available for occupancy in a relatively short time."

IBM Shows New Optical Mark Reader that Ties In to Computers

IBM has introduced a new optical mark reader, the 3881, that handles documents ranging in size from three-by-three inch to nine-by-twelve inch.

The 3881 can send numeric and alphabetic data directly to an IBM System/370 Model 135 or 145 or place the data on magnetic tape through attachment to an IBM 3410 magnetic tape unit.

IBM says the new mark reader can process up to six different types of documents in a single operation, as long as the documents are the same size.

An electric utility, for example, could use the 3881 for one-step handling of cards with customer numbers preprinted in binary code and marked by meter readers. Up

to 6,000 of these documents could be processed in an hour, IBM says. Cards marked for special attention could be automatically separated from the rest during processing.

Besides meter reading and billing applications, the utility could use the 3881 for processing personnel forms, such as attendance reports, or to enter equipment survey data into a computer for tabulation.

Purchase price for the 3881 will start at \$51,000. Under the IBM rental agreement for shorter term needs, monthly charges will start at \$1,234. Under a 24-month contract, monthly rental will start at \$1,050. Customer shipments are scheduled to begin the first quarter of 1973.

UNIVAC Will Give RCA System Owners Trade-In Allowances

RCA 301 System users are being offered substantial trade-in allowances by UNIVAC, it was recently announced. The trade-in program allows 301 owners to move to UNIVAC Series 70/35s or 70/45s on either a purchase or three-year lease plan at low monthly rates, UNIVAC explains.

UNIVAC acquired the RCA general purpose computer base January 1, 1972.

More emulation to come

In the fourth quarter of 1972, UNIVAC plans to have 301 and 501 emulation available on Series 70/6 and 70/7 processors. The emulation will be supported under both the DOS and TDOS operating systems.

A. L. Fazio, director of planning for Series 70 operations, said, "This means a user can run second generation jobs concurrently with the newer applications he had developed for his third generation systems, thus increasing his overall system utilization."

Ex-RCA European Licensee Tries to Build Continental D.P. Industry

When RCA's computer division closed in early 1972, Siemens, its European licensee, agreed to collaborate with CII and Philips to try to make the European computer industry a successful one, explained André Charguéraud, president of Diebold Europe, S.A., at a May 23 press conference in New York.

Describing the agreement, Mr. Charguéraud said, "Many American magazines and other recent studies describe the February, 1972, agreement as a merger. This is not so.

"Cooperation is the word: each partner will retain his identity and his business activity. The group will work together in many fields, including the redistribution of market territories and probably the establishment of common subsidiaries for research and specific production."

Move insufficient

"It is an important step forward but it is not sufficient. Against monolithic competition, European manufacturers must merge their activities as soon as possible to succeed."

Mr. Charguéraud said he does not believe that the European manufacturing group he described would be a serious threat to American-made computers. The only threat to the American EDP companies' activities he envisioned was the possibility of European governments taking them over. "But this is as unlikely to happen as the full dismantling of IBM through a U.S. anti-trust suit," Mr. Charguéraud said.

He pointed out that ICL did not join the other three European computer manufacturers in their agreement because it wants to develop non-IBM compatible systems. Mr. Charguéraud observed, "By the late 1970s when the new systems resulting from the club's activity

reach the market, technological advances will have made that problem obsolete. The recent introduction of IMITATOR by IBM, which allows direct processing on the 370's series of RCA's 301, Honeywell 200, and ICL 1900, clearly shows the trend."

Honeywell Cites Achievements Since Merger with GE

Honeywell management recently patted itself on the back for merging with General Electric's computer interests back in 1970, when the computer industry started to restructure itself.

C. W. Spangle, executive vice president of Honeywell, told a meeting of large-scale computer users in Montreal, May 1, "The withdrawal of RCA from the main-frame business, the get-together of CDC and NCR, and the European consortium of Siemens and CII all confirm our decision in 1970 that a marginal or geographic supplier simply cannot afford the long-term costs associated with supporting complete current and future product lines."

Financial stability a must

To be competitive in the current market, suppliers must exhibit financial and organization stability, Mr. Spangle said. The customer does not want to "tie his future to a loser," the Honeywell executive said.

"One of the reasons we can be attentive to your needs, and act upon them, is that Honeywell is a profitable computer company. Along with the many other changes that have occurred in our industry in the past year and a half has come the realization that the computer user is taking an increasingly close look at the balance sheet of his supplier. Looking back over the last year, it makes eminently good sense," Mr. Spangle told the users.

State Capital Tries to Form Car Pools via EDP To Lower Air Pollution

State employees in Hartford, Conn., may soon find themselves matched to one another by one of the state's computers. The purpose of this matchmaking is not matrimony, just the formation of car pools to help cut down on Hartford's traffic congestion and air pollution.

The plan is being developed by the Connecticut Department of Transportation. Information on work hours, residence, and travel patterns of government employees who work in buildings in the State Capital complex is being fed into a UNIVAC 1106 computer system.

The computer matches people who live in the same locality, work about the same hours, and have offices in close proximity to each other.

Three riders per car

"If we can increase the number of riders per car to three, it would appear that we possibly could take 50 per cent of the cars off our congested highways," said Deputy Commissioner of Transportation James F. Shugrue. Studies show that presently only an average of 1.5 persons are carried in each car in rush-hour Hartford traffic.

Representatives of the transportation department will approach commuters the computer designates "compatible" and suggest that they think of organizing a car pool.

Besides the car pooling operation, the department of transportation's computer is also working on highway planning, engineering applications, stores inventory control, budget preparation, statistical information, and payroll processing.

If the pooling project proves successful with state employees, it may be expanded to include the major companies in the Hartford business district.

Model to Assess Before and After Effects of Conversion to Four-Day Work Week Described in Michigan State University Publication

A growing number of companies are converting to the four-day 40-hour work week. A general model with which to assess the before and after effects of an organization's work week conversion has been developed by Don Hellriegel and is presented in the spring issue of *MSU Business Topics*.

Mr. Hellriegel, assistant professor of organizational behavior, College of Business Administration, The Pennsylvania State University, explained, "The need for personalized analysis is critical since there has been no in-depth and longitudinal research conducted on the 4-40 plan which managers can easily apply to their organizations for reaching a go/no go recommendation."

Three-stage model

The Hellriegel model consists of three stages of analysis. Unless management is satisfied with the impact of the 4-40 on the elements of the first stage it need not go on to the second, likewise the second and third stages, Mr. Hellriegel explains.

In the first stage of 4-40 analysis management should consider conditions related to the organization. Some of these are capital utilization, competitive consequences, union position, and legal implications.

Type of work considered

"The type of technology, such as unit and small batch, assembly and mass production, or continuous process, may have differential effects on the form of an acceptable 4-40 plan," Mr. Hellriegel points out. "Conceivably, the greatest flexibility, because of the low task interdependencies, is provided with unit and small batch production."

At the second stage of the Hell-

riegel model management analyzes how the workers might be affected by the 4-40 plan. Mr. Hellriegel states, "A careful understanding of how their lives within and external to the organization might be changed should serve to highlight the potential advantages and disadvantages. By incorporating demographic factors [sex, age, marital status], it may be possible to anticipate the different sets of reactions to the plan."

Worker attitudes important

In the third stage of analysis several classes of worker attitudes as well as possible and actual changes in organizational effectiveness are measured and evaluated.

Worker attitudes toward the 4-40 plan can influence organizational effectiveness, Mr. Hellriegel says. "There may be differential effects in terms of the quality and quantity of outputs for the operation as a whole and within its subunits. These effects are also interrelated with the impact of such variables as worker recruitment, training costs, absenteeism, and tardiness."

Union opposition

Mr. Hellriegel believes that the unions' position in relationship to the 4-40 plan cannot be generalized. However, he sees one conclusion that can be drawn on their stand, "Considering the long history of union pressure for reduced hours and/or workdays, the acceptance of the 4-40 plan surely will be viewed as part of a larger strategy for further reductions in the number of workhours."

Three-day week

Nationwide Insurance Companies have been using a three-day work week in their EDP operation

to maximize the number of hours their equipment is used, a company executive recently told an AMA meeting (see *M/A*, May-June, '72, p. 8).

The Nestlé Company, Inc., White Plains, N.Y., announced that as of June 5 it was putting a flexible working hour system into effect for its 670 headquarters employees. Although a five-day work week will be maintained, workers will be able to choose their working hours. They can arrive at work at any time between 8 and 10 a.m. and leave between 4 and 6 p.m. They can also take a lunch break that lasts from 30 minutes to two hours.

Flexible workday

Lufthansa's Long Island City, N.Y., office experimented with this flexible work schedule last year and has now accepted it on a permanent basis. Nestlé, unlike Lufthansa, will not make its employees punch time clocks but will have them sign in and out of the building on an honor system.

Congress Warned of Perils in Entrusting EDP to Specialists

Systems fail when operating managers leave EDP development to systems specialists, Marvin Kornbluh of Wiley Systems maintains.

He explained how this user attitude developed and what can be done to remedy it at a special seminar held for Congressional members and staff. Copies of Mr. Kornbluh's presentation, "Who's the Master of Your System?," are available free of charge from Wiley Systems, Inc., 6400 Goldsboro Road, Bethesda, Md. 20034.

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about this issue

This issue of *MANAGEMENT ADVISER* represents a sharp departure from past issues. All feature articles discuss some aspect of a single industry—food or more particularly processed food.

We have done this because a large segment of our readership felt the magazine would be more valuable to them if from time to time it discussed the problems of one industry in depth. This issue represents an attempt by *MANAGEMENT ADVISER* to meet this request. We do not intend to devote another issue to a single industry for some time. We shall need time to evaluate the response to this idea from all our readers, and the worth of this particular issue to that percentage of our circulation that has asked for occasional issues devoted to a single industry.

Why food? We chose food, processed food, for our maiden attempt because it represents the largest retail industry in the country, and because everyone is concerned with it, if only as a consumer. Then, too, food is much in the news these days both from the point of view of costs and nutritional worth. Even as this is written, President Nixon has lifted all quotas on foreign meat imports; he has also indicated that “further measures” will be taken if necessary.

On nutritional value and safety, the Senate approved 69-10 on June 21 a bill to replace the present Food and Drug Administration of the Department of Health, Education and Welfare with an independent Federal agency. The Nixon Administration has recommended extension of the powers of the FDA while keeping it within the Department of Health, Education and Welfare. This recommendation has been rejected by the Senate 51-32.

So the subject is news and promises to remain so. We hope that those who wished a single industry emphasis will find this issue of the magazine valuable; we hope that all readers will at least find it interesting.

Won't you let us have your comments on this July-August, 1972, issue of *MANAGEMENT ADVISER*?

—*The Editors*

MARKETING INFORMATION: THREE SQUARES A DAY REQUIRED FOR THE FOOD INDUSTRY

by Neil Doppelt

Arthur Andersen & Co.

THE FOOD industry markets its products in a big way:

- The nation's food bill was approximately \$94.4 billion in 1971.
- An estimated 220,000 separate items were available, in grocery stores somewhere, to satisfy customers' appetites.
- Food manufacturers spend about \$1 billion annually to bring their products to consumers' attention through advertising in newspapers, magazines, and network and spot television.
- An estimated 625,000 sales calls per week were made to supermarkets in 1971.

These massive numbers provide only the outlines of the food industry's complex and costly marketing

effort. Because of the magnitude of its marketing activity, the industry is often viewed as representing "the state of the art" in the critical areas of marketing technology and marketing information systems development. How else, one reasons, could the millions and billions be allocated and controlled with any confidence? While this assumption holds true for some industry leaders, many other firms are just starting the process of upgrading their skills in the management of marketing resources.

In the following sections of this article some of the food industry's problems, practices, and opportunities will be explored. The techniques now in use (some of which have evolved through two or three passes at systems development) can

provide valuable direction to companies within the industry as well as other manufacturers and their advisers.

Inside the pressure cooker

The structure of the food industry includes three traditional distribution levels: manufacturer, wholesaler, and retailer. Over the years these channels of distribution have become pliable in order to accommodate varying market conditions. Large chain operations had bypassed wholesalers, but many wholesalers have reappeared as suppliers to chain outlets by demonstrating cost advantages for certain products. Specialized products such as frozen foods, ethnic foods, and "health" foods have generated cor-

EXHIBIT I

Grocery Store Sales - 1971

	NUMBER OF STORES (000)	% OF TOTAL	\$ SALES (BILLIONS)	% OF TOTAL
Large Supermarkets (\$2,000,000 per year +)	10.4	5.1%	\$35.6	37.6%
Medium Supermarkets (\$500,000-2,000,000)	28.5	13.9	36.8	39.0
Small Supermarkets (\$150,000-500,000)	33.7	16.4	12.0	12.7
Small Stores (under \$150,000 per year)	132.3	64.6	10.0	10.7
TOTALS	204.9	100.0%	\$94.4	100.0%

responding specialized wholesaling operations. Groups of independent retailers have organized formally and informally to create their own wholesaling operations, again in response to cost pressures. As a result of these kinds of adjustments the distribution lines crisscross.

At the retail level, however, the slow trend toward volume concentration continues. Statistics from *Progressive Grocer* magazine's most recent Industry Survey* are summarized in Exhibit 1, above. The thousands of retail outlets and their complex supply lines represent a continuing challenge for food manufacturers and distributors. An understanding of trends and problems at the retail level is essential to the formulation of sound marketing policies.

Viewed from a distance, the marketing process for a food manufacturer looks simple. He must provide a product that is competitive in price and quality, encourage

a variety of direct and indirect customers to buy it, insure that his distribution system keeps stock available at the retail shelf, and keep a careful eye on costs. Since everybody has to eat, the product should attain a reasonable market share and generate satisfactory contribution dollars to profit and overhead. This image of a relaxed, smoothly operating industry is almost exactly opposite to the real situation. Food manufacturers are being squeezed by a number of environmental trends as illustrated by the following statistics:

- The profitability of chain grocery stores, as measured by net profit as a percentage of sales, now stands at a tiny 0.9 per cent (1971).

Result: Manufacturers are under continuing price pressure, and any item that offers some promise of a little extra margin for the supermarket moves to the top of the "approved to buy" list.

- The net population growth of the United States has slowed to just under 1 per cent per year (1971). Zero Population Growth may be around the corner.

Result: A long history of growth through domestic population increase is ending for the food industry.

- Supermarkets seem to be reaching a plateau in terms of the variety of items they carry. After rising rapidly from 3,000 in 1946, the average item count is increasing at about 100 per year, and the average large store now carries about 7,900 items.

Result: Any new food product, package size, or non-food item will probably have to displace something else in order to appear on retail shelves.

- Government activity in the areas of price levels and profit margins (Phase II), quality and in-



NEIL DOPPELT is a manager in the Administrative Services Division of Arthur Andersen & Co. in Chicago. Formerly he was a senior marketing analyst with Esso International, Inc. Mr. Doppelt received a B.S. in chemical engineering

from the Massachusetts Institute of Technology and an M.S. in industrial administration from Carnegie-Mellon Graduate School of Industrial Administration. His articles have appeared in several professional journals.

*This Survey is an excellent source of industry information; most of the statistics in this article are drawn from current or historical Survey issues.

The average item count is rising at about 100 a year; about 7,900 items are stocked.

redient regulation, and marketing practices has accelerated sharply.

Results: Some of the basic marketing assumptions and marketing policies of the industry are being successfully challenged and changed.

This list of problems is a formidable one for any industry. Those firms with the most successful marketing innovations stand a good chance of maintaining volume and profit growth; those companies that move more slowly may see their horizons contract rather than expand.

Many segments of the food processing industry have begun to approach the limits of cost reduction within the manufacturing function, and are struggling to keep distribution costs from rising. Again, the marketing function, or more specifically the cost-effectiveness of marketing activities, offers opportunities for profit improvement. Leverage exists to reduce the growth rate of marketing costs by making current spending levels go farther.

Data by the bushel

No marketing manager within a food manufacturing or distribution company should complain about the lack of data. He is surrounded by willing suppliers, each of whom has a price. The industry helps to support several peripheral industries whose primary function is to collect and report detailed statistics on product movement, market share, consumer buying habits, competitive prices, and media audiences—to list the main categories. The Government is also generous (and the price is right) with data on population, average price levels, spending trends, and economic activity. Within his own organization, the marketing manager can obtain

reams of detailed sales statistics, and often cost and profitability data as well. In the case of these latter figures, he may have to settle for less than he needs.

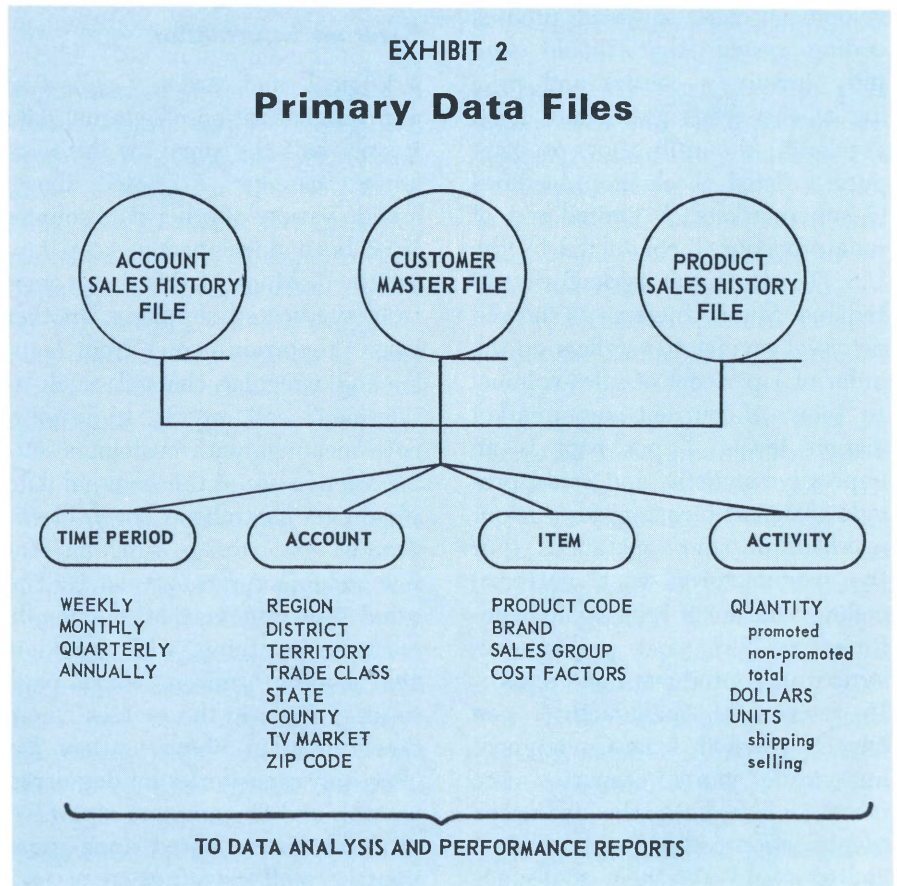
All too often, however, these sources combine to produce a glut of raw, unsummarized data that immobilizes management activity. For example, food industry customer lists often run into the thousands and sometimes tens of thousands. Analysis of the sales pie cut six ways for ten thousand customers is a hopeless task.

Because of this problem, data processing equipment is almost mandatory for companies in the industry. EDP-based information systems allow data collection at the most detailed level while providing manipulative capability to summarize, average, and aggregate the data into information for management purposes. The detail is al-

ways there, in the computer, for those instances when customer-by-customer or item-by-item information is required. Under normal circumstances, however, these reports are too voluminous to be usable.

A number of larger companies in the industry have elected to maintain their data files on a completely "disaggregated" basis; that is, with complete flexibility to retrieve and rearrange the detail according to management requirements. Exhibit 2, below, shows the key data files in such a system. The three primary files—account sales history, customer master, and product sales history—serve the production, accounting, and distribution functions as well as billing, order entry, and, of course, marketing.

