

United States Senate

Budget Committee

Corporate Profits are Soaring as Prices Rise: Are Corporate Greed and  
Profiteering Fueling Inflation?

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Testimony of Robert B. Reich

Mr. Chairman and members of the Committee,

My name is Robert Reich. I am currently Chancellor's Professor of Public Policy at the Goldman School of Public Policy at the University of California at Berkeley. In the Clinton Administration I served as Secretary of Labor. In the Carter Administration I directed the Policy Planning Staff of the Federal Trade Commission. In the Ford Administration I served as Assistant to the Solicitor General. I am the author of eighteen books about the American political economy.

Today I want to address a major cause of inflation which Congress and the Administration have the power to ameliorate. I will explain why corporations are raising their prices, assess the evidence, discuss why this entails an upward distribution of income and wealth from average working people to corporations and their shareholders, and suggest what government should and should *not* do to deal with this.

### **1. Corporations with near-record profits are raising prices because they don't face meaningful competition**

The Commerce Department reported last Wednesday, March 30, 2022, that corporate profits are at a 70-year high.<sup>1</sup> This raises an obvious question: With corporate profits at near record levels, why do we have inflation? When corporations are so flush with cash, why are they raising prices?

They are *not* raising prices because of the increasing costs of supplies and components and of labor (which are real but expected when an economy goes suddenly from a pandemically-induced deep freeze due to meeting the soaring demands of consumers who are emerging from the pandemic). Corporations enjoying record profits in a healthy competitive economy would *absorb* these costs. Instead, they're passing these costs on to consumers in the form of higher prices. Why? Because they *can*. And they can because they don't face meaningful competition.

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<sup>1</sup> <https://www.bea.gov/data/income-saving/corporate-profits>

If markets were competitive, companies would keep their prices down to prevent competitors from grabbing away customers. As the White House National Economic Council put it in a December report: “Businesses that face meaningful competition can’t [maintain high profit margins and pass on higher costs to consumers], because they would lose business to a competitor that did not hike its margins.”<sup>2</sup>

The underlying problem is that large American corporations have so much market power they can raise prices with impunity. Since the 1980s, two-thirds of all American industries have become more concentrated.<sup>3</sup> This concentration gives corporations the power to raise prices because it makes it easy for them to informally coordinate price increases with the handful of other companies in their same industry — without risking the possibility of losing customers, who have no other choice.

## 2. The Evidence

Corporations have been using the *excuse* of increasing costs to raise prices and make fatter profits. For example:

Starbucks is raising its prices to consumers, blaming the rising costs of supplies. But Starbucks is so profitable it could easily absorb these costs – it just reported a 31% increase in yearly profits.<sup>4</sup> Why didn’t it just swallow the cost increases? Ditto for McDonald’s and Chipotle, whose revenues have soared but who are nonetheless raising prices.<sup>5</sup> The reason they’re raising prices rather than absorbing increased costs is they have pricing power in their locales.

In April, Procter & Gamble announced it would start charging more for consumer staples ranging from diapers to toilet paper, citing “rising costs for raw materials, such

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<sup>2</sup> <https://www.whitehouse.gov/briefing-room/blog/2021/12/10/recent-data-show-dominant-meat-processing-companies-are-taking-advantage-of-market-power-to-raise-prices-and-grow-profit-margins/>

<sup>3</sup> <https://hbr.org/2018/03/is-lack-of-competition-strangling-the-u-s-economy>

<sup>4</sup> <https://www.nytimes.com/2022/02/01/business/starbucks-prices>.

