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Weak Links In Chains Of Stores

By Joseph M. Mellen

The legislative searchlight shortly will be turned upon chain-store merchandising, the effect of which upon normal economic life in a rural community is discussed by Joseph M. Mellen.

BILLION DOLLAR STAKES sound a trifle too big to be of concern to the average American housewife, as she dabs powder at her nose on the way to the butcher and the grocer.

Yet, if the conflict between the interests of chain stores and of independent dealers has not been exaggerated, her role is one of the controlling factors in a clash of at least this magnitude which is imminent, and cannot long be postponed.

The conviction grows steadily that something is wrong in the situation, and that something must be done to right it.

Though many small shopkeepers still do not know it, chain store executives are aware that the tocsin of economic warfare is ringing with wild discordance today. Also involved in the hostilities are farmers, newspaper publishers, railroad officials, manufacturers of household articles, small town bankers, tobacconists and pharmacists.

Thoughtful citizens, who may have believed themselves removed from the fighting zone, cannot but realize that the problem, somehow without their knowledge or consent, has crept menacingly within touch of their fortunes.

If the trouble were, or could be, confined to a mere matter of competition between chains of stores and independent owners, a solution might be neither difficult to reach, nor of great importance. But what complicates it is the huge sums of capital invested, the great number of employees involved and the many different industries affected. Indeed, the problems created by the chain store can be likened in far-reaching effects to those arising from sex, prohibition and gang warfare. Otherwise, the easiest disposition would be to lump them with Communism, War debts and political corruption, and forget them until they solve themselves.

Unfortunately, prejudice still further complicates the subject, beclouding judgment to some extent and throwing a mist of poison gas around the vital issues.

Like a great octopus, the chain store method irresistibly extends its influence into every avenue, street and alley of the nation's retail business. Its first objective is to paralyze forces which oppose it that it later may grow fat on inordinate profits. Whether in the city, where it seeks to crush the weakly neighborhood merchant, or in the country, where it seeks to exterminate the local tradesman, the story is ever the same: individualism in business must give way to the great, inanimate power of organized capital. And as the struggle continues, the helpless farmer, ever more helpless, must stand aside and see his product given away.

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A few figures illustrate the stature of chain store organization, and the degree to which it has prospered.

In 1929, the last year before the depression struck normal business, six million men and women were employed by chain stores at an aggregate payroll of five billion dollars.

In the same year, according to the fifteenth census of retail distribution compiled by the United States Department of Commerce, chains owned one of every ten retail shops. The seven thousand chain systems operated 159,826 of the 1,549,168 places of retail business in the country.

The total amount of retail trade in 1929 was approximately $50,033,850,792 in net sales, but the ten per cent of chain stores did $10,771,934,034 of this trade, or twenty-one and a half per cent of the total!

In the miniature department store field, selling articles for nickels, dimes, quarters and dollars, earning charts show an average return on capital invested in 1920 of nearly fourteen per cent. In 1925, this percentage rose to twenty-five. In 1930, after trade had begun to suffer, earnings still were in excess of thirteen per cent.

In the field of food products, earnings apparently have been much greater. One important private banking house, specializing in chain store operations, estimates that one food chain, before deducting interest, taxes and dividends, earned as much in one good year as one dollar and fifty cents on every dollar invested. A group of seven food chains earned an average of forty-eight cents for every dollar invested over the period from 1925 to 1930, inclusive.

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Two trends, however, indicate that, while the chains can annihilate independent ownership in business, they eventually injure all trade, themselves included. The first is a steady decrease in profits from 1925-6, peak years of earnings. The second is the steady increase from 1925-6 of the net fixed investment in individual shops, showing decreased earnings on dollars invested.

Profits attract investors. Also, the pressure of investment seeking profits causes profitable business to expand. These principles explain the tremendous development of chain store systems. This growth has been accentuated in the past decade by the falling level of earnings in such long established industries as iron and steel, petroleum, automobiles, gas and electricity, railroads and the telephone, where competition for business and competition for ownership of securities have forced return upon investment to conservative percentages.