A significant event in the food industry's management of data is



Retail Movement: Grocery and Non-Food Items*

Weekly unit sales	No. of items	% to total
Less than 4	1605	32.5%
4-6	966	19.6
7-12	1029	20.8
13-24	749	15.2
25-48	345	7.0
49-96	173	3.5
97 and over	70	1.4
TOTAL	4937	100.0%
Up to 1 case	4349 items	88.1%

*SOURCE: *Progressive Grocer*, November 1970 study of 7 A&P stores over a 13-week period. Average weekly sales: about \$60,000.

on the horizon. The industry, including distributors and manufacturers, is proceeding with the development of a universal product coding system that should simplify inventory control and pricing at the retail level, and could accelerate the utilization of computer-assisted checkout procedures in supermarkets. A limited test of such procedures, conducted by the U.S. Department of Agriculture and Indiana State University, showed potential savings to retailers on the order of 1 per cent of sales volume. In view of current supermarket margin levels, 1 per cent is an impressive statistic, and could provide sufficient incentive for a major overhaul of store operations. For the manufacturer, such universal coding will mean revising item information files, and perhaps restructuring product line reports. In return, the manufacturer can expect to benefit from Government and trade journal reports more closely aligned to the industry's identification codes. Better product coding could also help to reduce

pipeline inventory levels at all stages in the distribution process.

External information

Logical and orderly collection and summarization of internal data is only half the story for the marketing manager. As noted above, a wide variety of other data sources have been developed to keep him informed. Much of this data comes from syndicated suppliers; another large proportion comes from regular and irregular channels such as salesmen's call reports, trade journals, meetings with customers, etc.

Effective use of this external data requires a centralized entry, classification, and storage function that few manufacturers yet have. The usual situation is that everybody receives something, with considerable overlap, routing, and page turning. Even in those cases where firms maintain libraries, they are often only repositories for dog-eared journals and Government reports. A retrieval system based upon identification and classification of ran-

dom input can produce highly informative compilations of data.

For example, recent trends in the retailing end of the food business point toward some important shifts in the makeup of retail outlets. "Convenience stores," which offer long shopping hours seven days a week and handle about half the usual number of items, have grown rapidly. According to *Progressive Grocer* magazine, these stores have successfully resisted the trend toward fewer outlets by increasing their numbers fivefold in ten years. Convenience stores now account for an estimated 3 per cent of total industry grocery sales. Add to this piece of information another *Progressive Grocer* article, a year earlier, which reports on weekly unit sales of groceries and non-foods in A&P supermarkets: only 12 per cent of these items moved as much as a case of 24 units each week, as shown in Exhibit 3, on the left. An additional input to this picture might come from internal sources, as shown in Exhibit 4, on page 21. Here, marketing managers learn about the distribution costs and eventual contribution margins of various classes of trade. (The data is illustrative only.) Based on these facts, an examination of distribution patterns and possible marketing strategy changes could prove to be both timely and profitable. Possible alternatives include:

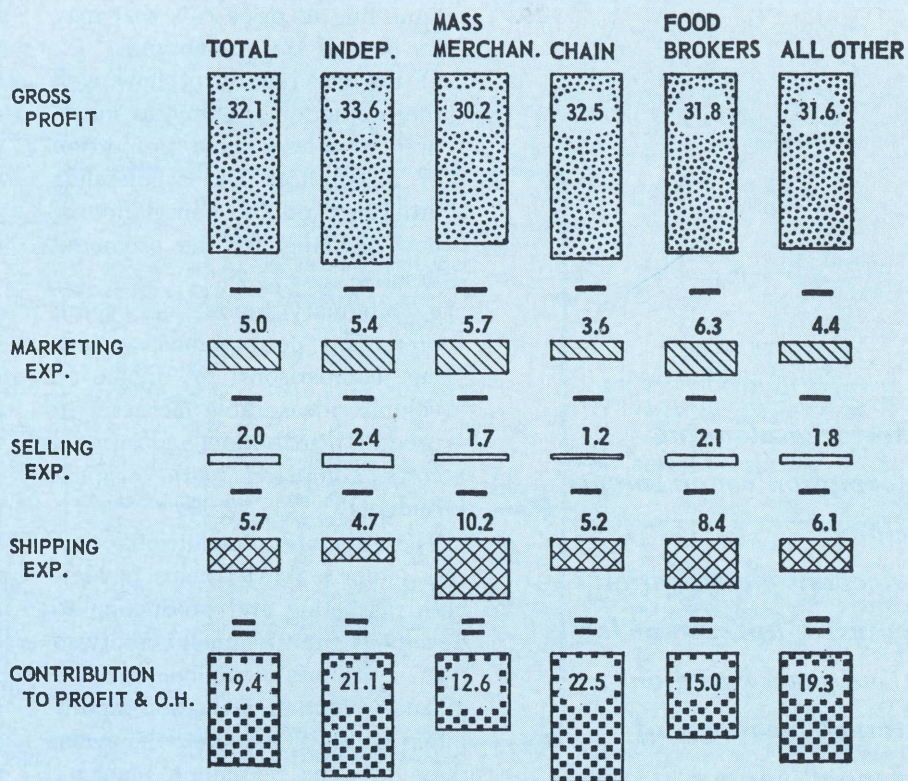
- Investigation of just why so many items turn so slowly in supermarket inventories; the average supermarket turns its stock about once a month.
- Experimentation with revised minimum order sizes to various channels of trade, considering the "half-case" customer who might be better served through a wholesaler or food broker.
- Placing special emphasis on the service needs of convenience stores, as well as on developing specific marketing plans for achieving more volume in this rapidly growing segment.

The point to this example is that

EXHIBIT 4

**Estimated Profit
Contribution by
Trade Class
first half 1972**

(illustrative data only)



an effective classification and retrieval system for external data—a “market intelligence” segment of a total marketing information system—should surface combinations of facts such as these for management attention. Without an organized approach to handling these inputs, the marketing manager is forced to rely on his own memory and chance to bring useful information into focus. Market intelligence should occupy a highly visible, centralized position within corporate staff organizations. Some companies have moved to utilize computer-based indexing systems, such as Key Word In Context (KWIC), to facilitate rapid sorting and retrieval. The availability of syndicated data may also trigger realignment of sales territory boundaries to conform to established trading areas or television markets, so that direct comparisons with external statistics are more easily accomplished.

Planning and control

The most important reason for

amassing data and converting it into useful information is to enable marketing managers to prepare plans and monitor performance against those plans.

Like God and motherhood, the importance of planning and control is not arguable; it is very easy, however, for many managers to put these activities at the bottom of their priority lists. The planning process is difficult—it requires commitment and quantification. In the food industry, the marketing-planning process really consists of many small plans within an overall framework.

1. *Trade and consumer promotions*, for example, are commonly used to encourage retailers to stock specific items, and to provide consumers with incentive to buy them. Many food companies carry out dozens of different promotions each year, offering a variety of case allowances, cooperative advertising allowances, free goods, coupons, price-off packages, and premiums. Food manufacturers are spending an estimated \$500 million annually

on these kinds of promotions, broadly classified as “merchandising allowances.”

While most companies budget an overall spending level for promotions, a much smaller number take the necessary next step to plan and monitor individual promotional campaigns. Promotion planning can be considered as another module in a marketing information system, and should include the following data and information inputs:

- a) A forecast of normal demand for the anticipated promotion period.
- b) A forecast or estimate of increased demand that will result from the promotional activity.
- c) An estimate of volume decreases, as compared to normal volume, that will take place after the promotion has been run (to account for pipeline fill during the promotion).
- d) Estimates of the extra packaging, handling, and sales literature costs that will be incurred for the promotion.
- e) A calculation of the required breakeven volume to recover all

additional costs (including the reduction of normal per unit revenue due to price cuts that may be part of the promotion).

f) Regular reports of how well the promotion is going, as measured by sales volume, proportion of distributors and wholesalers ordering, and the penetration of new accounts for the promoted item.

g) Summary reports on overall promotion performance, including comparisons to breakeven volume, measurable increases in product distribution, and internal costs compared with original budgets.

The promotion monitoring process (item f above) helps to alert both marketing and production to deviations from planned activity so that appropriate action can be taken. Promotion evaluation reports (item g above) complete the cycle; they help the marketing manager do a better job of planning future promotional campaigns.

2. *The effective utilization of salesforce personnel* can be one of the biggest potential payoffs of planning. Food manufacturers usually divide their field sales forces into "direct" and "indirect" groups. "Direct" calls are selling efforts focused on chain store buying offices, wholesalers, and other locations where buying decisions can be influenced. "Indirect" calls are made at the retail level, where the manufacturer's representative arranges shelf stock (and attempts to obtain better locations or more shelf space), helps the store manager prepare orders to his warehouse, and installs or replaces promotional displays. Considering the hiring, training, and maintenance costs of individual salesmen, food manufacturers are constantly seeking ways to make more effective use of their resources in this area. Routing schedules for indirect calls and simplified call reporting procedures are now common in the larger companies. Call reports, of course, supplement other information sources with data on competitive activ-

ity, inventory levels, and price changes at the retail level. Call reports with special "flash" sections are used to solicit observations of specific market conditions on an as-needed basis. One month, the need may be for shelf-facing information, while later in the year the section may be used to record price levels or new product information.

These scheduling and report techniques help direct the activity of individual salesmen, but they do not address the fundamental planning and budgeting question: How many salesmen are required, and why? Again, the marketing manager must combine information from a variety of sources in order to properly plan overall salesforce manning levels. This process is illustrated in Exhibit 5, on page 23.

The end result is the assignment of call frequencies to groups of accounts, and numbers of salesmen to specific territories to make those calls. Note that the key indicator of account classification is potential volume, not historical volume. These two indicators must be balanced, of course, so that regular accounts are not neglected in an attempt to crack other accounts.

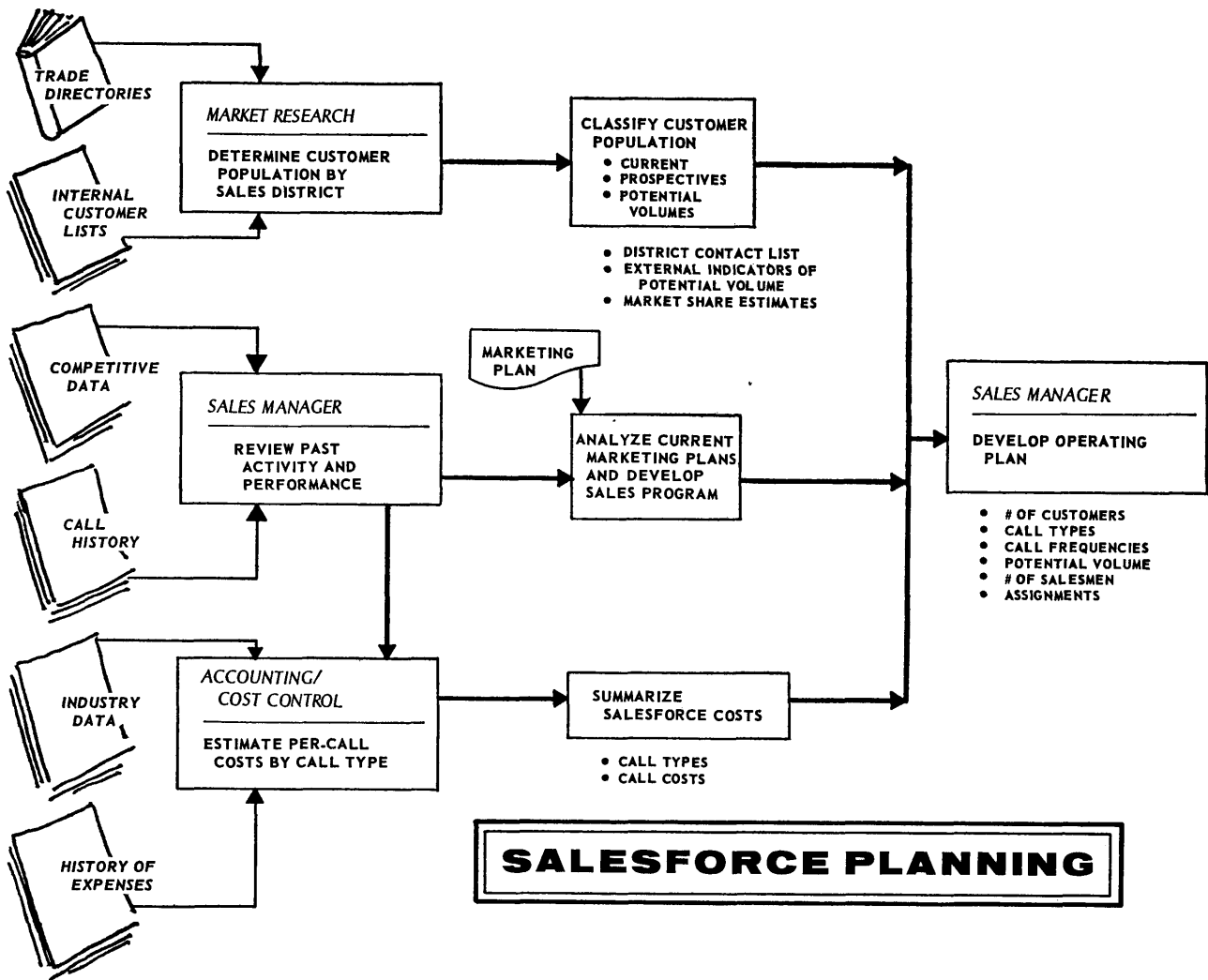
This analysis sequence may reveal that many calls are made on accounts that cannot be expected to provide any significant order volume. These tend to be the smaller, independent stores and supermarkets. When reasonable estimates of account potential for these smaller outlets yield low volumes, some other service technique should be considered. One alternative for indirect calls on smaller stores utilizes separate salesmen entirely. These "contract" salesmen may offer cost savings versus in-house salesmen, particularly for food manufacturers with limited product lines, or low distribution in certain parts of the country.

Once the output of a planning sub-system can be accurately visualized, the information requirements to support plan development are also defined. In the salesforce planning example above, for in-

Salesforce planning information requirements include:

- ***Account classification measures, updated at least once a year, based on external measures of potential volume.***
- ***Call frequency reports for sales territories.***
- ***New customer or new prospect lists obtained from external sources.***
- ***Cost estimates for hiring, firing, maintaining salesmen in the field.***
- ***Historical sales volumes (and profitability) for key accounts.***

EXHIBIT 5



stance, information requirements include:

- Account classification measures, updated at least once a year, based on external measures of potential volume.
- Call frequency reports for sales territories.
- New customer or new prospect lists obtained from external sources.
- Cost estimates for hiring, firing, maintaining salesmen in the field.
- Historical sales volumes (and profitability) for key accounts.

This is the way marketing information systems are developed: key outputs define required information inputs, which in turn define basic data files. In a well-designed information system the plans themselves become information input to other

functional areas (such as finance and manufacturing) to aid decision-making processes throughout the organization.

Those companies that have been successful in supporting their costly marketing efforts with user-oriented information systems have concentrated on the output first. The complete design of a planning subsystem thus spells out the sources for all information, and (equally important) the responsibilities, timing, and formats for the development of regular annual and project plans. Control reports tied directly to the level of detail contained in the plans round out the plan/monitor/re-plan cycle.

Better information systems

The examples cited in the sections above are only a few of the

steps being taken by industry leaders to improve their marketing operations. The internal pressures for cost control and the dynamic competitive activity of the food industry have convinced many marketing managers that improved information systems such as these are well worth the investments that they require. A reasonable rule-of-thumb guide to the "dollar stretching" value of a comprehensive marketing information system is 10 per cent of the annual marketing budget.

Just as an army travels on its stomach, the food industry moves forward on marketing information. Given both the need and the initiative to strengthen information systems within the marketing function, food manufacturers of all sizes can reap substantial benefits from the end product.

Supermarkets, which for so many years have been able to do no wrong, now show all the signs of a mature industry with all that that implies. The era of management improvement may now be needed —

FOOD RETAILING NEEDS A SYSTEMS APPROACH

*by Harold W. Fox
DePaul University*

RETAILING is marked by ease of entry, deceptive simplicity of operation, and high frequency of failure. The American dream of independence and income still lures thousands every week into starting a small store—much as staking out a farm did in the last century. But one-half of the modern new ventures cease operations within two years. Most of these are not even counted in Dun & Bradstreet's statistics on business failure.

Over the past three decades the number of retail stores per capita has declined steadily. In fact, every U.S. Census of Business since 1939 has reported a total of about 1¾ million retail establishments. Meantime, the population has increased

60 per cent! The field with the largest absolute decline is food stores.

Fewer and bigger stores—this has been the structural change in the food trade. But ever since supermarkets revolutionized food retailing, their average operating expense ratio has increased almost continuously. What practices and problems account for this trend? An examination of supermarket operations reveals growing complexities that will be manageable only through a systems perspective. Packaged foods pass through various stages after they leave the manufacturers. Ultimately, the inedibles require recycling or some other disposal. From manufacturing to final disposal many problems are

interrelated. Some of these problems are under study by progressive industry associations and companies. Meantime, retailers are devising imaginative ways to cope with mounting challenges.

Food stores—fewer and bigger

Between 1939 and 1967, the number of food stores—as reported by the U.S. Census of Business—dropped from 560,000 to 294,000. An estimate for mid-1972 is 265,000 establishments, of which 200,000 are grocery stores. Total sales of all food stores are expected to reach nearly \$100 billion in 1972.

Almost one-half of all food stores either lack paid employees or sell

less than \$50,000 annually. Many of these small operations are a form of disguised unemployment. At the other extreme are 25,400 supermarkets (included in the grocery total above). These are departmentalized food stores featuring fully self-service grocery, dairy, meat, and other sections, mass displays of wide merchandise assortments, relatively low prices, and heavy advertising. Most avoid such typically department-store and specialty-store services as telephone orders, home deliveries, credit, and gift wrapping. The checkout counters of these supermarkets register annual sales of at least \$1 million.

Scholars have traced the concept of supermarkets back to the Providence Public Market in 1887, followed by other, separate attempts elsewhere in prosperous 1910, 1916, 1925, and 1928. The industry usually credits Michael Cullen as the first successful supermarket operator. In 1930, after both Kroger and A & P had rejected Cullen's idea, he opened "King Kullen, the Price Wrecker" supermarkets in Long Island, New York—and retailing entered a new era. Three decades later, the supermarket concept dominated the food trade. Since then, the pace of further encroachment has been slow.

From a multitude of small shops with salesclerks the food trade changed to fewer, huge, strategically located, self-service marts. What are some of the economic, commercial, psychological, physical, financial, political, and social forces that helped spark and sustain this movement? The Great Depression had made the public acutely price-conscious. Shoppers accepted manufacturers' brands wherever sold. Economies of scale in retailing enabled the early supermarkets to offer dramatic bargains. Spreading ownership of automobiles and electric refrigerators made household buying in larger quantities feasible. An unwitting spur to consolidation was a progressive franchise tax on each store of a chain, enacted in some states during the 1930s. After World War II, the growth of sub-

urbs and the construction of shopping centers were conducive to high-volume operations.

From a commercial point of view the supermarket business holds three major attractions:

1. Revenues are likely to exceed costs at least slightly, and the extremely high turnover produces a very good return on investment.
2. Foods are a basic necessity with a permanent, continuously rising demand.
3. Sellers of general merchandise who operate supermarket departments can divert some of that heavy traffic to adjacent areas where sales are more profitable. Foods are the core volume for any kind of convenience-goods business.

Supermarkets have gently falling marginal costs, but optimum store size is largely a matter of trading area. Space in new units stabilized at 20,000 square feet during the mid-'60s. Currently, a trend toward giant stores exceeding 25,000 square feet is emerging. Slightly over two-thirds is selling area. Accounting for 10 per cent of America's food stores, supermarkets handle 61 per cent of the sales. In the immediate future the relative importance of supermarkets is expected to remain near present levels.

The problems of maturity

The number of supermarkets is still growing slightly, but there are indications that in many areas, "overstoring" is a problem. Among the new supermarkets, two visible trends are: (1) relatively more units with higher sales and (2) relatively more units as adjuncts to general-merchandise stores. Supermarkets in the top sales category—\$5 million to \$15 million—can capture new efficiencies such as more direct shipments from manufacturers into the store. Combination stores offer consumers the convenience of one-stop shopping.