<sup>5</sup> <https://money.com/chipotle-starbucks-mcdonalds-price-increases/>

as resin and pulp, and higher expenses to transport goods.”<sup>6</sup> But P&G continues to rake in huge profits. After its price increases went into effect, it reported a whopping 24.7 percent profit margin. It even spent \$3 billion during the fourth quarter buying back its own stock.<sup>7</sup> The reason it could raise prices and rake in more money is P&G faces very little competition. The lion’s share of the market for diapers (to take one example) is controlled by just two companies – P&G and Kimberly-Clark – which coordinate their prices and production. It was hardly a coincidence that Kimberly-Clark announced price increases similar to P&G’s at the same time P&G announced its own price increases.<sup>8</sup>

Or consider another consumer product duopoly – PepsiCo (the parent company of Frito-Lay, Gatorade, Quaker, Tropicana, and other brands), and Coca-Cola. In April, PepsiCo announced it was increasing prices, blaming “higher costs for some ingredients, freight, and labor.”<sup>9</sup> Yet PepsiCo recorded \$3 billion in operating profits through September.<sup>10</sup> If PepsiCo faced tough competition, it could never have gotten away with it. Consumers would have deserted it for lower-priced competitors. But PepsiCo appears to have colluded with its only major competitor, Coca-Cola – which announced similar price increases at about the same time as PepsiCo and has increased its own profit margins to 28.9 percent.<sup>11</sup>

All have been able to pass cost increases on to consumers in the form of higher prices because they face so little competition. As Chipotle’s chief financial officer said, “Our ultimate goal ... is to fully protect our margins.”<sup>12</sup>

The *New York Times* recently pointed out that “corporate executives have spent recent earnings calls [with Wall Street analysts] bragging about their newfound power to raise prices, *often predicting that it will last*” (emphasis added).<sup>13</sup> The Chief Financial Officer

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<sup>6</sup> <https://www.wsj.com/articles/procter-gamble-will-raise-prices-in-september-11618916498?redirect=amp>

<sup>7</sup> <https://www.cnbc.com/2021/10/19/procter-gamble-pg-q1-2022-earnings.html>

<sup>8</sup> <https://www.cnbc.com/2021/03/31/higher-commodity-costs-lead-to-price-hikes-from-kimberly-clark.html>

<sup>9</sup> <https://www.cnbc.com/2021/07/13/pepsico-and-conagra-plan-to-battle-rising-costs-with-higher-prices.html>

<sup>10</sup> <https://finance.yahoo.com/news/pepsico-earnings-q2-2021-103318871.html>

<sup>11</sup> [https://d1io3yog0oux5.cloudfront.net/\\_fd5695e7395cd38ea318a62ddca3817e/cocacola.com/news/2021-10-27\\_Coca\\_Cola\\_Reports\\_Continued\\_Momentum\\_and\\_Strong\\_1040.pdf](https://d1io3yog0oux5.cloudfront.net/_fd5695e7395cd38ea318a62ddca3817e/cocacola.com/news/2021-10-27_Coca_Cola_Reports_Continued_Momentum_and_Strong_1040.pdf)

<sup>12</sup> <https://www.nytimes.com/2022/01/21/business/fast-food-prices-inflation.html>

<sup>13</sup> <https://www.nytimes.com/2022/02/27/business/economy/price-increases-inflation.html>

of Constellation Brands, the parent company of Modelo and Corona beers, told investors in January that the company wants to “take as much as [we] can” from customers.<sup>14</sup> (Publicly, however, the company has blamed rising material costs for their increased prices.) The grocery food brand Hormel saw a 19 percent increase in operating income in the first quarter of 2022. Their CFO’s response to these soaring profits? “We’ve done a great job with our pricing.”<sup>15</sup>

Big Oil, too, has hit a gusher. Although major oil companies have faced increasing costs for crude oil, their profit margins are so large they could easily absorb those costs. The biggest oil companies (Shell, Chevron, BP, and Exxon) posted near-record profits last year, totaling \$75 billion.<sup>16</sup> But they’re passing the costs on to consumers in the form of higher price at the pump and for heating oil, and keeping their record profits. How can they do this? They don’t worry about losing market share to competitors.

