Thank you all very much for joining us. The questions we’re here to explore are both very important and very complex, and I’m very grateful for the opportunity to learn from the best minds in the business.

With apologies to the Richmond Fed folks in the room, who’ve heard this before, I thought I’d start by telling you a little bit about myself and my perspective. Before I say more, I have to note that the views I express are my own and not necessarily those of the FOMC or the Federal Reserve System.

I joined the Richmond Fed last January, after a 30-year career in consulting at McKinsey where I had roles including chief financial officer, chief risk officer and leading our offices in the Southeast. I’ve spent my professional life helping firms make decisions about hiring, compensation, prices – and, yes, M&A – and I’ve made a lot of those decisions myself. As the only member of the FOMC coming from management, I can approach the issues your work sheds light on as a practitioner rather than a researcher.

And that’s how I approach the topic of market concentration. I’ve certainly seen industries that have consolidated and, as a consequence, fundamentally altered their competitive dynamics and
the resulting markups they capture. Airlines are a classic example. Once, they were the poster child for destroying value. But about 10 years ago, the U.S. industry consolidated to four carriers, and they leveraged international joint ventures to limit competition transoceanically. As a result, they increased their ability to profit: They found it easier to introduce and sustain higher fares and new fee structures, and they increased their negotiating power vis-à-vis their unions. Profitability has improved dramatically.

But I have to say I am less confident that the same effect has been replicated across industries. Modest increases in concentration have nowhere near the power I just outlined. Markets are increasingly globally competitive or—as our Richmond team has outlined—locally competitive. The inflation data we monitor suggests that, if anything, business are losing rather than gaining pricing power.

So, why are we seeing markups increase?

One aspect of market concentration that strikes me as particularly important is the effect on suppliers: In the cases I’ve been a part of, and in my experience more generally, when firms get large, they acquire more bargaining power—especially with respect to their suppliers. This might help to explain how increased market concentration could coexist with quite muted inflation, particularly for consumer goods. It’s easiest to see in the retail sector. In 2017, the five largest retailers in the United States accounted for more than 35 percent of the 100 largest retailers’ total U.S. sales. I’ve seen directly the significantly greater pressure that these large stores are now able to exert on manufacturers with respect to pricing, delivery time and packaging, among other
variables. Suppliers that don’t comply might be replaced or lose space on a store’s shelves. And, as trade barriers and the costs of transportation and information have declined, it has become easier for retailers to develop new suppliers, both domestic and foreign, to take the place of suppliers who can’t meet their requirements. As these trends continue, and more downstream firms are subject to this “new normal,” I suspect we will experience continued downward pressure on an even broader range of relative prices. And these real factors could interact with monetary policy in a way that leads to a longer period of relatively low inflation.

The shift toward “private label” goods also has affected retailers’ bargaining power. Long gone are the days of “generic” food sold in black and white cans. Today, large retailers have the scale to develop their own products, and they can distribute everything from gourmet chocolate to pet food to clothing. By one estimate, the dollar share of private label goods will account for more than 25 percent of U.S. sales within the next decade. Private label goods offer retailers higher profit margins and a chance to increase their connection to consumers. But they also give retailers leverage over national brands; research has found that retailers earn much higher margins on national brands in categories where they have a strong presence with a store brand.

Retail isn’t the only sector where bargaining power relative to suppliers has increased. Beginning with the auto industry, companies across sectors have invested significantly in the capabilities and sophistication of their purchasing departments. They have built talent in their organizations and set high aspirations for savings. Executives are now, far more than at earlier points in my career, incentivized to avoid price increases, so they look for creative ways to reconfigure their operations to reduce purchasing volume and capture margin dollars from suppliers. When these
efforts are successful, they paint a different picture of how market concentration might lead to higher profits—a picture with far lower inflationary pressures.

And, of course, this perspective is equally applicable to the biggest supplier—labor. We know labor’s share of income has been decreasing over time. Part of that is perhaps the declining role and influence of labor unions. Part is no doubt the opening and leverage of low-cost global labor pools. But part is also likely increased bargaining power by evermore concentrated employers within domestic markets.

I’m struck, as I speak to employers and employees about today’s tight labor markets, by how hard it has been to see significant wage increases.

Employees aren’t changing jobs the way they did in the late ’90s; they often cite a “hangover” from the Great Recession that has made them feel less secure. Employers feel they have more ability to withstand wage pressure than they have power to pass increases along.

Net, I believe more-concentrated employers are leveraging their market power not to raise prices to consumers but to extract value from suppliers and from employees.

Understanding how market power affects labor and suppliers, and in turn the economy more broadly, is a topic I’m continuing to study and one I would love to get your thoughts on.

Now, I welcome your reactions and questions.