The supermarket industry now is mature, if not overextended. Many companies are diversifying. This is consistent with expected strategy at the maturity stage of an industry's life cycle. Another manifestation of maturity is emphasis on efficiency because expansion of sales is more difficult. In general, operating savings of \$100,000 have the same impact on pretax profit as a \$6¼ million rise in sales. The supermarket manager is often required to trade off one against the other. Depersonalizing mechanization of operations or curtailment of services can reduce sales drastically.

The present incidence of one supermarket per 2,560 households is not low. If food volume were concentrated in fewer stores, prices could be lower, but at reduced accessibility and choice for some consumers. Apparently, only a radical innovation that consumers prefer because of lower cost or perhaps greater convenience is likely to decrease the number of supermarkets. Fixed costs are an extremely low 7-8 per cent of sales, a McKinsey-General Foods study found. "In a large operation, a store's volume must shrink to very low levels before shutting it down makes financial sense," the study stated.

Beyond a minimum of competitors necessary to spur efficiency, the more stores there are to divide the demand for food which exists at any one time, the higher each unit's cost of operation. Since supermarkets are wedded to traditional markup policies, higher operating costs lead to higher gross margins and higher prices.¹ Rising gross margins symbolize a key problem of maturity in food retailing.

Total costs rising

The total cost of supermarket operation, measured by gross margin, has been climbing relentlessly

¹ A technical explanation is in Edward H. Chamberlin, *The Theory of Monopolistic Competition*, Harvard University Press, Cambridge, Mass., 1935, pp. 105-106.

EXHIBIT I

Common Size Operating Statement of a Supermarket For the Year 1971

Sales (\$2½ million median)	100.0%
Cost of goods sold	<u>78.7</u>
Gross margin	<u>21.3%</u>
Warehousing, distribution, and headquarters overhead	4.1%
Store expenses:	
Labor and benefits	9.3%
Advertising, stamps	2.4
Supplies	0.8
Real estate	1.4
Utilities and misc.	1.7
Total store expenses	<u>15.6%</u>
Operating expense ratio	19.7%
Net margin before taxes	<u>1.6</u>
Total economic cost of supermarket operation	<u>21.3%</u>

Based on data from Super Market Institute

to a plateau. Exhibit 1, above, presents a modern supermarket's financial profile.

Although widely used, margins can be misleading. For instance, even when a store's gross margin rises, the overall efficiency of total distribution may improve. Here are three realistic examples. One is greater emphasis by supermarkets on their own brands and on non-foods, often at a saving to the consumer. Another is backward integration, netting lower total-channel costs and, due to competitive pressures, lower prices. Finally, extra operations and promotions that consumers want boost a store's volume, entitling the retailer to extra discounts from vendors. There is no need to belabor the point that rising margins do not always evidence a higher price level. But often they do. Rising margins in food retailing largely reflect increases in the number of stores, increases in services, and increases in complexity.



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The consumerist who condemns the rising margin of supermarkets ignores the fact that originally they operated out of abandoned garages at the outskirts of town. Goods were displayed on old ginger-ale cases. In due course, consumers took convenient locations, wide aisles, and ever increasing assortments on suitable fixtures for granted.

Prosperous conditions after World War II favored an improved store atmosphere through air-conditioning, music, rest rooms, special lighting effects, carpets, murals, and automatic doors. Supermarkets also had to invest in equipment for meat and frozen foods and in other new technology.

Customers demanded larger parking spaces, longer store hours, additional checkout and express lanes—plus check-cashing, parcel pickup stations, and free deliveries to their cars. Supermarkets even reverted to clerk-attended bakery and delicatessen departments which became quite popular. The newer, larger units have prescription-drug departments manned by professional pharmacists.

Usually such additions are sound tactics in the short run. They give the originator in each area a competitive advantage which increases his revenues and profits to the detriment of his rivals. When the latter match or surpass the extra services, all are saddled with extra costs and have no way of offsetting them except through higher prices. Old

ginger-ale cases and quaint locations do not attract the typical hurried shopper.

Furthermore, supermarkets are changing in many ways that are not evident to the consumer. There is much experimenting with new approaches to reducing theft, removing trash, changing stockroom procedure, allocating various functions, and saving administrative expenses. The shopper sees simple sameness; the manager acts in an environment of rapid change.

The new complexities in modern retailing separate it more and more from the halcyon days of the small proprietor; they push up gross margins.

For example, nowadays more than nine out of ten supermarkets are part of an organization that operates a central warehouse. But this logistical improvement only exposes an administrative problem: in most of these companies, buying, warehousing, and distributing are separate functions. Each pursues different goals. Actually, supermarkets may need even deeper functional backward integration, controlled through interconnected computers.

Among other complications, the top echelons in supermarket corporations evaluate 7,000 new product offerings and 10,000 new tie-in promotions from manufacturers and wholesalers per year, supervise their own processing facilities, bargain with labor unions, conduct location analyses, manage their real estate, appraise opportunities for diversification, consider feasibility studies, raise capital, and administer cash flows . . . and the expense of performing these functions is rising. So are property taxes and other governmental levies.

Although other causes could be cited, it is evident that since the Great Depression a variety of sources has forced a larger share of the consumer's food dollar into defraying the cost of store operation. High gross margins are a key problem to the supermarket industry because they make it vulnerable to a basically different type

of low-margin enterprise. As explained by Professor Malcolm P. McNair in his "Wheel of Retailing" concept, the newcomer undersells the established retailers and wins their customers. This is, of course, exactly what the supermarket industry did in its early years.

How serious is the problem of record-high margins? The answer is not clear-cut because published series are not internally consistent due to changes in definition, composition of the sample, etc. But, apparently, supermarket chains required a higher gross margin during the past decade than grocery and meat chains in the 1920s.² Certainly, it is clear that, from both societal and commercial points of view, the high cost of food distribution signifies a need for management advisers to develop a more efficient system.

Statistics of Income, published by the Internal Revenue Service, show gross margins of the largest retail food corporations as low as 14.8 per cent in 1941 and 1948. The leading chain, A&P, was lower yet. Gross profits in its fairly typical Middle Western division were 13.5 per cent in 1941 and 12.6 per cent in 1942, according to M. A. Adelman's landmark study of the A&P. The 1967 U.S. Statistics of Income puts gross margins of the largest retail food corporations at 21.8 per cent. Studies of supermarket expenses inaugurated during the past two decades similarly show a rising trend. In OPS-controlled 1951 the median gross margin reported by Super Market Institute was 16.0 per cent; in 1971 it was 21.3 per cent for operators with warehouse and 19.3 per cent without. The operating expense ratio may have climbed even more.

One soaring expense is the cost of labor. This is important. On the accompanying common-size statement, wages and supplemental benefits account for nearly one-half of operating expenses. Another source, *Progressive Grocer* magazine, puts

payroll expense of chain stores at above 11 per cent. Both studies agree that the proportion of labor costs is rising. The potential for cost escalation is high because most wage rates in retailing are still low. Unionization is increasing. Some scarce skills like meat-cutting already command very high rates. Many managements have surrendered the flexibility of rotating store employees between stockroom, sales floor, and checkout. Some unions are opposing such changes as moving in-store meat-cutting to a more efficient and sanitary centralized operation.

Productivity crisis

In recent years, real output per manhour has declined. Prior increases in productivity were outstripped by higher hourly labor costs almost 1:4. "The retail food industry is faced with a major productivity crisis," declared Dr. Gordon F. Bloom, former chairman of the National Association of Food Chains. "It is sobering to consider that in the entire period from 1929 to 1958, which was marked by one of the most revolutionary changes in the long history of food distribution—the transition from service to self-service stores—the rate of improvement in manhour output in good wholesaling and retailing averaged only 1.8 per cent per annum."

At present, many in the food industry bank on breakthroughs in mechanization and automation. They are working on a ten-digit universal product code which will give almost every American grocery product—some 900,000 items—its own identification number. The code will be readable by either a person or a scanning device. The concept is similar to the magnetic ink character recognition on checks and the expected benefits are similar. The ultimate goal is to make automatic checkout operational. Since these plans push the state of the art, management advisers are needed in all phases. Not only do companies require new software

and operating systems, individualized procedures and trained personnel, but projects are even hampered by such questions as, whose equipment should we buy?

Along with mechanization, the industry's hope for resolution of its "productivity crisis" may be new personnel programs with two-step objectives. First is a reduction in costly turnover. Part-time employees outnumber full-time 7:5; more than 100 per cent of the part-time and one-third of the full-time help are separated annually. Second, as employees' tenure lengthens, more training to improve performance and operate new equipment is practicable. The entire spectrum of personnel utilization and management offers many opportunities for consultants. Finding ways to cut payroll 10 per cent can boost the bottom line by one-third. How many other industries offer such an incentive to efficiency?

Dr. Willard R. Bishop, Jr., director of research for Super Market Institute, points to the need for more serviceable two-way communication between warehouse and stores as one reason for locating some computer facilities in the latter. In turn, store managers and their assistants will have to learn to run this equipment and to interpret the printouts. "As labor cost increases, management will be even more willing to spend money on programs that are designed to improve labor scheduling, increase labor productivity, and substitute equipment for labor." But Bishop also cautions that further depersonalization of a supermarket might alienate shoppers.

After all, the mission of supermarkets is not to minimize costs. It is to promote purchases on their premises of foods and related staples at competitive prices, and with the shopping comforts that consumers want. What are some typical merchandising practices in the supermarket industry? Profit is the incentive for these efforts. How do companies foster patronage of their stores? Another question, much in the news in the spring of 1972,

² Federal Trade Commission, *Chain Stores*, 1933. See also annual reports of individual companies.

involves their pricing. A few important aspects of each will now be analyzed, beginning with merchandising.

Merchandising

A typical supermarket displays 8,000 items. The grocery department accounts for 67.7 per cent of total revenue, meat 25.0 per cent, and produce 7.3 per cent. Product mix varies among stores mainly according to consumer preference. Supermarkets have relatively little latitude and profit potential in deviating from the wanted combination. Instead, management's discretion lies in policies on nonfoods, proprietary brands, deployment of shelf space, and add-drop decisions.

The grocery department handles dry packaged-goods food, dairy, and nonfoods. The latter include health and beauty aids, hardware, phonograph records, and so on. These have higher margins but lower turnover than foods. Originally hailed as profit restorers, nonfoods have leveled off at a disappointing 6.1 per cent of sales. Due to the diversity and complexity of these lines, they are often handled by rack jobbers. These specialized middlemen assume responsibility for the buying, delivery, display, pricing, and point-of-sale advertising of nonfoods — and the liquidation of poor sellers. Supermarkets have vacillated between delegating these functions or performing them themselves. In general, arrangements with rack jobbers have the same advantages and disadvantages for supermarkets as leased departments have for general-merchandise stores.

A more critical merchandising policy is the use of resellers' brands. Shoppers do not know whether a product that, except for its "private label" and lower price, looks similar to a well-liked manufacturer's brand, is in fact identical or not. Indeed, many resellers' brands come from the same source as their heavily advertised brethren, but some emanate from indepen-

dent plants with deficient sanitary control. Under the prodding of consumerists, retailers are increasing the surveillance of their vendors (as well as their own premises).

A proprietary-brand program is by no means an easy task. After defining the product, the reseller must pay for design of separate labels, unique packaging, segregated inventory, and special stock control. Once a retailer's name appears on the package, the product is unsalable in other outlets. Since the shelf life of food is limited, such an operation is economical mainly for a large organization. As in the case of nonfoods, specialized middlemen have sprung up to service supermarkets.

Shoppers loyal to store brands

The main purpose of food chains in establishing their own brands, The National Commission on Food Marketing found, is to cultivate shoppers' loyalty to a line of exclusive products. They are potentially lucrative; merchandise costs and advertising for resellers' brands are relatively low. But many supermarkets shelve their own brands at the most desirable place (eye level), sell them at a lower price, yet experience lower turnover than for manufacturers' brands. Many embark on this course because their competitors have developed proprietary brands. Some seek independence from manufacturers whose brands are strongly entrenched. Another objective is greater freedom in cost and pricing than various laws permit for generally available goods.

Merchandising policies vary. Some retailers use a large number of proprietary names for different product classes, qualities, etc. Some concentrate on a limited number of brands. Some emphasize their own, but many do not. It is clear, however, that the battle of the brands has intensified vendor's rivalry for shelf space. Payment for exposure is not uncommon. There have even been occasional instances of violence.

Almost two out of ten grocery items are displaced every year. A typical supermarket adds about 900 new products and drops 700. To screen the flood of new offerings, over one-third of the companies use formal buying committees. A study of buying committees by A. C. Nielsen Co., the research house, found that their criteria rank as follows:

1. Evidence of consumer acceptance
2. Advertising and sales promotion support
3. Introductory terms and allowances
4. Logic behind developing the product
5. Recommendations for merchandising.

But other observers feel that most of these committees tend to endorse the judgment of the product buyer and their main contribution is to let him reject six out of seven proposals gracefully.

In general, the merchandising function seeks to satisfy customers, making total cubic footage of space as productive as possible. Store managers' decisions on shelf space and displays can have a major and immediate effect on sales. But the managers have little research or few plain operating facts to guide these decisions. In most organizations, *Progressive Grocer* found, computers spew out too many reports for executives at headquarters and too few for executives at the store.

Some companies are installing new procedures to stock ever more closely to consumer demand. A routine which replenishes on the basis of bimonthly sales is unworkable for goods with fluctuating popularity. Not too long ago, supermarkets overbought at the end of each product's season. Then the product's low volume caused an insufficiency in stock long after consumer demand had resumed.

Supermarkets need better information on shopping patterns and current preferences to gauge sales

opportunities for their thousands of products and brands. In addition, daily summaries of product movement and open-to-buy could improve service levels as well as problem cognizance. And, since sales respond quickly to advertising and sales promotion, such statistics can also guide supermarket operators to more effective promotional tactics.

Promotion

Four out of five shoppers read food store advertisements or handbills regularly, and most compare prices of two or more supermarkets, according to annual surveys by Burgoyne, Inc., the marketing research specialist. These consumers visit two supermarkets weekly, on average. During a typical month, the majority shop in three stores or more. Apparently, supermarket advertising performs a significant informative task for consumers.

It also is of critical importance to each store because fluctuations in patronage exert a substantial leverage on net profit. Store location and size circumscribe largely the range of profitability, the McKinsey-General Foods study discovered, but a manager can vary the net 75 per cent through a 20 per cent change in volume. No wonder supermarkets put heavy emphasis on promotion. Besides advertising in all media, supermarkets use giveaways, banners, public-address systems, and special displays.

The practice of giving premiums to induce patronage of food stores antedates the Civil War. "The most important psychological and economic fact in premium-giving is that it diverts the buyer's attention from the thing being *bought* to the thing which is being *given*," Leverett S. Lyon explained in an analysis published by the Brookings Institution.

In the 1950s the ideal method of fastening consumer allegiance to a particular supermarket was the trading stamp, which retailers have used on and off since before the turn of the century. Most stamp

plans give supermarkets local exclusivities; since brands are not interchangeable, stamp savers return to the same store because spaces in their booklet are empty. Just about everybody did save. Supermarkets with an exclusive stamp brand had at last a commercially significant device which—unlike shopping comforts or price cuts—distinguished them and could not be imitated.

Almost every major food chain fought bitterly to escape what most retailers regard as an albatross. "We fought them by cutting prices; we gave away hosiery, dishes, and dolls. We used every gimmick known—and still the stamp stores took sales away from us. We couldn't fight them, so we joined them," declared the president of The Kroger Co., now owner of the country's number two stamp, Top Value. In California several leading retailers even organized a nonfranchise stamp plan, allegedly for the purpose of destroying the stamp system,³ but the results were perverse. Although confined to California, this brand (Blue Chip) became the third largest in the country.

By 1961 stamp usage peaked at 78 per cent of all supermarkets. Many felt that availability of different brands and the rate of disbursement were excessive. In fact, the stamp industry's leader—S & H—tried to confine its franchises to a standard rate of one stamp per ten-cent sale. Some Government officials, retailing spokesmen, and social critics kept up a running barrage against stamps, promising that discontinuance would shrink prices. Outside California elimination of trading stamps has proceeded apace since 1966; presumably shoppers who no longer receive them are still waiting for prices to taper off. Members of the Super Market Institute say that in 1972 their stamp usage will plummet to 20 per cent.

In many supermarkets, stamps

Supermarkets need better information on shopping patterns and current preferences to gauge sales opportunities for their thousands of products and brands. In addition daily summaries of product movement and open-to-buy could improve service levels as well as problem cognizance . . .

³ "Blue Chip Stamp Co. Consent Judgment Approved by Court," *The Wall Street Journal*, June 7, 1967, p. 22.

were succeeded briefly by promotional games some of which were rigged, it was asserted in hearings before a subcommittee of the U.S. House of Representatives.⁴ Subsequently the Federal Trade Commission adopted regulations aimed at ending these deceptions.

Joint promotions

A more enduring promotional practice in the food trade is joint promotions with suppliers. Most of these are an allowance per case to defray a portion of retail advertising expense for the manufacturer's goods. About one-third of all offers are accepted, the U.S. Department of Agriculture found in a study of 100 major food retailers. One reason for wide usage of this "cooperative advertising" is that space costs of most newspapers are much lower to local merchants than to national manufacturers. There have been numerous abuses such as illegal discrimination by manufacturers, and fraudulent claims by retailers. These problems, too, have provoked action by the FTC.

Another problem in joint promotions is the heavy incidence of waste among the point-of-sale materials with which manufacturers deluge food stores. Arriving unsolicited, many are difficult to erect and unsuitable for the recipient. Somehow, he must get rid of the unwanted display pieces. The successful displays, however, can double or triple a brand's daily sales volume. Perhaps the main complaint about short-term promotions is that they disturb normal sales patterns. When heavy buying during a short period is offset by subsequent slack, everybody from manufacturer to consumer experiences some costly disruptions.

Altogether, supermarkets are un-

der daily pressure to stimulate sales. The average transaction still is only \$6.50. It takes a lot of customers to accumulate sufficient volume. Traditionally, a convenient location, an attractive store, and a desirable selection of groceries and produce have been important shopping criteria. They still are influential, but their relative importance has declined, partly because so many supermarkets seem alike. Of greater influence on consumers in the early '70s is fresh meat of high quality and—particularly—low prices. Hence each management emphasizes tactics which give an appearance of spectacular savings.

Pricing

To set prices on many thousands of items, in stores of various sizes and with different competitive environments, and under constantly changing demand and supply conditions, is a very difficult task. Many observers have criticized the unscientific methods that supermarkets employ. Some researchers have noted widespread recourse to rules of thumb, such as vary markup inversely with cost or volume, charge per square foot or cubic foot, sell a few leaders near cost, etc. At least one investigator of this arcane art concluded that prices seem to result from random processes.

The main problem may be that dealers do not know their products' handling costs. A functional analysis by McKinsey & Co. showed that any traditional markup formula misclassified some goods as highly profitable, whereas they really resulted in losses when direct handling costs were considered. This appears to be an area in which a team of accountants and merchandise experts can suggest material improvements in a client's profitability.

Most companies use separate

pricing routines for produce, meat, and groceries. The greatest uniformity in markup rate is in the produce section, particularly on merchandise subject to seasonal fluctuations and quality differences which hamper price comparisons by consumers. Much variation remains, of course, based on custom, pressure to move perishables, and arbitrary decisions. As in all parts of a supermarket, managers prefer numbers ending in an odd digit (like 29 cents) or multiples (two bags for 89 cents).

Fresh meat, a case of joint variable cost, is priced mainly to apparent demand. The sales potential for chuck and other popular grades, priced below average cost, determines the total quantity available. Better cuts sell at higher prices, often insulated from comparisons because shoppers equate a high price with high quality. In general, supermarkets tend to place a higher markup on items which appeal to only a small segment of their clientele.

The grocery department has the greatest variation in markup rates and techniques. Many chains use zone pricing based on the intensity of competition in each area. Nevertheless, chains are still relatively inflexible in the marketplace. The administration of chains is regionwide. Uniform practices throughout a zone facilitate control of the stores. Moreover, chains are a target for various state minimum-markup laws.