Inflation itself has given some large corporations cover to increase their prices *above* their rising costs. With consumers expecting rising prices, it’s easy to tack on some extra beyond the corporation’s own increased costs. More than half of the companies surveyed by the business services reviews website Digital.com reported raising prices beyond what was required to offset rising input costs.<sup>17</sup>

Meat prices are soaring because the four giant meat processing corporations that dominate the industry are “using their market power to extract *bigger and bigger* profit margins for themselves,” according to a December report from the White House National Economic Council (emphasis added).<sup>18</sup>

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<sup>14</sup> <https://twitter.com/owenslindsay1/status/1493963096737656839>

<sup>15</sup> <https://www.minnpost.com/community-voices/2022/03/its-not-just-inflation-its-price-gouging/>

<sup>16</sup> <https://www.accountable.us/news/big-oil-companies-net-75-billion-in-profit-while-americans-struggle-to-heat-homes-fill-gas-tanks/>

<sup>17</sup> <https://digital.com/half-of-retail-businesses-using-inflation-to-price-gouge/>

<sup>18</sup> <https://www.whitehouse.gov/briefing-room/blog/2021/12/10/recent-data-show-dominant-meat-processing-companies-are-taking-advantage-of-market-power-to-raise-prices-and-grow-profit-margins/>

### **3. Corporations are using their near-record profits to buy back their shares of stock**

What are large corporations doing with their near-record profits? Using them to buy back their own shares of stock in order to deliver higher returns to their shareholders. Buybacks reduce a company's shares outstanding, pushing its profit-per-share figure higher.

Stock buybacks hit a new record last year. This year is on track to exceed it. In the first two months of 2022, S&P 500 companies have disclosed authorizations to buy back \$238 billion in stock -- a record pace, according to Goldman Sachs, which expects *\$1 trillion of buybacks this year* – an all-time high.<sup>19</sup> Chevron engaged in \$1.4 billion in stock buybacks and spent \$500 million more on shareholder dividends than it did in 2020. This year, the oil giants are planning to buy back at least \$22 billion *more*.<sup>20</sup>

Connect the dots. (1) Corporations have the highest profits in 70 years. (2) They have enough market power to pass on higher costs resulting from supply bottlenecks to consumers in the form of higher prices, rather than absorb the costs and accept lower profit margins. (3) They're utilizing consumer expectations of continued higher prices to raise prices even more than their higher costs, giving them even higher profit margins. (4) They're using their near-record profits to boost their share prices by buying back a record amount of their shares of stock. (5) As corporations raise their prices, they're also eroding the value of their workers' wages. Corporations are handing out wage increases to attract or keep workers with one hand, but eliminating those wage increases by raising prices with the other.

What's the result? An upward transfer of income and wealth from consumers and workers – many of whom live from paycheck to paycheck – to shareholders, half of

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<sup>19</sup> <https://www.thestreet.com/investing/stock-buybacks-at-record-pace-for-2022>

<sup>20</sup> <https://www.bloomberg.com/news/articles/2022-03-15/oil-and-gas-share-buybacks-boomed-before-energy-prices-hit-highs?sref=OKUfhQHv>

whom are in the richest 1 percent of the population and more than 80 percent of whom are in the richest 10 percent.

Pointing out these connections between corporate pricing power, inflation, and this upward transfer of income and wealth is not “bashing” big business. Big corporations are doing precisely what their shareholders want and expect them to do – maximize profits and share values. But just because this is good for shareholders doesn’t mean it’s good for the economy, which includes consumers and workers. We may rail at what corporations are doing -- accuse them of price gouging and profiteering -- but unless or until there are laws preventing them from doing this, they will continue to do so.

#### **4. What should *not* be done**

The Fed is battling inflation the old way. It has already raised interest rates by a quarter point and penciled in six more increases by the end of the year. Fed Chair Jerome Powell says he is ready to do whatever it takes to bring inflation down, including following the example of his predecessor Paul Volcker, who increased interest rates to 20 percent in 1981. Let me remind you that Volcker’s rate rise triggered a deep recession and double-digit unemployment.

We can debate whether that harsh medicine in 1981 was necessary. What should be clear is that the current inflation is nothing like the inflation of the late 1970s.

The Fed apparently believes that inflation is coming from the wage gains workers have been receiving due to their newfound bargaining leverage in an economy facing worker shortages. Powell openly worries that “the labor market is extremely tight,”<sup>21</sup> to “an unhealthy level.”<sup>22</sup> As a result, the Fed is on the way to raising interest rates repeatedly in order to slow the economy and presumably reduce the bargaining leverage of American workers.