Chain store profits began to decrease immediately after 1925-6, their peak years. This preceded the depression. A current bulletin on chains, published April 17 by the research bureau of the Graduate School of Business Administration at Harvard University, indicates that this decrease continues uniformly at present.

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It is easy to see what stirs the ire of the independent merchant against his chain store rival. Loss, fear and jealousy are factors. Yet, there is nothing inherently

Woolworth's Lunch counter

sinister, or vicious, in the theory of chain organization—at least, so far as appears upon the surface.

The chain store originated, to all practical purposes, in the mind of a man from Maine named Hartford to whom it became apparent that, if the owner of one shop could earn a profit, he could make greater profit from the ownership of two shops. Still more profit would result from the ownership of three shops and so on, until overtaken, of course, by the law of diminishing returns.

Another source of increasing profit soon came to light. The combined capital of multiple ownership conferred purchasing power so much greater than in the case of individually operated shops that merchandise, bought in large quantity, could be acquired substantially cheaper per unit of measure. This gave the chain operator immediately a profit and an advantage over his competitor. He could cut established prices and, at the same time, retain a larger margin of profit.

When the desirability of group operation caught the fancy of investors, the rise of chain selling was rapid and diversified. Its ramifications extended into many fields, though practice showed it best suited to articles of small value. Food, household necessities, wearing apparel, minor luxuries, tobacco and druggists' sundries proved to be the stock lending itself most conveniently to the rapid turnover of capital, large volume of sales and small unit of profit indispensable to chain selling.

At first, the chain store encountered no resistance, at least organized, from independently owned shops. In this period, when chain stores earned more comparatively for their owners, whether individuals, families or stockholders, than other forms of enterprise, public demand for investment opportunities encouraged establishment of a growing number of chain selling organizations.

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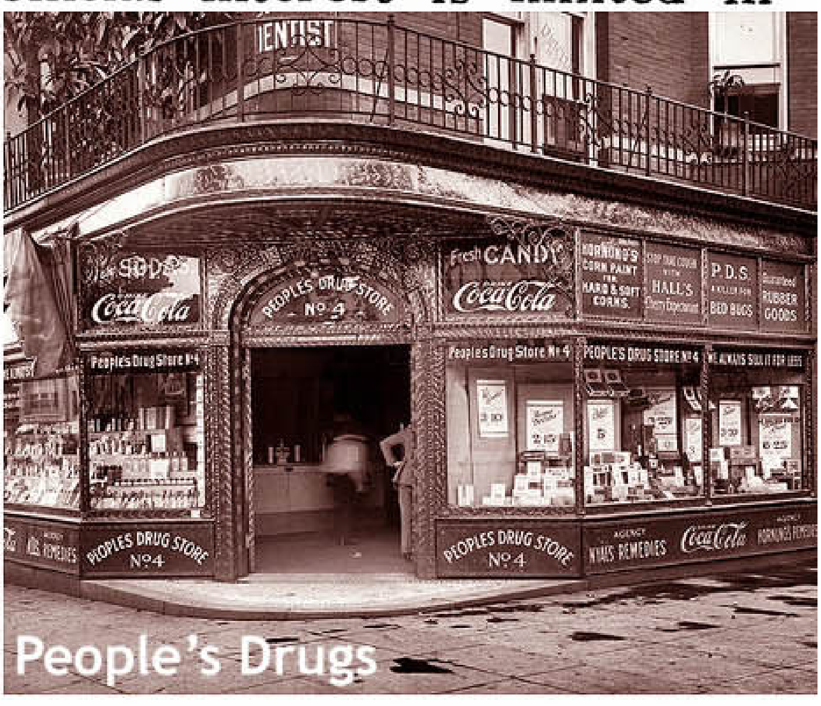
Other forms of enterprise felt the attraction to amalgamation and merger which was spreading rapidly among small, retail shops. Manufacturers of automobiles and airplanes, operators of public utilities and steamship companies, even banks, caught the fever. The only restraining force apparent was the Federal government, prohibiting and regulating through powerful anti-trust laws and commissions.