Independents, on the other hand, tend to be more responsive to local demand. Some use a competitor's price as a basis for matching, exceeding, or cutting their prices, according to basic policy. Others ignore competition, instead taking clues on appropriate merchandising, promotional, and pricing tactics from their customers.

Most householders consider them-

⁴ Subcommittee on Regulatory Agencies, 1968.

. . . whereas they really resulted in losses when direct handling costs were considered

selves expert comparison shoppers, but surveys have refuted this illusion over and over again. For example, consumers cannot name the prices at which they last bought their foods. Comparisons are unbelievably complex. One researcher needed 300 manhours to evaluate the prices in eight stores, using only 77 items. "Given complete price information, the help of computers and all the clerical help needed," the National Commission on Food Marketing conceded, "it is impossible to say which retailer in a particular community has lower prices."

Perhaps supermarkets have more pricing freedom than some executives surmise. A few companies retain home economists to help their customers get the most food value for their money; more companies are expected to seek professional advice on this subject. Studies reveal that a low-price image attracts—and holds—more customers than low prices.

In recent years, as inflation accelerated and consumers' price consciousness increased, many supermarkets have shaped their strategy around the concept of discounting. The pioneers in each area achieved substantial sales gains by a program involving the following elements:

1. Drop shelf prices in the grocery department a discernable rate—often, 7 per cent seemed to be the threshold of perception.
2. Feature "every day low prices," thereby eliminating weekend specials and saving the high labor cost of changing prices.
3. Cut number of items from 8,000 to 6,500, reducing expenses of inventory management and logistics.
4. Discontinue stamps and games.

5. Shorten trading hours and reduce services.

6. Increase advertising heavily, to expand the trading area from 1.5 to 4 or 5 miles.

7. Plan on lower profit or incur a loss for a period after the change-over.

As competitors lost sales to the discounters, they retaliated by matching the price cuts, and volume was once more redistributed among the stores. It was also learned that, while customers want lower prices even if paired with relinquishing stamps and games, they insist on a wider selection of merchandise, longer store hours, speedier checkout, and other services. As a result of these reactions from competitors and consumers, the price differential between the typical discount operation and conventional supermarket has shrunk to about 2 per cent. Some companies offset reductions in grocery prices by increases in meat. "Almost three out of five discount store shoppers think that discount store prices are the same or higher than other supermarkets," reports Burgoyne, Inc.

Unit pricing

Another recent development is pressure for unit pricing. This is one of many expense-boosting reforms that some consumerists advocate. But the vast majority of respondents to surveys on these issues express more concern for basic operating and pricing practices. Most people feel that supermarkets reap enormous net profits on sales, and that they can well afford to slash prices. This high-profit, wide-latitude image of the industry was reinforced in April, 1972, when, after a publicized conference with the U.S. Secretary of the Treasury, the presidents of some leading

supermarket chains announced substantial price cuts on meat, suspension of further price increases, etc. A few others said nothing publicly.

Organization

But the hope for lasting relief from soaring costs and prices lies largely outside the boundaries of a store. "If we really want to make possible large breakthroughs in productivity in the food industry," explained Dr. Bloom, "we must look at the movement of product from manufacturer to consumer as one system. . ."

Dependent on a cumbersome, costly maze of distribution, unaffiliated independent stores have been squeezed down to a sales share of 8 per cent. The rest is divided about equally between chains (more than ten stores under common ownership) and affiliated independents (cooperative and voluntary groups). The basic idea of affiliation is to combine the flexibility of independence and the efficiency of bigness. Usually, the store fronts of all members feature the group's name.

Under a cooperative plan like Shop-Rite or Certified Grocers, independent retailers establish a central wholesaling resource. The participants gain the advantages of mass purchasing power, jointly owned brand names, coordinated promotions, and feasibility of television advertising, streamlined data processing, and other staff services. The expense of this arrangement is relatively low. Each member retains the freedom to buy from other sources and to determine his store's other policies.

Voluntary groups are similar arrangements, but sponsored by an independent wholesaler like Super Valu or IGA. The sponsor's margin and obligations are set forth in a contract. Since dealings are at

Much . . . past success is attributable to executives with a distrust of intricate models . . .

arm's length, the ties are often looser than in a cooperative plan. In either case, success depends upon the leadership of the central staff and the commitment of the members. The participants' autonomy has handicapped some wholesaling facilities. At times, access to capital has been difficult; investment in processing machinery too risky. But overall, the cooperative and voluntary forms of organization have enabled many thousands of merchants to survive and prosper.

In the 70s, emphasis in realignments has shifted from corporate to functional. Striving to improve their efficiency, supermarket organizations are exploring new ways of combining the activities of various departments. One aim is to curtail or eliminate multiple handling, delays, and errors. Often, this leads to mechanization of manual tasks. Usage of computers is expanding from record keeping routines to aids for operational and planning decisions. How should communications and physical distribution be coordinated? Can unusual sizes and slow-moving items be relegated to regional warehouses with parallel intercompany information exchanges? These are new frontiers for company managements; systems experts are needed to help solve these problems.

Retailing will always offer opportunities for an innovator with the right market timing or for an entrepreneur with a streak of luck. During recent years various kinds of small food shops have become popular. One example is a rapid buildup of convenience stores featuring some 3,200 items such as beer, soft drinks, bread, and milk, in 2,400 square feet of space. The gross margin of convenience stores averages from five points above the supermarket. Operated on a self-service basis, convenience stores are open until very late at night.

Of the more than 16,000 convenience stores in mid-1972, one quarter are on a franchise basis. Predicts food retailing authority William Applebaum, "The majority of small food stores will give way to streamlined neighborhood convenience markets which, by staying open long hours, will provide extra time convenience." Others note a new trend toward small specialty stores that cater to consumer segments who buy geriatric, ethnic, exotic, gourmet, frozen, organic, natural, or other distinctive foods. Most experts agree that a fully automated store or centralized supply center for home deliveries based on television advertising and telephone orders will not be operational soon.

Conclusion

In the early 1970s all institutions are under attack; the supermarket industry is no exception. Its record-high gross margins make the industry vulnerable to social critics and to radically new forms of retailing. Paradoxically, its record-low net margins limit its ability to respond. Any relatively minor change jeopardizes the net or, at least, makes it swing wildly.

A review of supermarket merchandising, promotion, and pricing shows that most managements continue or extend the tactics that have made the industry great. Over the years the operators have done a magnificent job in making good food inexpensively available for the American household. The supermarket method of operation is indeed the envy of the world. In some foreign countries it is serving as a model of progress. Much of the supermarket industry's past success is attributable to pragmatic executives with a healthy distrust of intricate models that are built on unrealistic assumptions.

Yet it is significant, perhaps, that in America the top retailers outside the food trade have moved to install a different kind of management—even at a diminished emphasis on operating experience. This can be very dangerous, of course, if overdone. But in coming years the supermarket industry faces various conversions to sophisticated technology, and it needs managements that are receptive to staff men who advocate radically new approaches, conduct technical and financial feasibility studies, and install new procedures. It needs managements who have enough confidence and knowledge to tolerate occasional mistakes by the recent college graduate who lacks firsthand familiarity with wresting another cent through meat-trimming techniques but offers various analytical tools.

Supermarkets will confront and weather the mounting challenges. Since ultimate power resides in public opinion, the industry must get the facts across. But the industry cannot triumph if it blames labor unions, consumerists, trading stamps, and other proliferating vexations. Perhaps the turn of the Wheel of Retailing is best made evident through an article in the September, 1969, issue of *Progressive Grocer* entitled, "How King Kullen Went Stampless. . . . And Loved It." Actually, the article had relatively little to say about stamps which were discontinued as a by-product of King Kullen's new objectives:

1. More aggressive merchandising.
2. Improve the relationship with suppliers.
3. Restructure internal management."

Evidently, the supermarket industry is changing to a systems approach.

The food industry, which has been revolutionized in the past 35 years, may have moved so fast that it has outpaced itself. Certainly, many of its present problems are a result of its past headlong pace —

FOOD: ITS PAST VICTORIES, ITS CURRENT PROBLEMS

by Robert M. Smith

Editor

A RECENT cartoon in *The New Yorker* showed a distraught man in a chef's hat weeping bitterly in the kitchen of a large and obviously expensive restaurant. A bewildered waiter was asking one of the assistant cooks what was wrong. The reply:

"The only compliment he got today was on his instant mashed potatoes."

The situation depicted—which would only have drawn a blank stare from a reader as recently as 1935—would be instantly recognized today. Indeed, the very young would not see the humor in the cartoon at all; to them there would

be nothing incongruous in being complimented only on the instant mashed potatoes. What other kind are there?

The cartoon dramatizes the revolutionary changes that have characterized the food industry, the nation's largest, in less than 40 years—changes that have moved it from primarily a distribution process to primarily a manufacturing and marketing process. Distribution is still vital, of course, but it is definitely subsidiary to the other two functions today.

The reasons for the change, of course, are complicated but put in their simplest terms they could be

summed up in these four phrases:

Supermarkets

Suburbs

Sales

Quick freezing.

The history of this largest of American industries, which had been relatively quiescent from colonial times until World War II, thus has changed directions abruptly in the 30 years since. As such it has mixed new techniques and old rule-of-thumb principles in a strange melange of methods within the industry as a whole and often within a given company in the industry.

And the products are perishable; they must be sold . . .

As an industry it has some qualities peculiar to itself. There are giant production facilities manufacturing great quantities of a few products which must then be filtered through a distribution system to a consumer who buys only one or two units of these products at a time but must be offered a tremendous variety of them. And the products are perishable; they must be sold within a certain time period or they are useless.

Problems posed

All of this poses tremendous problems for the three major segments of the industry—manufacturing, distribution, and retailing.

They arise because of the very fundamental changes that occurred with the rise of the supermarkets in the mid-30s. Supermarkets, almost from their inception, demonstrated one thing: The average shopper, faced with goods on shelves which she could select herself, tended to buy a great deal more food than she would in a service store where she had to ask the clerk for each item she wanted. Before the rise of the first supermarkets, which were individually owned operations, the chain stores and the individually owned groceries and butcher shops and produce stores had dominated the market; the chain store units were definitely in the ascendency.

The supermarkets, housed originally in the cheapest possible premises (abandoned garages or loft buildings with old boxes serving as display counters), changed all that. The very poverty of their environment and furnishings served to underline their appeal—lower prices. It was a shrewd marketing device for a period when the country was still deep in the Depression and each shopper felt that every penny in her budget was to

be spent as carefully as possible. To allay any fears the customer might have about the quality of the food sold, the early supermarkets had one common characteristic; they carried only well-known name brands. The fact that the customer, even buying at lower unit prices, was apt to end with a total food bill higher than she would at a full service store was an unexpected dividend—for the supermarkets and for the manufacturers.

As the nation moved from the Depression into the war years, the picture changed again. People were more rushed and the idea of doing all one's food shopping at one location rather than going to a grocery store for canned and packaged goods, another for fresh produce, a third for meat became more appealing than ever. And as the Depression was ending, people could spend more than they had in the early days of the supermarkets. The traditional processed foods, canned goods with well-known brand names, were feeding the military. It represented a golden opportunity for the manufacturer and a solution for the shopper. With so many familiar foods and brands so often unavailable she could pick her substitute choices from open shelves at her leisure rather than make a hasty decision while an impatient and overworked store clerk waited for her order.

By the end of the war, it was perfectly clear that the supermarkets were going to dominate the retailing end of the food picture. The chains saw the handwriting on the wall and began closing their smaller outlets and opening supermarkets themselves. The individual Ma and Pa operation, the independent store which had once been the major retail outlet, all but vanished.

But at the same time in these years something new was added to

the brew. Home refrigerators had been around for a long time. It was possible to freeze food that the customer could store at home. It only required devices that could keep frozen food at the right temperature level in the retail outlet without sacrificing the open display principle that was so large a part of the supermarket's appeal. The refrigeration industry was not slow in seeing the opportunities, and hastened to supply the need, first with deep cabinets in which the customer had to root more or less blindfold, and then with the open refrigerated cabinet on which frozen foods could be displayed just like canned or packaged goods.

But the display units brought a new factor into the complicated food situation. Many foods had, of course, been "processed" for years. Any canned staple or any frozen vegetable is processed. But now a new novel development came along—the "convenience food" in the euphemistic term of the marketplace, or the "prefabricated food" in the far more cynical phrase used within the trade.

Packaging and shelf space

Prefabricated foods—combinations of ingredients prepackaged in a well-designed container—soon took over larger and larger amounts of shelf space in the supermarkets, which themselves had become glittering display cases for the goods they sold. The package became just as important as the contents—and sometimes even more so. And the price naturally went up, with most of the lion's share going to the manufacturers, the people who had prefabricated the food.

But meantime the supermarkets had not been idle. As the nation started its long trek to the suburbs, with its consequent dependence on automobiles, as home freezing ca-

. . . within a certain time period or they are useless

capacity became greater, the average shopper's purchases grew. The supermarkets, which had started in low rent premises in city neighborhoods, with bare tables for displays and practically no services, began to duplicate many of the peripheral services that small stores had supplied in the '20s. Checks could be cashed again. In affluent urban neighborhoods, where there was no parking space, the city housewife, like her suburban counterpart, could get by with shopping only twice or so per week. The store would deliver her purchases.

But supermarkets remained true to their tradition by having very low markups on their goods. Supermarkets have always gained their profits by sheer volume of trade.

The King Kullen supermarket in Jamaica, New York, generally considered to be the prototype of the modern supermarket, had a very simple plan of financial operations. Of 1,100 items stocked it would sell 300 at cost, 200 at five per cent above cost, 300 at 15 per cent above cost, and 300 at 20 per cent above cost. The percentages have changed, of course, but the principle still exists. Supermarkets live because of their high traffic, not because of their profit margin. (As a matter of fact, one Eastern chain, Pathmark, has just embarked on a policy of keeping all its stores open 24 hours a day, to catch the night workers, or the shopper who can leave her children with her husband during the evening but can't get babysitters during the day. Every additional customer represents additional profit. Other Eastern chains think the Pathmark action is too radical but are seriously considering keeping their own outlets open from seven a.m. until midnight each day.)

Although the profit per sale is very low in supermarkets, the profit on total amount invested has al-

ways been quite respectable. But it has been shrinking as competition has increased and store labor costs have gone up until it now stands at only 0.2 per cent of sales. A&P, the nation's largest chain, actually lost money during the third and fourth quarter of last year.

Pressure on manufacturers

All of this has, of course, put pressure on the manufacturers to set their prices as low as possible for the large chains and to simultaneously promote their own products as vigorously as possible. Yet all the promotion and advertising in the world will do no good if the product isn't stocked by the store and isn't prominently displayed in the store. The situation has become so extreme that some manufacturers make identical foods under different trade names just to ensure good shelf space for their products. If a customer doesn't like Cereal A, he might be tempted to try Cereal B, which is actually identical to A, but which may have a package or a name more appealing to the customer. Either way, the producing company gets the sale.

Unless, of course, the store wants its own brand name on the goods. Here the manufacturer can expect a slight profit on his goods but nothing like the margin he can get under his own name. Yet he's in no position to refuse to pack under the chain's label. There are approximately 35,000 food processors in the country. A large chain can always find some processor to pack its merchandise. And there goes the first manufacturer's sales to the chain of his own label. Or if he promotes and advertises so heavily that a chain simply cannot afford not to carry his brand, there goes his favored shelf position.

So, no matter how vigorously they deny it, most manufacturers

also produce private brand labels for their customers. As a matter of fact, some manufacturers produce food for other manufacturers. One of the most revealing aspects of the Bon Vivant botulism case was the number of major manufacturers for whom Bon Vivant produced canned foods, all of whom were named in the news stories that followed the botulism death that resulted from a can of Bon Vivant vichysoisse.

Thus a processor whose line is weak in some areas—canned soups for instance—may find it simpler to pay another processor who is strong in that area to produce soups for him under the first manufacturer's label rather than set up his own production facilities. This is so common in the industry that one food broker in the Mid-Atlantic area says that he seldom receives goods, even though they are all under one national name, from the same source twice.

The Bon Vivant case illustrates another problem the food industry is faced with for the first time since 1906, consumerism. In 1906, following the publication of *The Jungle* by Upton Sinclair, public reaction to the food industry practices described forced passage of the Pure Food and Drug Act and focused attention on the Division of Chemistry of the Department of Agriculture—the “poison committee,” the forerunner of the Food and Drug Administration. Once again, public reaction to a recent flood of consumerist books and stories is forcing a much-heightened interest in the Food and Drug Administration—what it does and how vigorously it does it. The books, *Food Pollution*, *The Chemical Feast*, *The Great American Food Hoax*, are uniformly critical of the Food and Drug Administration, and of the Department of Agriculture. Though there is undoubtedly a large amount of hysteria betrayed by the authors

All in all, the American purchaser, who only a few years ago shopped for food in the supreme confidence that the Government guaranteed its quality, has deep and continuing reasons for cynicism.

(one customarily refers to food company researchers as “the mad scientists”), there is a core of validity to their criticisms. Nor has the Food and Drug Administration gained much public confidence by its recent admission that it has permissible levels of filth for food products. The filth allowable includes rodent hairs, bits of insects, and other extraneous matter. This permissible level was made even more suspect when a General Accounting Office team sampling food processing plants across the country reported to Congress that a full 40 per cent of those sampled operated under unsanitary conditions, and charged Food and Drug with failure to follow up on frequent complaints, or of making such inadequate investigations that it failed to discover “rodent and insect-infested raw materials, live insects in raw materials, numerous roaches, equipment that had not been cleaned” (*The New York Times*, May 10, 1972, p. 35). The GAO recommended that Congress consider the adequacy of the FDA with the funds it now has, and promised continuing studies of the agency’s effectiveness.

So it appears that maximum permissible limits of filth may be met far more often in the breach than in the observance.

All in all, the American purchaser, who only a few years ago shopped for food in the supreme confidence that the Government guaranteed its quality, has deep and continuing reasons for cynicism. The Department of Agriculture, which attests to the quality and quantity of the actual food materials going into foods (as contrasted with manufacturing controls and additives, has long been thought to be far more solicitous of agricultural interests than of consumers’. The Food and Drug Administration is now deeply suspect of being more concerned with the interests of the processors it is supposed to regulate than the health of the consumers it is supposed to protect.

And in this election year the experienced citizen will not be sur-

prised to find many more evidences of this kind of Government shortcoming. Anything the opposition can discover to embarrass any Government department is apt to be fully aired. And, if anything, the Nixon Administration is most deeply vulnerable on the domestic front, and is widely suspect of favoring business over private concerns. The track record of the Food and Drug Administration is not something the Democrats are likely to overlook in the coming campaign.

The Food and Drug Administration, for example, has had to reverse itself in a number of cases recently, the most notorious being the use of the drug cyclamate in a number of soft drinks advertised as non-fattening.

The Delaney clause

There is one Federal law concerning the use of chemicals or drugs in foods that is explicit and simple, the Delaney clause incorporated in the Food Additive Amendment of 1958. This prohibits the use of any food additive that can be shown by scientific testing “to induce cancer in man or animals.” This was specific enough certainly and cyclamates had been shown to induce cancers in laboratory rats. The only trouble is that the tests were made in 1969 and cyclamates had been listed on the Food and Drug Administration’s “generally recognized as safe” (GRAS) list for food additives since the 1950s.

Cyclamates, which were tested first by a Midwestern university and later, after the university reports, by the manufacturer, a drug company, tested positively as a carcinogen in both cases. However, the Food and Drug Administration first banned its use as an additive, then ruled that it might be used in food if the food were labeled as a drug. The food manufacturers using the additive relabeled their products as drugs but then Food and Drug reversed itself again and banned cyclamates altogether. The processors

claimed that they had lost over \$15,000,000 in the entire process in unusable inventory of cyclamates and products containing cyclamates, in relabeling their products with the drug designation, and in withdrawing them finally from the stores where they had been shipped. They pointed out that they had been relying all along on the GRAS list and that, therefore, the Government was responsible for their losses. Now in Congress is a bill that would indemnify the manufacturers for their financial losses.