Chain selling seemed to escape attention from the Federal government because official interest is limited in scope to the maintenance of adequate public service and to the protection of the public against restraint of trade. The Constitution has been interpreted as giving to the central government authority to prevent whatever will raise prices of



People's Drugs

necessities to unnaturally high levels through the power of monopoly. Methods of obtaining large volume of sales, even though they have lowered prices below the range of fair and reasonable profit to a large number of producers and dealers, have been slow to draw disapproval.

While Washington has been content, so long as no citizen is compelled to pay excessively for life's necessities, the fact that low prices may bring harm to an appreciable number of individuals is working its way to the foreground of Federal attention. It is this question which now focuses interest on the grievances against the chain store in many fields of business.

The case, in a small, rural village two or three centuries old and located near the Atlantic seaboard, will illustrate the grievance in many of its aspects.

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Up to the advent of the chain grocer, the mercantile and trading life is serene. Perhaps it is too much so for progressive youth, which makes its way for vital excitement to larger centers of population.

The village grocer is an independent merchant, owning his shop and his home. In every sense, he is a citizen of the community. His family has lived there since the dawn of village history. He is related to many of his neighbors, and he is one of them, a friend. He may not be efficient in business practice or in the range of his stock, but he provides about what the villagers want and sells it at a price which supports his family and his share of village charities without much margin toward accumulation of an independent fortune. He is content, and his shop is sound enough to give first training to many who rise high through their ambition in the industrial and commercial life of America.

Then one day, word spreads in the village that a new grocery is to open. The news has undoubted interest.

Since real estate values are stable, with little to disturb them, the agent of the chain store is able to acquire a central location at an extremely moderate rental or purchase price. He has the advantage of being able to threaten not to bring the chain store to Bumpkinville, but to go instead to a neighboring village. This argument is not to be resisted.

Next, after the site has been picked and made ready for its new uses, comes the advance publicity or propaganda in the local newspaper. The editor, under pressure of the advertising manager or publisher, prints a laudatory article extolling the virtues of the great company which has been wise enough to appreciate the future possibilities of Bumpkinville. A second point in its favor is that it is going to bring to the village delicacies from distant India, France, England, Italy and the Far West, as well as the Old South. And, *mirabile dictu*, all these delicious and mouth-watering articles of food will be sold at low, ridiculously low prices. The newspaper does not say the new grocery is coming because of love for the people of Bumpkinville, neither does it hint that it is coming merely for profit. In the publisher's mind, however, is the pleasant prospect of columns of advertising regularly submitted, telling their story of variety and prices.

Finally, the day of opening arrives. The new shop, naturally, is a center of interest in the village for the time being. Everyone visits it, whether to purchase, or to look it over. Prices immediately catch attention. Why not? Are familiar articles not priced several cents lower than those known in the village for a decade?