The difficulty here is in the GRAS list itself. Authorized under the Food Additive Amendment of 1958, it was compiled by FDA by a survey rather than a scientific technique. Several hundred food people and nutrition experts were asked to rate a list of several hundred food additives that by then were in fairly common use. Since most of these had never been tested or at best rather casually tested by the manufacturers using them, and since most of the experts polled were either employed in the food industry or closely connected with it, the results were predictable.

Now, however, after the cyclamate uproar and reports of heavy use of monosodium glutamate in baby foods (MSG was subsequently voluntarily relinquished by the major baby food manufacturers), a large portion of the GRAS list is under review for the first time. No one really knows what the results may be. But anything comparable to the cyclamate uproar could hurt the food processors badly.

Some food processors are already beginning to hedge their bets on the additive question, and they are not all obscure health food manufacturers by a long shot. Two of the major baking companies in the Northeast, Arnold and Pepperidge Farm, now market breads that list all their ingredients and proclaim proudly that each of them is natural in origin. One beer manufacturer, Rheingold, lists all its ingredients, asserts they are all natural, and challenges the drinker to

compare them with the ingredients used in *his* beer. Jones Dairy Farm now provides sausages with no "unnatural preservatives" and even Beech-Nut Baby Foods, which only a few years ago was deeply involved in the addition of MSG to baby foods, now makes it a point in its print and television advertising to point out that it uses nothing but natural ingredients, and that it never would think of adding MSG.

So the industry—particularly the manufacturers—may be in for rough sledding ahead. The pressure from supermarkets to prepare canned goods and frozen goods under the stores' own names, the possibility of heightened Government action against the use of drugs as additives or preservatives (already hundreds of substances on the GRAS list are under investigation), all pose potential problems for the manufacturers. And they are possibly going to be caught in a bad cost squeeze simply because of their size. Innovations are expensive to produce and market on a national scale. Yet they must be introduced continually if a company is to remain prosperous and competitive. The only solution—and the most obvious one—would be to invent and introduce new "convenience foods" on which higher prices could be charged. But it is precisely these foods that depend most heavily on the use of additives, which are themselves in danger from Government action now that the FDA is under continuing investigation, the GRAS list is being reviewed, and Ralph Nader is on the warpath.

Add to all this the very real worries about public health posed by processed foods—which have to be handled by many more workers and go through a much longer distribution line than was true 30 or 40 years ago, creating problems of cleanliness, of preservation, even of proper storage and refrigeration in the retail outlet, and one can understand the endemic cry of the entire industry:

"You can never predict anything in the food industry."

Some food processors are already beginning to hedge their bets on the additive question, and they are not all obscure health food manufacturers by a long shot.

The food service industry — which accounts for about 20 per cent of the food produced in the country — has undergone changes almost as radical as the industry as a whole. What problems do these changes pose?

THE TURBULENT FOOD SERVICE INDUSTRY

by Alfred N. Califano and Allen Weiss

Laventhol Krekstein Horwath & Horwath

EVEN A CASUAL observer must certainly have noticed a great many changes in restaurants and other food service operations since mid-century. Not that the changes began then. The origins of many developments go back a long way. But the acceleration of change that seems to have swept our society since World War II is also evident in the food service industry.

Fast food counters proliferated, along with other chains and franchises. Specialty restaurants thrived on limited menus and fixed prices: hamburgers only, or chicken only, or beef, or a choice between steak and lobster for the main course. Suburban restaurants flourished as center city restaurants faded; and the new differed significantly from the old. Department stores and shopping centers served meals to

lure shoppers and to hold them.

Serving food as a secondary activity led the airlines into volume feeding as their traffic expanded. The trend here is toward simple meals, except in those instances where intense competition leads to excesses in the opposite direction. By contrast, hospitals pay more attention to individual patients, offering them a choice of menu items. In the institutional feeding field, contractors have broadened the scope of their operations. They are to be found in hospitals and rest homes as well as factories and offices. They feed Government employees, including the military. They serve school lunches, and they run university dining halls. They are also branching out into management of recreational facilities, where food service is no

longer the main or central function.

Analysis of financial and statistical data discloses other industry characteristics that may be less obvious. The restaurant business is highly competitive. Despite many failures, new restaurants are always opening; and the competition remains keen. The 1971 edition of our firm's annual restaurant study provides an indication of the low profit margins achieved by restaurants around the country (Exhibits 1 on pages 40-41 and 2 on page 40). For example, center city restaurants serving food and beverages showed income before occupation costs equal to 12.1 per cent of sales, of which 6.8 per cent of sales went into occupation costs, leaving only 5.3 per cent of sales for net profit before income taxes. Neighborhood restaurants fared even

worse, with 5.1 per cent of sales remaining as pre-tax profit. Suburban food and beverage restaurants and "food only" restaurants did better than center city and neighborhood restaurants, but the averages cannot be said to be attracting large numbers of investors into any category. The lure must lie elsewhere.

Something does bring people into the restaurant business, as evidenced by a persistent growth in the number of restaurants in existence, despite a high failure rate. There are probably over 350,000 restaurants now, employing 2.5 million people and serving over 40 billion meals annually. Incidentally, 80 per cent are independently owned.

The food service industry has a substantial impact on the economy. It buys almost 20 per cent of all food produced in the United States; and it accounts for over \$700 million of equipment purchases annually. Besides these links to agriculture and capital goods, food service is tied to transportation, recreation, and institutions, as noted previously.

From the consumer side, there are certainly a number of factors supporting the growth of the restaurant industry. Long-term trends in life styles involve eating out more, traveling more, spending more. These activities are supported in turn by more leisure time, and by higher disposable incomes per family over the long run, sometimes brought in by a working wife who is perhaps less eager than formerly to spend time in the kitchen.

While the economic trends continue, the restaurant business, which ranks fourth among retail trade categories, will go on growing. It is only fair, then, to point out that size and growth bring responsibilities; and to ask whether a population that is fed largely by restaurants will continue to be regarded as overfed and undernourished. Or will restaurants in the future take it upon themselves to raise the level of nutrition of large groups

of people who will be eating out often?

One aspect of the nutrition question has interesting implications for other industries, including agriculture and meat packing. It has been estimated that a steer, in converting vegetable feed into meat, requires seven pounds of vegetable protein to produce one pound of animal protein. Efficient use of our national resources may suggest that our diet ought to include more vegetable protein and less animal protein. For the restaurant industry and others, an important issue may develop concerning the encouragement of new eating habits.

Industry problems

While inflationary pressures induce a profit squeeze that afflicts industry generally, some industries do suffer more than others. In the restaurant business, the profit squeeze is aggravated by three identifiable factors of extraordinary severity. Consumer resistance to price rises is more effectively exercised against restaurants, for reasons we will explore in depth. Labor costs are expected to rise faster than average payrolls for all industry. And restaurant rents are painfully high. Let's look at these three factors more closely.

While the impact of consumerism has had varying effects on different industries, there can be no doubt that customers who can eat at home have an especially powerful weapon for punishing restaurants. The original do-it-yourself activity, home cooking, has never gone out of style. When family budgets are pinched by rising prices, a natural solution is to eat out less often. Thus a restaurant becomes a whipping boy for general inflation.

Furthermore, those who continue to eat out, whether by choice or from necessity, are inclined to trade down to plainer foods, less service, elimination of extras, such as wine with the meal. When this happens cyclically, during a recession, it reinforces a long-term trend

In the restaurant business, the profit squeeze is aggravated by three factors of extraordinary severity:
. . . Consumer resistance to price rises;
. . . Rising labor costs—costs that are rising more rapidly than payroll costs as a whole;
. . . Painfully high restaurant rents.

EXHIBIT 1

	1970	1970	1970			
	All Restaurants	Food Only	Food and Beverage Restaurants			
			Total	Neighborhood	Center City	Suburban
Sales						
Food	80.3%	100.0%	74.7%	75.5%	76.0%	72.6%
Beverages	19.7		25.3	24.5	24.0	27.4
Total sales	100.0	100.0	100.0	100.0	100.0	100.0
Cost of sales						
Food*	37.8	34.5	39.0	40.2	37.2	40.3
Beverages	30.0		30.0	31.3	26.8	32.5
Total cost of sales	36.3	34.5	36.7	38.0	34.8	38.1
Gross profit	63.7	65.5	63.3	62.0	65.2	61.9
Other income	1.3	.6	1.4	.7	1.2	2.1
Total income	65.0	66.1	64.7	62.7	66.4	64.0
Controllable expenses						
Payroll	29.8	32.6	29.0	28.2	30.7	27.7
Employee benefits	3.6	3.9	3.6	3.1	4.3	3.1
Direct operating expenses	5.8	4.9	6.0	5.9	6.3	5.6
Music and entertainment	.9	N	1.1	1.3	1.1	1.1
Advertising and promotion	1.7	1.7	1.7	1.8	2.0	1.2
Utilities	1.8	2.1	1.6	1.7	1.5	1.8
Administrative and general	5.2	3.8	5.7	5.8	6.5	4.5
Repairs and maintenance	1.6	1.3	1.7	1.5	1.9	1.6
Total controllable expenses	50.4	50.3	50.4	49.3	54.3	46.6
Income before occupation costs	14.6%	15.8%	14.3%	13.4%	12.1%	17.4%

toward simplicity and informality. Young people, whose significance in the market is already important, and whose generation will gain greater influence, seem to prefer the limited menu, few courses, and do-it-yourself salad making of the currently flourishing specialty restaurants, while luxury restaura-

rants with elaborate service appear to have passed their peak.

Elegant dining is out, simple fare is in, and still the trading down continues. Thus the restaurant business is hit doubly hard in times of economic stress. Not only does the industry lose the patronage of the stay-at-homes, but it also finds that the average check slides downward.

At the same time, persistent labor shortages have plagued the industry, largely because of traditionally low wage policies and poor personnel practices. Minimum wage exemptions for the industry have helped to hold costs down, but when restaurants must compete with other industries to attract scarce labor, the outlook can only be for faster pay raises to catch up

with the more common pay scales.

The low wages of the past were made possible by reliance on marginal workers drawn from the low end of the economic scale. New immigrants and untrained workers provided the labor pool for the industry. These sources are drying up. There are no new waves of immigrants from poverty-stricken parts of Europe; minority groups are making strong efforts to improve their lot; and training programs prepare the poor to increase their earnings and share in the American dream.

Meanwhile, mounting pressures have encouraged the mechanization of kitchens: for instance, mechanical dishwashers and potato peelers are prevalent. Methods have improved, too, with the aid of indus-

EXHIBIT 2

Occupation Costs
—Ratio to Total Sales

	Food and Beverage			
	Food Only	Neighborhood	Center City	Suburban
Rent	4.0%	5.9%	4.1%	5.0%
Property taxes	.8	.8	.5	.8
Property insurance	.5	.4	.4	.3
Interest	.5	.8	.7	1.2
Depreciation	2.6	1.5	1.8	2.7
Total	7.3%	8.3%	6.8%	8.3%

**Restaurant Operations:
1970 and 1969
Summary Profit and Loss
Ratios**

N=Negligible

All Restau- rants	1969				
	Food Only	Food and Beverage Restaurants			
		Total	Neighbor- hood	Center City	Suburban
80.2%	100.0%	74.3%	73.5%	75.8%	73.1%
19.8		25.7	26.5	24.2	26.9
100.0	100.0	100.0	100.0	100.0	100.0
39.0	37.2	39.6	41.0	38.1	40.7
29.9		29.9	32.2	27.6	31.2
37.2	37.2	37.2	38.6	35.7	38.2
62.8	62.8	62.8	61.4	64.3	61.8
1.1	.3	1.3	.7	1.2	1.9
63.9	63.1	64.1	62.1	65.5	63.7
29.6	33.0	28.6	27.6	30.2	27.3
3.6	4.4	3.4	3.1	3.8	3.1
5.9	5.3	6.0	6.2	6.3	5.5
.8	N	1.1	1.3	.8	1.2
1.7	1.8	1.6	1.5	2.1	1.1
1.7	2.0	1.6	1.6	1.5	1.7
5.5	4.3	5.9	6.0	6.8	4.6
1.5	1.4	1.6	1.4	1.7	1.6
50.3	52.2	49.8	48.7	53.2	46.1
13.6%	10.9%	14.3%	13.4%	12.3%	17.6%

*Before credit for employees' meals

trial engineers applying the techniques of job analysis to food preparation. Better layouts have enhanced efficiency and reduced labor requirements. There remains a need to infuse meaning into restaurant work, with special emphasis on the more menial tasks.

In addition to consumer resistance and labor shortages, restaurants are subject to another major factor exacerbating the profit squeeze: the high cost of space. Efforts to alleviate the impact of high rents have led to reduction of kitchen space and enlargement of the serving area. While equipment and layout have undoubtedly helped, a basic anomaly remains: as a retailer, a restaurant is required to pay for a good retail location; and its kitchen, which is

essentially a production activity, must also bear the burdensome rental costs of a good retail location.

While our discussion has focused on the problems of restaurants, institutional feeding is affected by analogous problems, particularly in regard to labor shortages and rising pay scales. Accordingly, as we turn to solutions, we may broaden our scope once more to the entire food service industry.

Convenience foods

The food service industry has been turning to convenience foods (prefabricated, pre-cooked, or frozen foods) as the principal solution to the problems of the profit squeeze. This is a good solution. Convenience foods do indeed offer

substantial benefits to the restaurateur and the institutional feeder.

Despite the higher price tag on prefabricated items, their use can cut a restaurant's prime cost. Butchered cuts of meat may cost more than larger sections, but they obviate the need for a butcher on the premises. Frozen foods may cost more than regular foods, but there is less waste from overbuying or overproducing. Unused portions simply remain in the freezer at the end of the day. Pre-cooked items may cost more than uncooked ingredients, but they can be heated and served by unskilled workers, replacing higher priced chefs.

By requiring fewer people with lesser skills, convenience foods do more than merely reduce the total cost of kitchen labor. They allevi-

ate problems associated with labor shortages, high turnover, and absenteeism. The result is a welcome relief to restaurateurs.

How is it done?

Nevertheless, a question still remains to be answered: How is it done? How can a food processor prefabricate or prepare dishes and deliver them to a restaurant at a price low enough to permit saving on labor by the restaurant to bring its total prime cost down below its previous level?

The answer lies partly in the food processor's freedom from a built-in kind of inefficiency that besets a typical restaurant. In a restaurant, demand, production, and consumption are so close to simultaneous occurrence that much employee time is lost in waiting for customers' orders to come in. To be sure, advance preparation can tend to level peaks and valleys of activity. But beyond a certain point, advance preparation runs a risk of its own: the risk of creating waste through overproduction. In the end, while the problem of wasting time may be ameliorated by planning, a complete solution is not available to a restaurant operation. Lost time cannot be eliminated entirely.

Another important reason why



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processing plant costs are substantially lower than restaurant production costs lies in economies of scale. With considerably larger operations, the processor can install more efficient equipment and better methods. Even while paying higher wages, he can come out ahead by keeping his people employed full time at the highest level tasks they are capable of. He makes quantity purchases at lower cost. And his receivers handle bulk shipments more expeditiously.

That isn't all. The processing plant can utilize joint products economically. After butchering sides of beef, the processor can divert chop meat and stew meat to certain markets among those he serves over a wide area. Maintaining a balance among outlets requires effort, but it need not be an especially troublesome problem. Additionally, disposal of waste is more efficient. Tallow for soap, and scraps for animal feed or fertilizer may be offered in quantity, and in good condition, for ease of transportation and use by the purchaser. At better prices, of course.

Furthermore, the processor has available to him another source of saving. He can hold his space costs down by locating his plant in a low rent area, and also in an area where the labor he needs is abundant. In short, the processor has many more opportunities for reducing costs than are available to the restaurant: in purchasing, receiving, processing, and marketing; in raw materials, labor, and overhead.

To get back to the restaurant or institution for a moment, convenience foods can mean lower prime cost for them, as we have seen. In addition, convenience foods offer savings in overhead expense items. Investment in kitchen equipment can be reduced substantially when a new facility is built for serving convenience foods and less space may be allocated to the kitchen. Savings in maintenance, depreciation, and rent can be significant. Moreover, there are savings to be realized in supervisory staff and in purchasing activities.

There is another aspect of this use of convenience foods, though, that is being developed by some traditional restaurants that pride themselves on their cuisine and dislike serving commercially prepared food. Some of these restaurants are beginning to experiment with their own convenience foods and food ingredients which they prepare in large batches, freeze, and then assemble into complete meals as they are needed. This can be done in low rent quarters away from the restaurant proper if kitchen space there is limited. As long as the restaurant has sufficient freezer space, it gains the advantage of lower or at least equal costs to those it would pay for commercially prepared food; it can give its customers fresher food; and it can preserve its own individual character better by using its own distinctive recipes and its own natural ingredients. Since such advance preparation can easily provide enough food for one or two weeks' meals, it can be done with a minimum number of high-cost chefs who prepare the food in bulk. Lower paid workers, when it comes to actual serving of the customer's meal at the restaurant, simply assemble the necessary ingredients and heat them.

Major airlines also, especially on overseas routes, find that they can maintain quality control more effectively while holding costs down by preparing convenience foods themselves at a limited number of kitchens for distribution through the system on deadhead flights.

Similar methods are being tried on an area basis. A group of Midwestern hospitals has banded together, for instance, to establish a central food processing plant. Foods and ingredients are processed at the central point, frozen, and then shipped to each member hospital, which can then assemble patient meals, insert its own seasoning and spices—if the individual patient's diet permits them—and prepare tasty meals at low cost.

Such area plants are also a possible development for restaurants in remote areas or sparsely settled regions which depend now on commercial prefabricated foods but which simply do not have enough demand for certain exotic items to order them economically through a food broker. With their own centralized kitchen serving two or more restaurants, the same process can be followed; fresh foods can be prepared, frozen, and shipped to the client restaurants. The long shelf life that requires the highly criticized use of artificial preservatives in commercially prefabricated foods is not necessary, the restaurant owners can control the cleanliness of their food from start to finish, and their restaurants can offer gourmet fare prepared by talented cooks at the central processing point.

The systems approach

For a food service activity to take full advantage of the opportunities for improved operation at the lower cost that convenience foods—either commercial or its own—offer, there must be a coordinated approach that plans for consistency between functions. Equipment must be the most efficient type for handling convenience foods. Staffing must recognize the lower requirements for skilled personnel. Marketing efforts should be directed at those market segments most likely to respond favorably to the appeal of the menu that is offered.

To be specific, the specialty restaurants that offer few selections (like steak and lobster), few courses, and a salad table, have found a following among young people; so they offer those things that the young people want. Casual dress is preferred by the young market, and casual dress is permitted by these restaurants. Attractive furnishings lacking in elegance suit the tastes of the same market segment. So does advertising that features fixed prices for entire meals. Such advertising policies help a young family to stay within

its budget when it goes out to eat.

Actually, the systems approach is applicable to all restaurants of all types. What we have said of one type of restaurant is merely an illustration of how a general policy is applied. To take another example, perhaps at the opposite extreme, with elaborate service must go elegant dishes, tasteful decor, dignified surroundings, and seemly attire. Since prices will be high, marketing efforts must be directed toward those who have the money to spend and an interest in spending it on luxuries. The objective of such a restaurant should be to make a concerted effort to provide its customers with a dining experience.

For new restaurants preparing to serve convenience foods, there is a real need for greater coordination than now exists between equipment manufacturers and suppliers of food. Since the restaurateur must plan a consistent operation, he needs coordination between those he must call on to meet all his requirements. The equipment that is installed should be exactly suited to the characteristics of the foods that are to be served.

Summary

Along with much of our society, the food service industry is changing. In part, the changes are designed to meet the preferences of a new generation that likes casual surroundings and wholesome food that is moderately priced. In part, the changes are necessary to cope with industry problems of long standing, problems connected with profit squeezes and labor shortages.

Convenience foods are playing an important part in solving the industry's problems, primarily because they require less labor, less skill, and less kitchen space. Specialty restaurants using convenience foods have also been found to appeal to large new markets. Their success is attributable in part to adherence to the systems approach, whereby all functions combine to make a consistent whole.