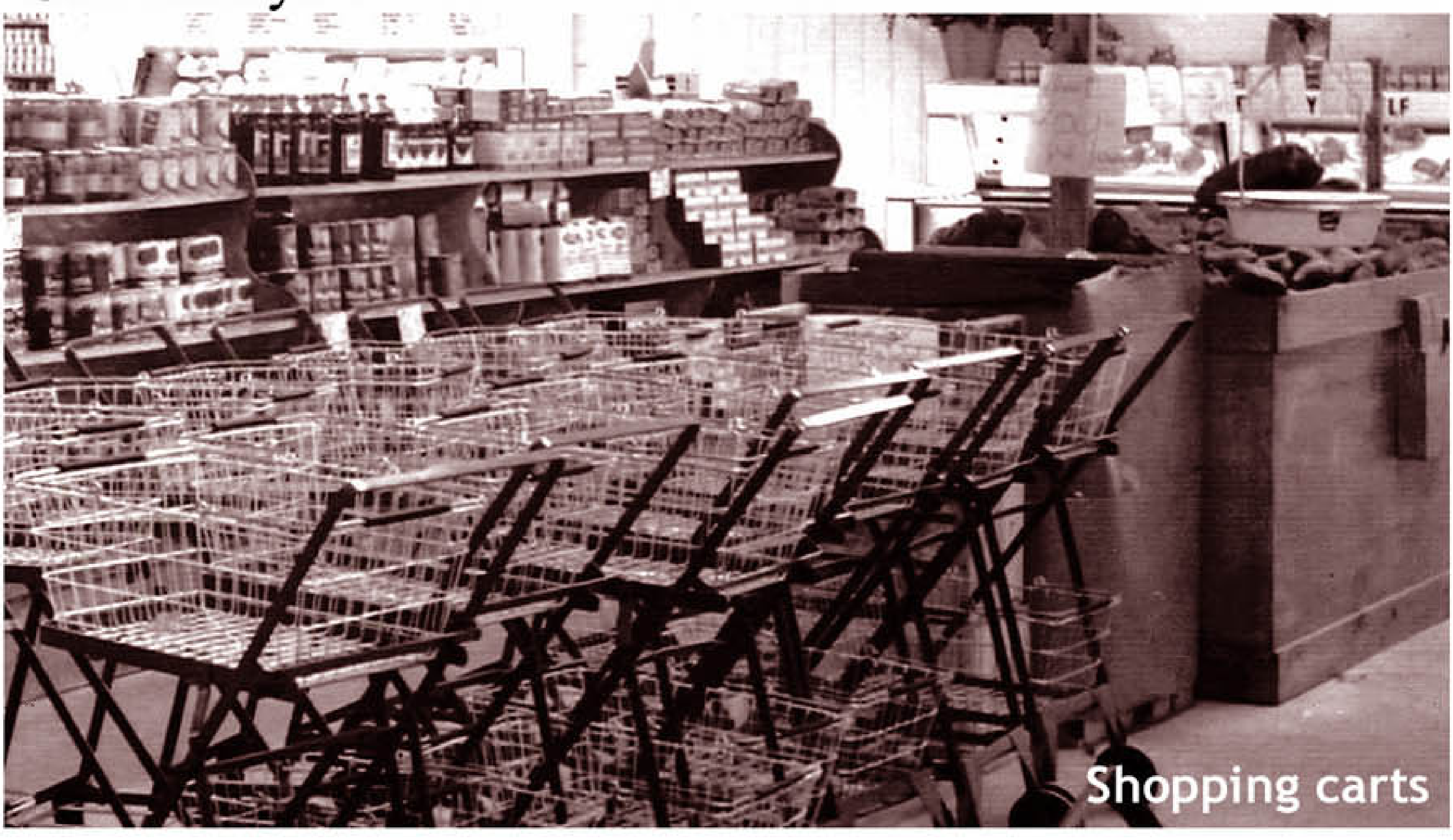
The manager makes two points clear to all: buy cheaply by paying cash; save money by carrying your purchase.

The old, established grocer is not worried at first. You cannot fool him. He has always had the trade, he is on friendly terms with everyone in the village, he knows what they want. No, Sir. Perhaps he is a trifle jealous the first day. But he knows that the vogue will pass. His customers, his friends, his neighbors are used to buying from him, charging mostly, and letting him deliver. They will not take up new ways overnight.

Gradually, the discouraging truth hits home to the village grocer. His trade is going steadily to the chain store. The primary cause is price. More and more of his best customers are coming to him only for items they cannot get at the new shop. His income is suffering a serious reduction.

The psychology of the village on the question is interesting, but it brings the grocer precious little comfort. He finds resentment growing against him and he discovers it is due to a feeling he is overcharging his customers, that he has been overcharging them for years. His only defense is to make reductions wherever possible. And without reasoning very carefully, he puts up a fight in the one field in which he cannot hope to compete with his adversary. The struggle is now growing serious. He seeks cheaper items from his supply house. The bulk of his trade, after a time, comes mainly from the slow pay customers who find it inconvenient to pay cash at the chain store. Thus, the proportion of his questionable accounts receivable rises in the total amount of his trade. Too much of his working capital is tied up in sixty and ninety day accounts.