. . . there must be a coordinated approach that plans for consistency between functions. Equipment must be the most efficient type for handling convenience foods. Staffing must recognize the lower requirements for skilled personnel. Marketing efforts should be directed at those market segments most likely to respond favorably to the appeal of the menu that is offered.

Better packaging, better nutritional content, improved test marketing models, and much closer attention to the needs, desires, and attitudes of consumers characterize food processors today —

FOOD MANUFACTURING: PRODUCTS, PROBLEMS, PROTESTS

by Louise H. Dratler

Associate Editor

IF THE CONSUMERISTS have achieved nothing else, they have managed to seal the mouths of food manufacturing executives so that it will take more than the most modern can opener to get them to reveal too much about what is going on inside their industry. Whatever is not being kept secret for fear of competitors finding out is being kept secret for fear of consumerists getting wind of something. One trade publication¹ recently stated, "Happiness is . . . spotting trouble before Nader."

How do the manufacturers view their customers? Fred Posner, marketing research and information manager for the Jell-O Division of General Foods Corporation, recently told the American Marketing Association, "The consumer we are working with and for in this decade

of the '70's will: *Have more* affluence, leisure, sophistication; *Want more* pleasure, broader horizons, greater self-expression; and *Know more*, be attuned to what's happening throughout the world."

In more specific terms, he said that homemakers are looking for convenience, variety, and novelty in their grocery choices.

The consumer's affluence is being depended upon by Beech-Nut to offset the decline in birthrate that may affect its baby food business. George P. Maginness, vice president-finance and planning, said in the Squibb Corporation's 1971 annual report, "The U.S. population continues to grow, of course, and rising affluence should more than make up for any lessening of demand caused by the lower birth rate, assuming it is a permanent trend."

Judson Gooding, writing in *For-*

tune,² pointed out that "For the manufacturers, the sought-after characteristic in new food products is a high degree of added value beyond the cost of the commodity itself, so that unit profit will be less vulnerable to commodity-price fluctuations."

He was writing about Heinz's recent additions to its product line that differed only in size of container from previous products. In this way the manufacturer was able to get increased shelf space in the retail stores for the same products it had offered in the past.

Beech-Nut did the same with its chewing gum. George M. Perry, the company's president, said,³ "Engi-

² Gooding, Judson, "Heinz Battles for Space on a Worldwide Shelf," *Fortune*, October, 1971.

³ Squibb Corporation, *Annual Report* 1971, p. 16.

¹ *Grocery Mfr.*, June, 1971, p. 82.

neering improvements produced significant manufacturing economies and made it possible for us to introduce eight-stick gum before our competitors could market their larger packs." The corporation maintains that the eight-stick pack at a suggested retail price of ten cents is a better consumer value than the traditional five-stick packs at seven or eight cents.

"No one buys packages per se, you know," said Norman A. Vanasse, manager of the packaging corporate purchasing department for General Foods Corporation.⁴ "But the total product in its packaged form represents a value to the consumer—be it convenience, ease of use, or whatever." He suggested eight packaging criteria that go beyond traditional packaging design standards:

"Our new package must offer the ultimate in convenience . . . ; Our package must jibe with changing mealtime practices . . . ; New packaging which incorporates novel but useful features will gain ready consumer acceptance; Product and packaging innovations won't tempt the cost-conscious, more sophisticated consumer unless she can recognize that she's getting what she pays for" [i.e., packages that have reuse value].

"Packages must fulfill consumer needs for variety, for ease of use, and disposal; Individualized decorative packages should provide a marketing advantage among consumers who, more and more these days, feel the need to accentuate self as distinguished from others; Consumer concern for food ingredients and a product's contribution to health and nutrition will call for more information . . . on the package; New packages must be designed with ecological considerations uppermost in mind."

New products are at the heart of the food manufacturing business. It has been estimated that within ten years about one half of all the

products now on the grocers' shelves will be replaced by new ones. Approximately 12 per cent of the yearly dollar volume of the retail food business is spent for products not in the stores the year before. Obviously, more than just packaging changes are taking place.

High-protein products are being developed. ITT Continental Baking Co. has developed a snack cake (Hostess Astrofood) that it claims when served with a glass of milk has the nutritional value of a four-ounce glass of orange juice, one egg, two strips of bacon, one slice of bread, and a pat of butter. The breakfast cake was designed to meet the Government's 15 cent allowance for school breakfasts (seven cents for milk and eight cents for the Astrofood cake).

General Foods has developed a high-protein pasta, Golden Elbow macaroni, that has been approved by the U.S. Department of Agriculture for use in lunches and suppers served in its Child Feeding Program. This product is not available to the general public on the retail level because it does not fit into the present Food and Drug Administration definition of "macaroni." A G.F. spokesman explained that the product would have to be called "imitation macaroni" since it is not entirely a wheat product, containing soya and corn flour as well. There is a possibility that the FDA will permanently suspend its definition for the product (at the moment it is temporarily suspending it) and then the company will go ahead and launch a full-scale advertising campaign for Golden Elbow. The G.F. spokesman indicated that "the macaroni lobbyists" are preventing this FDA classification decision.

Test marketing tips

How does a company decide if its new food product is going to be a success? Test marketing. It's a costly operation that General Foods is trying to replace with its "TM" system, a computerized projection system that would do away with

"Our new package must offer the ultimate in convenience . . . ; Our package must jibe with changing mealtime practices . . . ; New packaging which incorporates novel but useful features will gain ready consumer acceptance; Product and packaging innovations won't tempt the cost-conscious, more sophisticated consumer unless she can recognize that she's getting what she pays for" [i.e., packages that have reuse value].

⁴ Remarks before Product Innovation-Canada Seminar, Muskoka, Ontario, September 30, 1971.

A strong appeal to a homogeneous group of 10 per cent of the population is often better . . .

standard test marketing procedures for its nationwide operation.

Until the system is perfected, some general guidelines for effective testing were outlined by the corporation's Fred Posner.⁵ When a market researcher presents a company with a product rating (such as 4.3 on a scale of 1 to 6) the company should remember, "product ratings are not volume measures because volume involves depth and breadth of concept appeal and measures of sustained use/interest," the G. F. executive said.

Mr. Posner explained, "We all know that traditional product testing cannot forecast volume. While traditional tools are adequate for screening out obvious product deficiencies, they generally are not sensitive enough to identify a product which, on the surface, appears acceptable, but which, over time, might fail because of customer apathy." He warned that often consumers can fall into the frame of mind in which they say, "It's a good product, but I don't have the need for it very often."

"A compelling concept" has to be worked out first so that, properly analyzed, consumer response to the concept will give an idea of the size of the trial potential, he advised.

"Greater experimentation in working with expected frequency of use and other information obtained from product testing could provide additional insights in making judgments about repeat volume," Mr. Posner said. "Some statistical models could emerge that would relate product testing information to volume, even if only on a gross basis. I might add that making these judgments on trial and repeat

based on product testing information and then monitoring market performance should enable us to refine the models (while building our case histories)."

The General Foods marketing research manager also suggested that exposure testing over extended periods of time be used and that a homogeneous segment of the population be appealed to.

"A strong appeal to a homogeneous group of 10 per cent of the population, for example, is often better than a moderate appeal to a diverse 80 per cent of the population. And this certainly has impact on volume potential. For with a message and a product specifically tailored to the homogeneous group, we probably have a better chance of gaining the kind of compelling commitment necessary for the volume we seek," Mr. Posner said.

Nature still plays role

Once a successful product is developed the manufacturer's problems are far from over. Mother Nature still manages to dominate the economic life of the food manufacturer. Sometimes less dramatically, as in the case of CPC International's losses because of a threatened corn blight, but sometimes more dramatically, as in the case of Campbell's losses because of its recent spoilage scare.

In its 1971 annual report CPC explained that as "the world's largest commercial user of corn" its management must always ensure it has sufficient supplies of corn available to the company. An executive task force estimated that in 1971, 65 per cent of the corn planted of that year's harvest would be susceptible to damage by recurrence of Southern Leaf Blight. These predictions of a widespread blight were confirmed by university, Gov-

ernment experts', and field reports.

"To protect production," the report explains, "CPC purchased more corn in advance than its normal level. If the blight had matured, the corn crop would have been drastically reduced in size and the company's supply . . . jeopardized. Since the blight did not occur and record acreage had been planted—in itself a hedge against a repeat of the blight—a record, price-depressing corn crop appeared instead. Consequently, CPC was left with a quantity of high-priced corn." Nature's whim did not damage the company too badly; it managed to declare the same dividend per share that it had the year before, but it must have given some CPC executives a few more gray hairs.

When product spoilage at Campbell's Paris, Texas, plant forced the recall of the company's products at over 103,000 retail food outlets, it cost the company \$2 million in earnings after taxes.

"It is our estimate that this product spoilage episode," Campbell's President W. B. Murphy said, "cost us approximately \$10 million gross or \$5 million net, or 15¢ per share considering the recall costs, the extra freight, the lost business due to out-of-stock conditions, the inventory inspections, excessive overtime pay, etc."

According to Campbell, the product spoilage occurred because of four conditions interacting: above-average viscosity of the can contents; over-fill of the can; incomplete hydration of the dry ingredients; and a canning process being used that involved a higher rate of agitation for a shorter period of time than was traditionally used. Since the spoilage incident, the shorter canning process has been abandoned.

"Needless to say, this most unusual occurrence had an effect on

⁵ "If Product Testing's the Answer, Then What's the Question?" delivered before the American Marketing Association, January 20, 1972, New York City.

. . . than a moderate appeal to a diverse 80 per cent of the population

our business," Mr. Murphy said. "First, there was a major distortion of our sales force work for nearly a month. Shipments from the Paris plant were held up for many weeks while a can-by-can inspection was made of the inventory with the result that the southern territory sales had to be taken care of by other plants. This depleted inventories at a time when we were engaged in packing tomato products. We have been unable to fill orders for as many as 45 to 50 products at times, despite much overtime work. All told, over a million and a half cases of orders have been cut . . . for lack of inventory."⁶

Planning for growth

How is planning done when things are running smoothly, i.e. natural causes do not interfere with business as usual? Many companies are reticent to talk about the planning operation for fear of giving the ever-vigilant competition a bit of information it did not have already. ITT Continental Baking Co., however, has been willing to risk that possibility, and a report about its operations was published last year.⁷

The company uses the ITT Continental Annual Budget, Forecast, and Business Plan system that starts budgeting right from the driver-salesman level. The driver-salesmen are each asked to budget sales, stales, gas mileage, new business, etc. These estimates are reviewed and coordinated at successively higher management levels until a total business plan is worked out by the plant manager, including details on all necessary activities

⁶ The President's Address at the Annual Stockholders' Meeting, delivered November 19, 1971.

⁷ "How ITT Continental Builds for \$1 Billion Sales in Bread, Cake, Snack, Frozen and Other Foods!" *Bakery and Marketing*, September, 1971.

and responsibilities for achieving the projected budget. Quarterly, detailed forecasts are made from the route level up and meetings of branch and sales managers are held to review the past quarter's performance as compared to the projected budget. Sales performance is analyzed weekly. If a route is not reaching its goal, stop-by-stop dollar value goals are set and a supervisor assigned to stay with the route until the goals are met.

The sales and profit goals are set for the regions in ITT Continental's headquarters in Rye, N.Y. Generally the annual goal is set at 15 per cent growth. Then the regional directors negotiate the goals with their plants. The regional office performs quarterly audits of the plants on product quality and production, sanitation, engineering, safety, and building maintenance and repair. The plants send monthly report letters to the regional offices as well as weekly profit and loss statements.

ITT Continental Baking has had its share of troubles too. While Nature has been kind, the Federal Trade Commission has not. It charged Continental with making improper nutritional claims in its Wonder Bread, Hostess snack cake, and Profile bread ads. The FTC charged that Wonder Bread could not claim nutritional values unless they were different from those of other breads, that the Hostess ads' nutritional claims were unsubstantiated and did not mention the percentage of sugar added to the cakes, and that the Profile ads made the bread seem to be a diet food.

Cab Woodward, ITT Continental president, in explaining his company's position on the FTC charges, said, "Ironically, since the post World War II days of Lee Mar-

shall, who continued war-time mandatory enrichment on a voluntary basis in the belief that the industry would follow, Continental has been a strong, consistent advertiser of nutrition. It did so through many years, when this theme was thought by many to be a poor marketing concept."⁸

More consumer awareness

Talking nutrition is now a very "in" thing for the food manufacturers. Many will send the inquiring homemaker booklets about nutrition. CPC International is printing nutritional information and open dating on its Skippy peanut butter labels. It has even gone so far as to establish a "Food and Nutrition Press Information Service."

*Grocery Mfr.*⁹ reported last year that many "high-level trouble shooters" have been appointed in food companies, probably to handle irate consumerists. Swift has created the post of director of public responsibility to "keep management advised on developments in ecology, nutrition and consumer interests, and suggest action programs," a large assignment.

The food manufacturers are well aware that a growing number of consumers are suspicious of them. Speaking at the Fifth Annual Marketing Roundtable of *Grocery Mfr.*¹⁰, one manufacturing executive, tired of hearing lectures on the need for focusing on profits, said of consumers, "one of their great fears—especially among the young who are mistrustful of many industries—is that profits are not only the number one priority, but the only priority of big business. Consumer groups know we are in business to make a profit; they hope we are in business to do some other things too."¹⁰

⁸ Ibid.

⁹ *Grocery Mfr.*, June, 1971, p. 82.

¹⁰ *Grocery Mfr.*, March, 1972, p. 34.

*The story of how one CPA firm made it possible
for one client company to change —*

FROM MERCHANTS TO MERCHANDISERS

by Michael H. Hagler

Alexander Grant & Company

THE ABC COMPANY started its life as the branch office of a long-established European food trading firm during the First World War. Arrangements with domestic growers soon expanded into a domestic fruit business in this country but still the major part of the company's work was devoted to supplying American products to the parent European concern.

With the outbreak of the Second World War the company picture changed rapidly. The European concern was all but destroyed, its offices closed, its warehouses bombed out of existence. The American operations became the center of the complex. As such the American operation spread itself rapidly. It had already become a manufacturer on a small scale with the establishment of a packing company in cooperation with one of the large domestic fruit growers with which it had been dealing, and just before the war began it had established a working relationship with Cuban interests. With normal trading patterns disrupted

by the war, the American company spread its interests to the Western Hemisphere, and set up branches of its own in South America.

After the war, the ABC Company found itself more or less transformed from a small branch office of a European concern to a small but flourishing manufacturing and importing company, marketing many of its foods under its own label. Cuban produce had by now become a large part of its business, and just before Castro completed his revolution, sales passed the million-case level.

Castro's revolution was successful, however, and ABC found itself without its most important source of supply. It had enough other products it was handling to weather the crisis and soon found new sources of supply.

So far, the company had sold most of its packaged goods under its own brand names with a percentage of its sales made to other food processors and packers who put the products under their own labels.

One vital difference had begun to appear, however. Whereas most of the ABC Company's old imports had been marketed under their own brand name, and had been slightly exotic in nature, so that a market could be found for them no matter how much was brought in, now the nature of their business was changing. From marketing commodities, where the nature of the crop—and the size of the crop—could affect their marketing plans radically, they were gradually moving into the marketing of staples, where long-range planning was essential—and possible—where the food had first to be grown, then processed, then marketed here.

United States weather conditions in any one season can have a tremendous effect on the price manufacturers must pay for their raw materials. The ABC Company saw its opportunity and developed foreign sources in a variety of countries prepared to pack products meeting American specifications (in some cases even particular com-

pany specifications). Because of the number of countries dealt with by ABC, weather or growing conditions in any one country could be handled by switching to another source of supply.

But this transformed the former small importing company into a major bridge between manufacturers abroad and food processors in this country. It had, in effect, become an essential link in a manufacturing process, something it had never been before. It knew importing; it knew how to negotiate letters of credit, how to ship goods; how to ensure that the foods it imported met U.S. Food and Drug Administration requirements; it knew distribution and marketing within this country.

The one thing it didn't know was how to forecast demand within the country for the goods it was importing. It had been moving and growing almost too fast to learn. Some materials it imported and marketed were handled through food brokers and some it sold to food processors; supplies had to be contracted for months in advance if the processors—both domestic and foreign—were to keep their production lines busy.

This is where they came to us for help: They needed it.

We found that each of the products ABC imported and sold had its own product manager. We found that none of the product managers had any valid manner of predicting sales of his line; he would do it intuitively, and he wouldn't share the results of his intuition with company management, the other product managers, or the accounting department. So the cash flow position was chaotic—especially as the company, like most importing concerns, paid for the produce overseas, paid the shipping costs to bring it to this country, paid distribution costs to food brokers' warehouses within this country, and only invoiced the final customer when he had accepted the goods.

This was a small company. A computer and the right system

would have gone a long way toward solving the problem but a computer wasn't economically justified. We also felt the main problem lay in the lack of scientific planning on the part of the product managers, many of whom never even referred to records of what their sales had been in the past year, much less in the previous quarter. Their standard answer to queries about why they didn't refer more carefully to their own records was that it wouldn't do any good: nobody could ever predict anything in the food business.

We felt the thrust of our work should be on developing a more rational attitude toward sales forecasting. If that could be done successfully, some of the other handicaps the company suffered would fall into place quickly enough. Purchasing could be geared to the sales forecast, funds could be planned to cover the necessary purchases, deliveries could be made on time and in sufficient quantity to meet processors' production responsibilities.

So we worked out a number of simple forms to aid the product managers in making reasonable forecasts. The company's major lines were divided into two main product groups, basically those products which were repacked by others or were used in the processing of others and those that were marketed primarily under the company name. We then prepared a sales forecast analysis and adjustment schedule for each product line with actual sales for each month of the previous year noted horizontally across the top and columns under each month for the current year (Exhibit 1, pages 50-51). Each product manager was asked to forecast sales for the current month, actual sales were recorded as the month ended and the variance between the forecast and the actual sales recorded.

This was done for each product line. Now the product managers could no longer rely on intuition as they had in the past. There were the actual sales of their product for the same month the

previous year recorded on their forms. If their sales forecast for this year was significantly different, they had to ask themselves why. Did the product show seasonal peaks and valleys in sales for the previous year? Why? Were there any new factors that might affect sales this year? What were they?

In other words, each product manager was being forced to make his forecast on a more scientific basis than he had in the past. He could see each month how close his sales forecast had been to actual sales. If any trends were developing, the chart made it clear to him.

Naturally, the sales forecasts started to become more accurate and as they became more accurate the company could itself begin to develop more meaningful figures for inventory and purchases as well as delivery commitments. The form shown in Exhibit 2, page 52, was developed to show the monthly status of inventory, of inventory for the previous period, of the sales to date, and of the purchases to date. The last two categories were the most significant ones—the 12-month running sales forecast schedule and the consequent 12-month running purchase commitment schedule. This was summarized in tabular form for all company products, showing inventory of each for each month, change in inventory from the previous period, sales for that period, three-month sales forecast, and three-month purchase forecast, and, finally, what inventory should be as of that future date if sales forecasts were met, Exhibit 3, page 52.