In the meantime, several other members of the community are beginning to find that the low prices of the chain store do not confer unmitigated blessings on the community.


Shopping carts

The president of the Bumpkinville Bank, to his surprise, is unable to induce the manager of the chain store to open an account. He learns it is the practice of the chain to send all cash in excess of local expenditures to the city headquarters within twenty-four hours. This means that the bank and its stockholders are losing the use of an appreciable part of the currency in circulation in the village.

Another fact, not entirely pleasing or reassuring, is encountered before long by the banker. Deposits, particularly savings accounts, are decreasing steadily in the local bank. What is worse, the decrease is not accounted for entirely by the reduced amount of money passing through the account of the old grocer. The only possible explanation the banker can formulate is that the chain store is draining the resources of the community, sending steadily to the nearest large city its excess of income over local expenditures.

In the course of frequent conversations with village inhabitants of various vocations, the banker begins to note new factors in the situation created by the chain store. Many of them did not occur to him for some time.

The farmers, he finds, are beginning to turn in sentiment against the new shop. They at first favored the spirit of "git up and go" which the chain manager introduced in the business of the village. He wasted no time when he gave them orders for vegetables, eggs and fruits in season. He was in just as much of a hurry when it came to setting the price. He named what he was willing to pay and intimated he was sorting out in his mind sources of supply for the future.

Before long, the farmers find that no more of their products are being consumed than formerly. Also, they find the amount paid for these products has been beaten down below former levels. As the bank's best customers, season after season, these facts add to the feeling of disturbance in the mind of the village banker.

The local publisher also brings a tale of woe to the banker. The volume of expected advertising from the chain store has not materialized. Furthermore, the advertising is being placed in the newspaper at rates below the established scale. The manager, in winning this concession, says that he has authority to pay no more. He is willing to take it up with his head office, but tells the publisher he is sure they will say: "Take it, or leave it."

Coupled with this disappointment, the publisher tells the banker, is the discovery that the local grocer can no longer afford to take as much advertising space as formerly, because he has lost too much business, and cut his margin of profit too low to warrant the expense.

The railroad, too, has a complaint which eventually reaches the banker. Through the mouthpiece of the local freight agent, he hears that the road is losing business directly through the advent of the chain store. The grocer is bringing in less goods over the rails, while the chain store brings all its merchandise over the state highways in great trucks. This worries the banker, who knows that the railroad has lost already a disheartening volume of passenger traffic through increasing use of the automobile.

As for the old village grocer, who begins to look a little peaked, his case worries the banker, though not solely through altruism. In making a loan on the basis of his slow accounts receivable, he begins to talk about a mortgage. The banker finds it embarrassing to realize that this customer steadily is losing ground.

To bring attention to the subject of increased expenditures by the village through the highway department for road repairs and maintenance might seem far-fetched. In any case, the banker realizes that money is spread over all property owners and represents an insignificant item at the end of the year. The highway superintendent, however, can testify that the roads are not holding up so well since the big trucks began regular visits to the chain store, especially at times when storms have softened road surfaces.

A final factor in setting the mind of the banker against chain selling comes directly from his wife's indignation. As head of a committee of women for a local charity, she reports that the chain store manager refuses to make a contribution. He gives two reasons. He says that his own earnings do not justify a gift, and he cannot commit the store without authority directly from his headquarters. The chain store, the banker sees, is wholly impersonal.

The banker, like the publisher who is his friend, is a sort of clearing house in the community for information. While, at first glance, it appears that the newspaper deals in humanity and the bank in economics, the two friends get both sides of the picture. In talking over the situation, they decide to assemble facts on both sides of the question. They agree that the chain store hurts those from whom it buys and those with whom it competes. The farmers, the real estate owner, the newspaper, the railroad and the bank all suffer, as well as the grocer.