This was a forecasting and planning tool, of course, but for far more than sales. Now the company

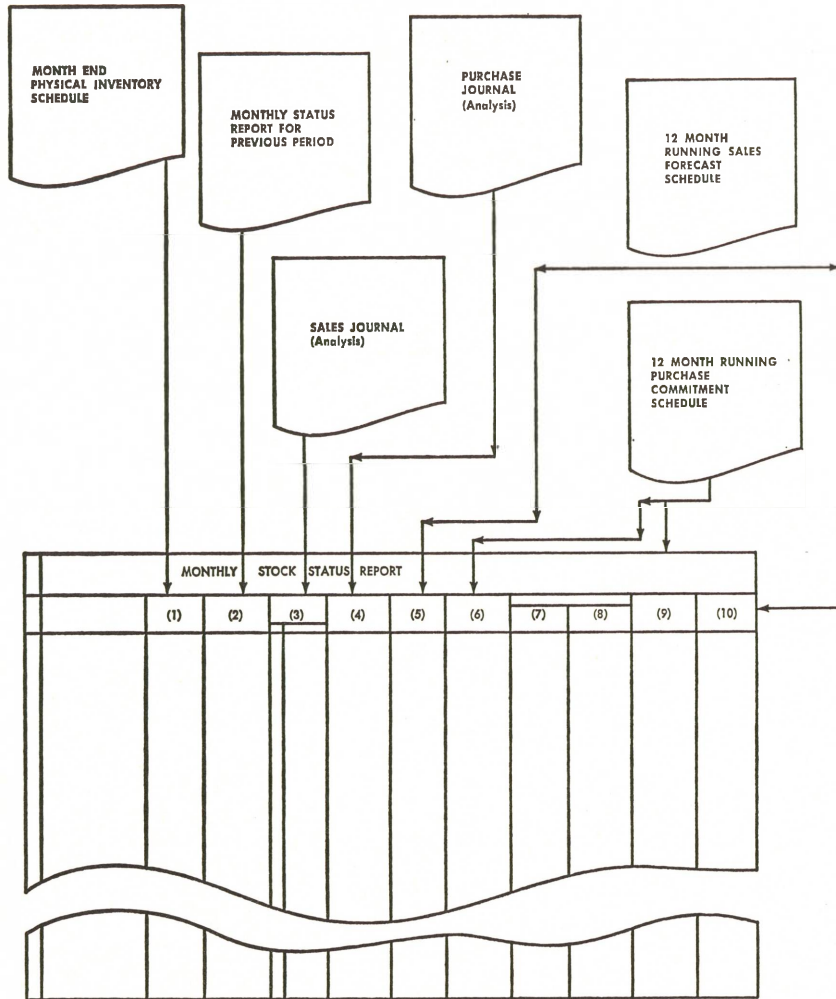


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EXHIBIT 2

ABC COMPANY, INC.
MONTHLY STATUS REPORT
SOURCE DATA FLOW DIAGRAM



had for the first time a rational basis on which to buy the semi-finished materials which it in turn sold to

processors. And as sales forecast accuracy improved, all the other figures—commitments to buy, anti-

ipated overages or shortages in inventory—improved as well. For, as the sales managers gained more familiarity and more confidence in the simple forecasting tool that had been supplied to them, as their sales forecasts came closer each month to the actual level of sales for that month, they would begin projecting their forecasts farther and farther into the future. This could make it possible for purchasing to buy its supplies at the most advantageous season and to ensure that inventory levels were always adequate to meet demands.

The monthly sales forecasts and actual sales figures were also summarized by years in graph form showing actual against forecasted sales for all products (Exhibit 4, page 53) as well as in tabular form (Exhibit 5, page 53) showing forecasted sales against actual sales for the previous year. All of these reports gave management a chance to spot trends almost as soon as they began to develop and to take action either to counteract them or exploit them.

Strangely, the product managers who at the beginning wouldn't even reveal their sales forecasts to each other began to pride themselves on the accuracy of their forecasts as soon as they were given a planning instrument to work with. The tabular graph (Exhibit 5) for all

EXHIBIT 3

ABC COMPANY, INC.
MONTHLY STATUS REPORT

Month ending _____ 1971

Commodity	(1)	(2)	(3)		(4)	(5)	(6)	(7)		(8)	(9)
	Inventory as of / / 71	Change from previous period (decrease)	Sales for period			3 month sales forecast ending / / 71	3 month purchase forecast ending / / 71	Projected inventory status as of / / 71			9 month sales forecast ending / / 71
			\$	%				Long	Short		
Product Line I											
Product A	\$	\$	\$			\$	\$	\$	\$		\$
Product B											
Product C											
Product D											
Sub-total											
Product Line II											
Product 1											
Product 2											
Product 3											
Product 4											
Sub-total											
All others											
TOTAL	\$	\$	\$			\$	\$	\$	\$		\$

sales shows how closely their forecasts matched reality. The peak in sales was reached a little earlier than their forecasts but only two months earlier, and certainly that discrepancy was analyzed and evaluated in making the next year's forecast.

What the forecast did show very clearly was that, despite the pessimistic warnings we were given when we first accepted the assignment, it is as possible to forecast in the food business as it is in any other.

This was not a very big or complicated assignment. But it did give the company the tools it needed to do a better job of sales planning and purchasing and, ultimately, of management planning and control itself.

And with this the one time merchant-importers had taken the essential first step toward becoming a link in a production process, and an important link. It had been done with no hurt feelings on the part of personnel—the product managers hadn't been forced into feeling they were competing with each other when their sales forecasts were first made public. And, in any event, it wouldn't have made too much difference. For as soon as they were forced to make sales forecasts on the basis of past figures—and to justify any radical departure from the trends revealed by the past—their sales forecasts became amazingly better.

In essence, this was a basic application of management science, without the imposition or suggestion of any detailed, complicated plan. Nothing could have been simpler than the measures we proposed, yet they accomplished almost everything we and the client could have wished. With the product managers no longer guarding their forecasts jealously, every other financial and management situation in the company became easier and more precise. The company's old haphazard attitude of "we can't predict anything in this business" became a more rational approach.

EXHIBIT 4

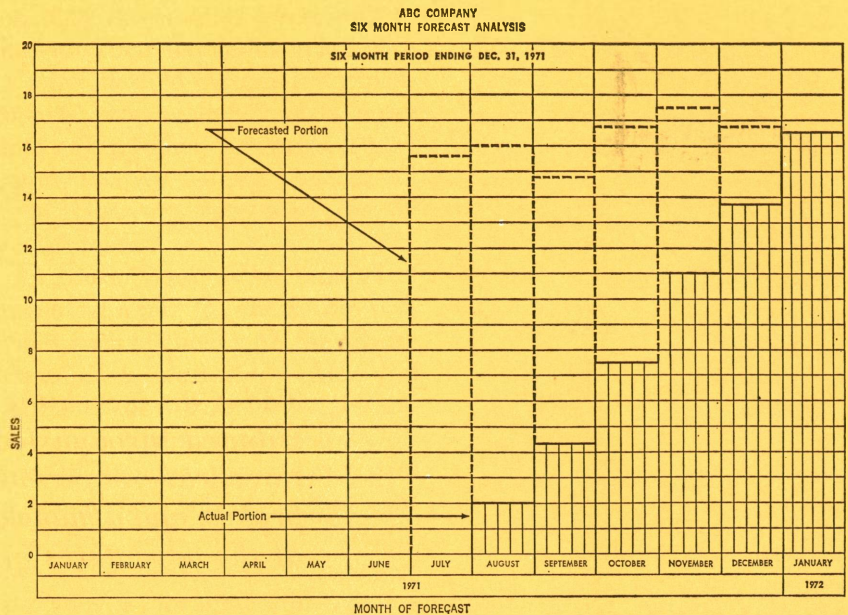
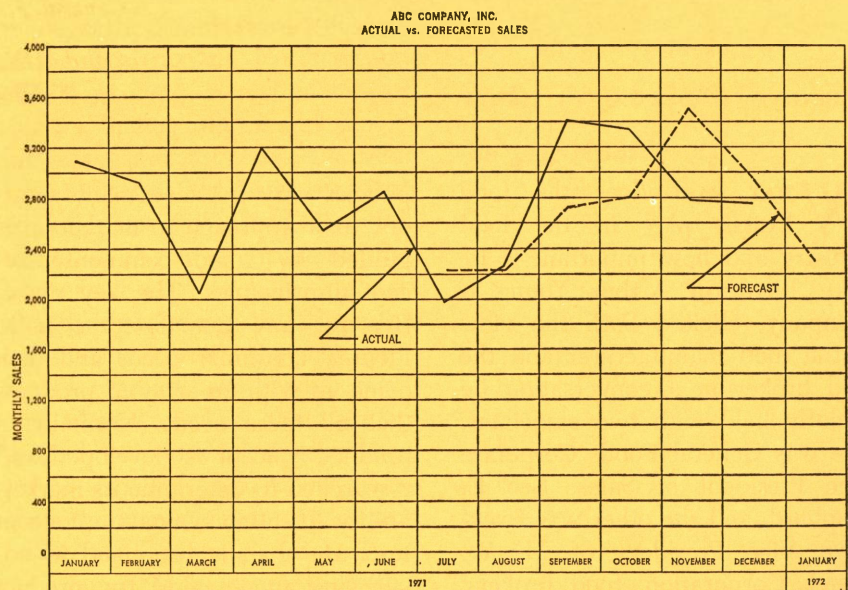


EXHIBIT 5



Today an increasing share of food products are distributed through food brokers. This transcript of a three-way conversation among a processor, a food broker, and a management consultant explores some of the advantages of this—

MARKETING FOR FOOD MANUFACTURERS: THE ROLE OF THE FOOD BROKER

*by Jerry H. Loyd
Arthur Young & Company*

*and Leo E. Sheperd
General Foods Corporation*

*and Albert L. Bonugli
M. W. Houck Corporation*

WHAT PART does the food broker play in the food industry and how important is it? Jerry Loyd, of Arthur Young & Company, elicited both the view of the food manufacturer and the food broker in a conversation he recently held with two associates. One was General Foods Corporate Vice President of Sales, Leo E. Shepherd, and the other was Executive Vice President of M. W. Houck Corporation, food brokers, Albert L. Bonugli.

Jerry—Leo, to start this off, would you briefly describe the general marketing approach of a food manufacturing company.

Leo—I would say at the outset that while marketing philosophies and

policies vary between manufacturers, their approach to marketing is guided by some commonly accepted principles. The key objective for any manufacturer is to identify consumer needs and then come up with an array of products that fill these needs. Normally, a product concept is developed and researched to determine its marketability. If, after evaluation concept tests, the manufacturer and its advertising agency find the product to have potential, a prototype product is developed. The prototype is then taken out to the field for further consumer research. Probably the most amount of consumer research is done at the prototype development stage.

Based on the results of the prototype research, the decision is

made whether or not to invest capital to introduce the product into a test market. If that decision is made, then the marketing strategies and objectives are set for the product. The product is manufactured either by a co-packer or the manufacturer's own manufacturing facilities, if available. The product is manufactured and then marketed in selected test markets. Before a product is expanded nationally, it must achieve specific marketing and financial objectives in these test markets. Through test marketing, the manufacturer is looking for answers to such questions as: Does it satisfy real or imagined needs that the product concept identifies? Does the consumer receive value relative to the price that has to be charged for the product in order to

make it a viable business proposition? Does she perceive that kind of value in her use? This is very important. Many manufacturers have introduced products that are short-lived because the product did not satisfy a need.

To test market a product, we normally select areas that represent a good mix of the national population that can be projected nationally.

If the product, through its test market experiences, meets the objective that has been established, then we take it into national distribution. At this point in time, a manufacturer's sales organization becomes involved. In GF, we employ both direct line and broker sales organizations. Regardless of the organization used, a product is introduced in basically the same way. Normally, an aggressive introductory advertising campaign and trade merchandising program is implemented in support of the product. The distribution pattern normally involves shipment from our warehouse to the individual customer warehouse for redistribution at retail on a precise time schedule so that the product is there and available for consumption at the point in time defined in our consumer advertising program.

Jerry—Al, Leo touched on the food broker in the latter part of his statement. What is the broker relationship? What exactly is a food broker? What services does he perform? Is the broker a middleman in all of this?

Al—First of all, Jerry, let me say that the broker is definitely not a middleman. A food broker is an independent sales agent who performs the service of negotiating the sale of grocery products for and on account of the seller (food manufacturer) as principal. He is not employed by an affiliate nor a subsidiary of any trade buyer. His compensation is a commission or brokerage paid by the seller.

Many food companies use food brokers exclusively as their na-

tional sales force. In addition, some of the industry giants have employed food brokers in recent years in an effort to relieve the workload on their direct sales forces and to provide their marketing team with a more flexible system for expansion of product lines and/or entry into new product categories. Today approximately 54 per cent of all food sales are accounted for by food brokers.

A broker represents a number of manufacturers. In effect, he provides each of them with the advantages of a local sales office but without the many expenses involved in maintaining such an office. Inasmuch as the broker is paid a commission only on actual merchandise sold, the manufacturer has a controlled sales cost. A broker provides a manufacturer with a ready-made sales organization which has long term customer associations and a depth of marketing know-how.

I believe another part of your question was what services are performed by the food broker? Believe me, there are many and they are varied. In essence, he professionally manages the manufacturer's business in the local market. He is responsible for selling to customer head-quarter buying offices and providing merchandising services to retail grocery stores. The latter is regarded by principals (food manufacturers) as the most important function of the food broker. Our merchandising salesmen are responsible for making certain that the principal's products are readily available in supermarkets, that they are properly displayed, merchandised, priced, etc. This department represents the largest single expenditure of any food brokerage firm.

Perhaps the next question that should be answered is what does it cost for the services provided by food brokerage firms? I believe the record will show that brokers have provided efficient, low cost service in the sale of grocery products. Commissions paid for these services vary depending upon volume of business and, of course, the amount

“ . . . the broker is definitely not a middleman. A food broker is an independent sales agent who performs the service of negotiating the sale of grocery products for and on account of the seller (food manufacturer) as principal.”

“Today, it is not uncommon for a manufacturer to have 60 per cent of his business . . .

of work performed. At all times, however, the food broker must bear in mind that the total commissions received cannot become so large that it would be cheaper for the manufacturer to establish his own direct sales organization. In a nutshell, Jerry, the food broker cannot be a luxury in the cost of doing business.

Jerry—You mentioned, Al, that some companies use food brokers on a 50/50 basis. Why is this?

Al—As manufacturers' businesses grew in size and they entered new product categories, they found that their present sales force could not effectively handle the workloads. Merely expanding the number of people in the sales organization was not the answer and to start a second national sales organization was a major challenge and expense. They, therefore, turned to food brokers who could offer them a ready-made sales organization with experienced professional personnel.

Today, it is not uncommon for a manufacturer to have 60 per cent of his business sold through his direct sales group with 40 per cent handled by food brokers. For example, such companies as General

Foods, Campbell Soup, RJR Foods, Lipton, Del Monte, etc., use a combination of direct salesmen and broker sales organizations.

Leo—The economics of a manufacturer's operation plays an important role in determining whether to utilize a direct line or broker sales organization. The dollar volume of the products marketed determine the affordability of a direct line organization. While important, economics is not the only factor to consider, however, when considering a broker. One of the things that the brokers have, and I don't know that they sell it as well as they should, is their ability to contact a large number of stores at a rather high call frequency. This isn't always affordable to a national sales organization. GF's Kool-Aid Division is probably a very good example of that. The Kool-Aid Division uses brokers because of the numbers of sales people available to them through the broker organization. A broker can achieve a frequency and depth of coverage in excess of our own sales organization.

Jerry—Are there other companies, Leo, some major food companies that use brokers exclusively?

Leo—Well, I don't quite know how to define "major." I think the Kitchens of Sara Lee certainly is a major company and it uses brokers exclusively.

Jerry—I guess I mean major in terms of their acceptance by the public, not necessarily in comparison to General Foods.

Leo—Some other manufacturers employing brokers who can be considered major in their respective businesses are Green Giant and Libby.

Al—Dole Pineapple is another good

example. They do the giant share of the pineapple business and use brokers exclusively. And, of course, as you know, Leo, most recently Libby, which had historically sold their products through a direct sales organization, discontinued their sales force in favor of food brokers who, they believed, would better assist them in correcting their downward sales trend.

Jerry—Quickly, just to keep this all together, what are the mechanics that a broker goes through to service a principal, to service a food company? He actually takes the order—how does that order get back to the food company? How does the principal keep some sort of record of sales and how does it keep statistics on where it is doing well or not doing so well? Al, in terms of your organization, how do you do that?

Al—Yes, we do process all orders received from customer buying offices. These orders are transmitted to the manufacturers who in turn ship the merchandise to the customer's warehouse, with very few exceptions, our manufacturers do all of the invoicing. Another part of your question related to maintaining sales records. The manufacturers we do business with keep complete records on all sales transactions by customer, by products, etc. Some have more sophisticated approaches but in all instances the basic data are available. We, however, due to the nature of our business as well as a desire to work in "real time," have a rather elaborate data processing system which allows our management to measure and control sales results. It arms our headquarter salesmen with sales analysis information which they can translate into effective personalized sales presentations. We are also able, based on our salesman's last retail store call, to

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... sold through his direct sales group with 40 per cent handled by food brokers.”

analyze retail store conditions, distribution, out-of-stock, authorized, won't carry, etc. This information is instantaneously available to us from our EDP memory storage units for approximately 2,300 retail outlets in the New York market alone. I mentioned working in real time. If we were to get similar information from Nielsen or some other research organization (through our principal) we would be talking ancient history rather than current conditions.

Leo—We set very definite objectives by market and we measure each broker by that market. We've divided our country into 52 marketing areas and we assign a broker to one or more of those marketing areas and that becomes his territory—and that's how we control invoices. We control invoicing by everything that is shipped to the customers on those products assigned to the brokers within those marketing areas. But we also set up local objectives against that product based on that product franchise in that area, and franchises do vary from marketing area to marketing area. So we can get specific marketing objectives against our products.

Jerry—Are these statistics a requirement of the food company? Must you, in order to service them, keep these kinds of statistics?

Al—In recent years manufacturers have placed a great deal of emphasis on the fact that food brokers should be able to give them a quick playback on market conditions, particularly the status of retail store distribution, out-of-stock and other related situations. As a result, some brokers have on-premise data processing systems while others have gone to outside service bureaus. Jerry. Because these were new costs for food brokers, there has been a

degree of reluctance to provide the service. However, now manufacturers are forcing the issue. On the other side of the coin, let me hasten to say that many brokers have voluntarily taken advantage of the opportunity to better manage and control their business through the use of advanced EDP techniques.

Jerry—We're talking overall about a 90 billion dollar industry of which the brokers have approximately 50 per cent, or 45 billion dollars. How many food brokers are there in the country?

Al—The National Food Brokers Association has a membership of about 2,200 brokerage firms. The association was formally founded in 1904.

Jerry—And I presume that each broker is tied to several food processors that constitute his entire clientele?

Leo—That's right. The latest number I have is that the average broker represents 21 separate manufacturers or principals on the average.

Al—The market size and product mix frequently decides the number of principals a broker can effectively represent. To generate the necessary dollars required to perform the total service in a small market, a broker may have to represent a large number of principals. On the other hand, in a major market, it would take fewer to do the job. The real measurement, however, should not be numbers of principals. The question is, is the broker properly organized to provide the services required? Can he get results? Many brokers have joined the so called Twentieth Century. They have departmentalized their business, implemented manpower development programs, in-

stalled EDP, etc.,—all designed to perform better services for their principals and customers.

Jerry—How about non-foods? Is that becoming a larger segment of both the food company's business and the brokerage business?

Al—Supermarkets are devoting more and more space to non-food items. The competitive pressure to sell high impact brands of foods at very low margins is cutting deeply into profits. Since non-foods offer larger margins, supermarket operators are forced to expand these departments in an effort to offset the profit squeeze. Non-foods, which include health and beauty aids, represent big new opportunities for the food broker. Conversely, the food broker represents a ready-made national sales organization for non-food companies that are doing a proportionately larger share of their business through supermarkets and yet do not have the manpower or the sales expertise needed to protect and merchandise their brand.

Jerry—I read, Al, in a recent article in *Supermarketing* magazine that over 50 per cent of the grocery products that are sold in the country are sold through food brokers while 87 per cent of frozen foods are distributed through brokers. What is the reason for the difference?

Al—To a large extent, it is an outgrowth of small companies that started their business with brokers and have now become major factors in the frozen food industry. Leo mentioned Sara Lee. There are many others that can be placed in the same category.

Leo—I think this goes back to the thing I covered before called frequency. Hiring ten brokers with

15 men apiece to cover the small marketing area gives you a lot more arms and legs. In the frozen food department, rather limited space is available relative to the dry grocery department—an average 200 feet of running space for 500 items of frozen foods. This demands quite a high call frequency that probably only a broker can achieve on an affordable basis.

Jerry—There very definitely has to be a volume point at which it is more economic to use direct sales rather than a broker.