What about the customers of the chain store? Do they, too, suffer?

The banker and the publisher know through the medium of their wives that almost every household in the village goes to the chain store, at least for part of its groceries. On the surface, every purchase represents an actual saving of copper pennies. If these savings are real, it will be difficult to answer their argument, for reduced costs of living, particularly in times of depression, play a great part in upholding, or raising, the village standard of living.

Another argument in favor of the new shop, apparently, comes also from its customers. They praise the variety of merchandise upon its shelves. They say some items, like coffee, are fresher. They say others, like butter and bacon and potatoes, are of better quality. While the facts cannot be disputed, it is obvious the old grocer is able to supply whatever his customers really want, for the chain store can have no exclusive right of purchase, except in the field of private brands. This argument, therefore, the banker and the publisher dismiss.

Another plea for the chain store is that it has created employment. In discussing this, the friends find that, as in the case of merchandise, it is deceptive. Every position created means ultimately another lost, just as the old grocer has had to do without one boy, the farmers without a few helpers, the freight-yard without a man, and so on. Furthermore, and to the disadvantage of the chain store, the older rates of wages were higher than those paid by the new shop to its staff.

The argument, then, comes down to the question of pennies in the pocketbooks of the chain store customers against dollars which the community is losing. This is more difficult for agreement between the banker and the publisher of the local newspaper, for, while the publisher sees the pennies saved and the dollars lost, he does not follow the banker's exposition of the economic loss to the community caused by the constant export of currency from village circulation to the city. The publisher can see no difference to the customer, whether he pays to one shop or another, except that from one he gets a better price.

The banker finally resorts to a simple illustration. Taking the village as a whole, he shows the publisher that if it spends more money outside than it takes in from the outside, it loses inevitably in the long run. It cannot balance its budget, for its expenses are greater than its income. In the view of the banker, bank deposits are the source of information, reliable except that they do not include money invested in bonds and other securities.

Since the advent of the chain store, the deposits at the bank, which represent the currency of the village, have steadily decreased. Therefore, the apparent saving in pennies is made at the cost of dollars lost.

The result, thus, of the examination by the banker and the publisher is that the chain store is a liability, rather than an asset, to the village.

Summarized, the charges are as follows: the chain store profits for its stockholders at the expense of the public, the farmers, labor, the banks, the railroads, the newspapers and property owners.

In addition to grocers, whose case the village represents, chain stores compete on much the same basis in other fields. These include butchers, clothiers, haberdashers, toy and game shops, dealers in household and kitchen goods, shops for dairy products, tobacconists and drug stores. In each case, the whole community suffers in the interest of those who hold stock in chain systems.

The question, of course, cannot end with a statement of the charges against chain selling organization. There still remains the future. What does it hold?

Two reasons exist for thinking that a solution will be found for the problem. The first is the size of the public's investment in the chain idea and the number of employees involved. The second is that, with the intelligence, industry and efficiency which it took to build up the successful chains still at the command of their managements, it is inconceivable that they will give up without a struggle.

Even if the public invokes legislation, as has been done in several states and considered in others, the real solution of the problem rests with the chain stores themselves. Bad laws are undesirable because they establish bad precedents and ways are found to circumvent them.

The chain stores can attempt to fight it out on the basis of their present practices, but it seems doubtful that they will do this. They know, fully as well as other intelligent human beings, that they have become unpopular and are considered guilty of unfair practices. They know, too, that a growing disposition not to trade with them portends trouble, for it is difficult to combat an aroused public opinion.

One principle of sound and successful business awaits application by the chain stores as a way out of their land of Egypt to their Promised Land. This is the Golden Rule that business, to be profitable to one party, must benefit both parties equally.

The answer, therefore, is for the chain stores to give up all appearance of a "Public be damned" attitude and to discover ways by which their business can be profitable to themselves without damaging further the interests of others, their competitors, their suppliers, their public.

When this happens, the American housewife as she prepares to go to market will not have to worry over a billion dollars.