Leo—I would agree that any time the cost of having a broker becomes considerably more than going to your own direct line sales organization, many principals would go to the latter. However, many principals are willing to spend more for a broker because of the added services he can perform.

Al—I agree with Leo. As a food broker, our cost must be competitive with what it would cost a manufacturer for his own sales organization. I do not believe, however, that manufacturers should look at the commission paid food brokers as an opportunity to reduce costs.

Obviously, the manufacturer makes the decision as to whether or not he wishes a direct sales organization or broker representative; however, these decisions should be objective, not emotional. What I am leading up to, Jerry, is that if a broker plays an important role in assisting a manufacturer in building his business to a point where he can consider a direct sales force as a form of cost saving, he should also be willing to allow the broker the opportunity to present his side of the story. As stated earlier, we cannot be a luxury in the system.

Leo—Well, there's another side to that coin, Al. You can build a product franchise and see that business double or triple with no additional sales effort, simply based on improvement of consumer franchise. And, as that product franchise in-

creases, it really doesn't take any more effort on the part of the broker or the national sales organization to keep it there. In fact, probably less, because as the franchise grows and it becomes a very dominant product, the grocer himself makes sure that the inventories are there and that it is on the shelf. But, with each case that's sold, an increasing amount of money goes to the broker. Whereas, with the national sales organization, it doesn't cost any more to have that product franchise grow and that's something that has to be kept in balance.

I do agree, though, with Al that any time a manufacturer is paying less than what it would cost him to have a direct line sales organization represent that product, he's treading on very thin ice to reduce his commissions, because that's the whole reason for a broker organization—to offer sales support on products that the manufacturer couldn't afford to implement himself.

Jerry—I think we are at the stage where it's obvious that the food broker is going to be a significant factor in food marketing for any number of years. It also appears to be a pretty general complaint of the food broker that he is in some sort of a cost squeeze and the fact that he's still going to be around would imply that there might be a change in the brokerage business, that there might be an emergence of larger brokerage firms, and that you might see some of the smaller firms drop by the wayside. Two thousand brokers is a lot of food brokers. Is that a fair proposition?

Al—Most of the people that I have had an opportunity to talk with in the industry expressed the opinion that brokers are becoming more professional and offering a wider range of services and are preparing themselves to represent all types of products that are sold within the confines of a supermarket. Brokers must continue to grow, in order to offset higher inflationary

“ . . . we are at the stage where it's obvious that the food broker is going to be a significant factor in food marketing for any number of years. It also appears to be a pretty general complaint of the food broker that he is in some sort of a cost squeeze and the fact that he's still going to be around would imply that there might be a change in the brokerage business . . . ”

costs; otherwise they will not be in a position to offer the services requested by their principals.

Leo—In this connection, the food manufacturers are growing in the different kinds of products marketed and the consumer needs they are trying to serve. The product mix in the grocery store today is changing. The presence of convenience items has grown rapidly. Roast & Boast is a great example. It's an item that serves a need that wasn't even conceived of two years ago. Shake 'n Bake is another example. So, I think we are growing. We might not be expanding in the old established commodity items, but we are growing in different kinds of items—better items that offer many conveniences and more product satisfaction.

Jerry—What's the product life on those kinds of items—it's pretty short isn't it?

Leo—Well, that's not true. A lot of our items have been in distribution for a good number of years because they continue to fill a consumer need. A good example is Jell-O Gelatin. One of our major responsibilities is to see that we introduce product improvements in those items to assure continued consumer satisfaction. There are some product categories that have been relatively static in recent years—coffee is a good example. Despite this fact, we've introduced product innovations in an effort to stimulate the market. Examples are freeze dried coffees, new decaffeinated products, and Max-Pax, a pre-measured coffee filter that provides convenience and uniform brewing quality.

True, the broker who represents a manufacturer who isn't innovative, who isn't coming out with new products, who is in the commodity business, might be stagnant, but that isn't true of the industry.

Al—It is very obvious to food brokers that some of the major brands of their largest principals are on a

plateau or enjoying limited increases. Unless these companies are feeding new items into the system their growth tends to stagnate. It is important for brokers to associate themselves with companies that are innovators. We cannot afford to stand still, as indicated in earlier discussions, because higher costs of operation would soon gobble us up. Therefore, brokers must maintain a significant rate of growth; otherwise I question whether long-term they will be able to perform effectively.

Leo—There are two ways for brokers to grow. First, to increase their product representation in the market by acquiring new principals. At times, this brings about problems because a manufacturer who has supported a broker over the years doesn't like to see the broker acquire additional sales responsibilities unless the broker is willing to put on additional manpower. The second way is to expand into new markets and open new houses. One of the interesting advantages the brokers have is that they don't necessarily have to rely on principals in any one market to be their principals in another market.

I think a good example is Al's company, M. W. Houck, which has five branches. He represents us in two. In addition, there are separate product categories in our divisions. He can represent one division in one market and another division in another market.

Jerry—Leo, do you think there is an advantage in having many brokers represent you across the country for the same products?

Leo—Yes, I think there is an advantage for the manufacturer to have a broker network and that could include having one broker represent us in several cities. I think there is a definite advantage for the manufacturer to be able to draw on the different strengths of many brokers.

Jerry—Is the basis for that the fact that the brokerage business is built

“There are two ways for brokers to grow. First, to increase their product representation in the market by acquiring new principals . . . The second way is to expand into new markets and open new houses.”

up around contacts with the customer, with the retail store? In other words, the strength of a brokerage organization in any community is the strength of its contacts and its association with the market?

Al—I can't speak for everyone, but as far as our company is concerned, we have felt for some time that the demands for new and improved methods, a depth of professional management, increased professional marketing services, manpower development programs, etc., are real challenges for individual food brokers. Several years ago we decided the way to meet this challenge was the establishment of a network of affiliated brokerage offices *managed by men in the market*. We now run five brokerage companies under different names; however, each has the opportunity to draw upon the capital, experience, manpower, and management expertise of a larger entity. But food brokerage strength is in the market. Food brokerage is a local business run by local men.

Leo—Another thing that's happened in recent years is that brokers are representing larger manufacturers. In the last ten years Al, most major manufacturers have utilized brokers on some or all of their products.

These manufacturers have introduced the broker to some of the marketing and sales disciplines of their own organizations. And, it's been great for both the brokers and manufacturers.

The larger manufacturers, not just General Foods but I'm thinking of Purina, Campbell Soups, Clorox, and many others, bring great discipline to their broker organizations. So food brokers are every bit as professional since they have really available to them many more marketing sciences than any one company. If they're really smart, they learn to pick and choose.

We set very definite objectives by market and we measure each broker by that market. We've divided our country into 52 mar-

keting areas and we assign a broker one or more of those marketing areas and that becomes his territory—and that's how we control invoices. We control invoicing by everything that is shipped to the customers on those products assigned to the brokers within those marketing areas. But, we also set up local objectives against that product based on its franchise in that area, and franchises do vary from marketing area to marketing area. So we can get specific marketing objectives against our products.

Jerry—What do you see in the future, not just in terms of food company/brokerage relationship, but in terms of some emerging patterns which will have an impact on marketing generally? Do you see, for example, that the pace of product turnover will become somewhat more severe?

Leo—Yes, currently in the average supermarket there are between eight and nine thousand items. I don't foresee any slackening in the introduction of new products. I do think for every new product that's been produced and held on the shelf, some other product will be in jeopardy of losing its point of distribution. I believe the numbers of items distributed might go as high as 12,000. I think probably in the future the leading brand or the leading one or two brands in the product category plus the private label will be all that remains in distribution.

Jerry—There's not enough system competence available in the grocery stores to keep them all straight.

Leo—That, too, and I think if you take away any item and put five brands within that category, three of them are profit robbers. There isn't sufficient turnover of sales on those three to warrant the cost of inventory and as our retailers become more astute businessmen in the use of money and in what generates money, they're going to

be very quick to get those kinds of items out of the stores. So I think it's a thing of economy as much as it is a thing of space.

Jerry—Will we be seeing the emergence of completely private stores?

Leo—I doubt it very much. I think private labeling is becoming a more and more important factor in the marketing of goods. But I think that we recognize that the private labels can maintain whatever margin advantage they claim to have simply because they don't support the development of the consumer franchise. In order to support the development of new products, they let the manufacturer develop the new product, develop the franchise, and then come in under that margin umbrella at a lower cost. Now, once they go into a complete private label system, they're going to have to assume the cost of both product and market development. When that happens, they're going to be national brand manufacturers and face all the costs of the national manufacturers.

I don't foresee that.

The retailer's costs have not diminished. If the trade maintains its traditional low margins, they're going to have to increase the productivity of their operations. The manufacturer has got to ask himself, "What do I do in my distribution system to allow the retailer to increase his productivity?" "What methods of operation or sales policies must I change, not necessarily to support him through price or trade activity, but to support him in a way that will increase productivity?" Increase in productivity at the retail stores has got to be the answer to preserve margins and to maintain the kinds of services that the retailers are currently providing.

Jerry—So, emerging problems in food manufacturing extend all the way down to the retailer, how he conducts his business, and how he can save money, and, ultimately, provide the housewife with a better product at a reasonable price. I would presume the problems for

the brokerage business involve the size of the brokerage organization, need for sophistication, and, I guess, getting rid of some of the old imagery.

Al—In my judgment, food brokers will continue to expand because they fit a need. I think perhaps you're right that they will become bigger in size and thus the demands for sophisticated management will increase. Regarding the latter, brokers have come a long way; however, like many businesses, constant upgrading will be the order of the day. We have attracted and will continue to employ a higher caliber of personnel. With a better input of people, we cannot help but become even stronger professional selling organizations.

Jerry—You'll need data to provide the food companies, your principals, with information on the cost of services. Now that appears to be an area on which most of the brokers haven't spent much money or time. But you really can't convince a principal that he ought to give you, say, a 3-3½ per cent commission unless you can convince him what it's costing you to sell his product. Now, I suspect that's not as easy a thing to do as it sounds.

Al—Jerry, you know my attitude on this subject; however, for the record, in my opinion it is extremely difficult, if not impossible, to come up with an accurate method for measuring cost of service. For example, our salesmen face an entirely different situation in each retail store they contact. We are not against coming up with a system which would allow us to better evaluate and manage costs of representing individual principals, but in our experience we have yet to see a program that works.

Leo—In the old days—I don't think it happens too much now—a lot of the smaller manufacturers provided salesmen incentives on their line. If I was representing 25 per cent

of a broker's total commission income and this guy was representing 5 per cent and the broker's people were spending a lot of time for him because of these incentives, I could get very emotional. I think the brokers are far beyond that today. I think they do a tremendous job in directing the sales efforts of their salesmen on a balanced basis against all manufacturers represented. And I think the manufacturers have brought this discipline to them through demanding certain things on each of their products.

Jerry—Leo, does the manufacturer also conduct education programs? Are you reaching down to the broker the same way you're reaching down to the retailer in terms of the conduct of the business.

Leo—Oh, yes, we developed for the Kool-Aid Division of General Foods a program under the auspices of Harvard Business School for training brokers. We hired Drs. Feathers and Schack of Rutgers University to conduct this program as outside consultants for our own people as well as our brokers.

Jerry—Well, I guess then you'd have to conclude from this discussion that the marketing relationship between the food companies and the brokerage firms is a pretty happy marriage and it's one like good wine—getting better with age. The brokers are conducting a much more sophisticated activity than they did in years gone by. Indeed, the food companies work quite closely with brokerage firms to help develop marketing competence and assure the creation of control and reporting disciplines which are reliable and professional. I am impressed with the strong spirit of cooperation that appears to exist between food manufacturers and brokers. I am impressed with how well the arrangement works. The melding of big and small business—major food companies and the relatively small food broker companies—is an outstanding example of capitalism at work to provide the best service for the consumer at the least cost.

“... and I think if you take away any item and put five brands within that category, three of them are profit robbers. There isn't sufficient turnover of sales on those three to warrant the cost of inventory and as our retailers become more astute businessmen in the use of money and in what generates money, they're going to be very quick to get those kinds of items out of our stores.”

what people are writing about

BOOKS

Effective Managerial Leadership

by JAMES J. CRIBBIN, American Management Association, New York, 1972, 264 pages, \$9.75.

Books on leadership tend to be either exhortations of the inspirational self-help school or scholarly studies encumbered by the singularly impenetrable jargon of the social scientists. This book is neither; it is, in fact, actually useful.

The aim of the author, a consultant with an unusually clear and

jargon-free writing style, is to provide "realistic guidelines" that line managers "can translate into appropriate behavior in their workaday situations." He has succeeded in avoiding two common pitfalls, "the dogmatically stated nonsense of . . . the 'Do this and thou shalt be saved' approach and the semantic morass of research jargon."

Plenty of attention is given in this book to the imposing body of research on leadership and supervision, and each scholar's contribution is summarized with unusual clarity. As a matter of fact, this book is worth buying just for that.

But Mr. Cribbin does more. The only universal conclusion that can

be drawn from all this research is that leadership is a situational phenomenon and that the right way to lead depends on the individual situation.

So Mr. Cribbin bravely attempts to describe the major factors that influence the choice of leadership methods in a given situation—from the Puritan ethic and the corporate climate through the authority system, the power system, the group system, the role system, and the status system down to the executive's relations with his superiors, peers, and subordinates—and suggests how to strike a balance among external and internal influences in selecting both a general style of

REVIEW EDITORS

In order to assure comprehensive coverage of magazine articles dealing with management subjects, MANAGEMENT ADVISER has arranged with fifteen universities offering the Ph.D. degree in accounting to have leading magazines in the field reviewed on a continuing basis by Ph.D. candidates under the guidance of the educators listed, who serve as the review board for this department of MANAGEMENT ADVISER. Unsigned reviews have been written by members of the magazine's staff.

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management appropriate to the individual and a particular response to particular problems. He concludes with a discussion of business ethics and the management of change.

Nothing in this book is new or startling, but as a synthesis of what has been learned about human relations in management and how to apply that knowledge it is invaluable to anyone in business.

Struggle for Identity: The Silent Revolution Against Corporate Conformity by ROGER M. D'APRIX, Dow Jones-Irwin, Inc., Homewood, Illinois, 1971, 193 pages, \$7.50.

Knowledge-workers ("the highly educated and generally youngish managers, engineers, salesmen, accountants, programmers, and others who earn their paychecks by contributing from their personal knowledge and understanding") are becoming increasingly alienated from the corporate way of life—much as their younger brothers and sisters are becoming alienated from the schools, family, and other institutions that touch them. That is the thesis of this book. Its author, who is himself one of these knowledge-workers, does a fairly good job of stating the problem but doesn't go very far toward suggesting solutions.

This is, Mr. D'Aprix notes, an age of protest against established traditions and authority. Americans no longer assume that their leaders are omniscient. They are losing their faith in progress, in the goal of "success," and in the work ethic. The old value system is being replaced by one which is "antisystem, antiauthority in nature," which holds "that people are more important than things" and which "stresses tolerance rather than conformity."

This "silent revolution" also affects business organizations "for the simple reason that they are an integral part of the society in which

these things are happening." This wave of discontent is on "a collision course with American industry, which is still largely authoritarian in structure and outlook. And it isn't just the blue-collar people who are disturbed. If the truth were known, they are probably less disturbed than the professional employee—the engineer, the salesman, or the manager, whose expectations tend to be considerably higher."

Here Mr. D'Aprix is speaking of and for the group to which he himself belongs. He is a writer and editor who has spent most of his career within the corporate fold doing public relations and advertising for large companies, most recently directing Xerox Corporation's employee communications program.

Corporations, Mr. D'Aprix concedes, are changing, too. As between Douglas McGregor's Theory X authoritarian style of management and his Theory Y participative style, the pendulum is gradually swinging toward the latter.

Corporate heirs' responsibility

"The inheritors of corporate power in the years ahead will inevitably accelerate the corporation's work as an instrument of social management," he predicts. "And when the dust finally settles . . . the basic mode of corporate organization will be a streamlined version of the much maligned vertical hierarchy" but "managed on a human scale."

Meanwhile, he thinks, we are in "a painful and confusing transitional period for both management and individual employee. During the next few years, while the new dogma is being formulated, the individual employee must fend for himself in deciding what his new relationship will be with his organization."

For some years to come, he warns the other knowledge-workers, to whom the book is primarily addressed, "you will have to invent your own rationale for your existence within the corporation. And

invent you must, for if you neglect this vital task, you will be hard put to find either job satisfaction or composure."

Mr. D'Aprix has some suggestions, although they are not very specific. The professional worker must be willing "to keep inventing" his job. He should see his job description as only a starting point and keep adding to it "whatever other opportunities there are to contribute."

He should develop autonomy. "If you are willing to act—even in a repressive organization—without concern for all the small career implications of your actions, it is possible to accomplish a great deal and to have strong influence in your organization."

He should become a "corporate activist." He must plan what he wants to do in his organization and what he wants to become, and then bend every effort in working toward those goals.

And he must search for personal growth and satisfying human relationships both within and outside the corporation.

None of this—the heart of the book, the preface suggests—is fundamentally very helpful. It is possible that Mr. D'Aprix has set himself an impossible task.

He is obviously deeply in earnest in his effort to present and solve a problem that clearly disturbs him profoundly. (Perhaps he is too earnest; the book would benefit from a touch of humor here and there.)

But he lacks the perspective and experience really to carry off a book of such scope. Perhaps in realization of this fact, Mr. D'Aprix says he is addressing his book to the individual employee. But he has done too much research—and quotes too many global thinkers—to come up with a genuine worm's-eye view.

The book is worth reading—more for the executive than for the knowledge-worker employee to whom it is ostensibly addressed. But it will not move any organizational mountains.

Projectability as a Criterion for Income Determination Methods by JOSEPH G. LAUDERBACK, III, *Accounting Review*, April, 1971.

Should a criterion for selection of an income determination model include the capacity of current income to predict future income within fairly close tolerances? This article examines the diverse notions of income determination and questions specifically the shortcomings in the income prediction arguments.

One scheme of income determination often advocated would measure the increment in value from one point in time to another where value is the present value of expected cash flows. Situations may be envisioned in which an income amount might be consistent with a value increment notion and inconsistent with an earnings predictor criterion because one period's value changes might not be repeated in the next period. Separating income into its components would afford a better means of predicting future income. In any event, proponents of value increment consider projectability to be a separate criterion for acceptance of income determination methods and suggest that enough information of the details of computation be supplied so that an analyst can make his own predictions.

Accountants who no longer search for a "one true value" concept of income emphasize the decision-making process. Income prediction is important to them because it is a distillation of the collection of diverse data represented by the income computation. The amount of research devoted to evaluating various income determination methods on the basis of predictive ability is extensive. Professor Lauderback, however, contends that both the value increment and surrogate arguments contain prem-

ises of seemingly doubtful status.

Income is an immutable, ideally precise conception in the value increment argument. Although unknowable, all values can be determined through some medium (e.g., current costs). Supposedly income determined in this manner is relevant to the users of financial statements. However, Lauderback notes, other writers have questioned the validity of this argument. The non-homogeneity and interdependent system of assets casts doubts on an attempt to relate accounting income to economic income.

Accounting income is constituted by the formulation of rules for the recognition and treatment of events. Accounting literature seems to be arguing that the important subjects for prediction are the same events originally selected for recognition. But as Professor Lauderback pointed out, it is not stated why the originally selected classes of events and their treatment are of any significance in investor decision processes. It is not sufficient to say that income prediction is useful because it is used.

Another question raised by Professor Lauderback is related to the behavior of management. Most decision making models assume that managements will maximize shareholder wealth given the imposed constraints of rate of return and cost of capital. Instead, it is quite possible that managements perceive their best interests lie in the achievement of steady growth in reported income and dividends.

Even if statistically significant relationships between income, dividends and share prices may be found, a structure of "natural" relations could not be assumed. The method of income determination used would only have served as a self-fulfilling prophecy.

The significance of prediction was not questioned in the article. Indeed, predictive ability is one criterion of a scientific proposition. However, in the conduct of human affairs, it is necessary to formulate propositions in reference to experienced problems. It is Lauderback's

contention that income projectability arguments are not supported by such propositions.

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