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<sup>21</sup> <https://www.federalreserve.gov/newsevents/speech/powell20220321a.htm>

<sup>22</sup> <https://www.youtube.com/watch?v=kb5Qn0kiO6I>

With due respect, this makes no sense. When American corporations are enjoying record profits, why should wage gains lead to price increases? In a healthy economy we would expect corporations to pay the higher wages out of their profits rather than to pass them on to consumers in higher prices. Most American workers have not had much of a real wage increase (adjusted for inflation) in four decades. The labor market is not “unhealthily” tight, as Jerome Powell asserts; corporations are unhealthily fat. Workers do not have too much power; corporations do.

Raising interest rates is the wrong medicine for the wrong disease. Higher interest rates will not stop corporations from using their pricing power. Instead, higher interest rates will slow the economy and potentially cause millions of lower-wage workers to lose their jobs and forfeit long-overdue real wage increases. Higher rates will hurt millions of people who are among the most vulnerable in the economy.

The objective should be to stop big profitable corporations from using their power to raise prices, thereby fueling inflation. The correct medicine is to reduce corporate market power.

## **5. What *should* be done.**

A preferable (but by no means perfect) set of weapons against inflation are tougher antitrust enforcement, a windfall profits tax, and price controls.

*Tougher antitrust enforcement* is necessary. As I noted earlier, since the 1980s, two-thirds of all American industries have become more concentrated. Monsanto now sets the prices for most of the nation’s seed corn. Wall Street has consolidated into five giant banks. Airlines have merged from 12 carriers in 1980 to four today, which now control 80 percent of domestic seating capacity. The merger of Boeing and McDonnell Douglas has left the US with just one large producer of civilian aircraft — Boeing. Three giant cable companies dominate broadband: Comcast, AT&T and Verizon. A handful of drug companies control the pharmaceutical industry: Pfizer, Eli Lilly, Johnson & Johnson,

Bristol-Myers Squibb and Merck. Two giant firms dominate consumer staples. A handful of national retailers and food outlets dominate local markets. And so on.

Such concentration makes it easy for corporations to coordinate price increases with the handful of other companies in their same market without risking the possibility of losing customers, who have no other choice. If corporations had less market power, they would have less power to raise prices.

But antitrust litigation is complex and time consuming. I directed the policy planning staff at the Federal Trade Commission in the Carter Administration and saw this firsthand. Corporate America will do whatever it can to keep its near-record profits. Nonetheless, antitrust is worth the effort over the long term. Corporate concentration continues to harm workers and consumers while rewarding CEOs and investors.

One possible initiative in the shorter term is a bill<sup>23</sup> introduced by Rep. Jan Schakowsky of Illinois, the COVID-19 Price Gouging Prevention Act. The bill provides that “it shall be unlawful for any person to sell or offer for sale a good or service at a price that is unconscionably excessive; and indicates the seller is using the circumstances ... to increase prices unreasonably.” The bill goes on to direct the Federal Trade Commission to investigate whether the price reasonably reflects “additional costs, not within the control of” the seller, or whether it reflects opportunistic price-gouging. The FTC already has the power to carry out such investigations and impose penalties under existing law.

*A windfall profits tax* is also sensible. Senator Sheldon Whitehouse has introduced a windfall profits tax bill that would levy a quarterly tax on large oil companies and distribute the revenue to consumers through a quarterly rebate. The per-barrel tax would be equivalent to half the differential between the pre-pandemic average oil price from 2015 through 2019 and current prices. Senator Bernie Sanders has introduced a temporary emergency measure modeled on the broad-based windfall profits tax implemented during the first and second World Wars and the Korean War, that would

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<sup>23</sup> <https://www.congress.gov/bill/117th-congress/house-bill/675/text>

levy a 95 percent windfall profits tax on the profits of large corporations that exceed their average profit level from 2015 to 2019

*Price controls* are a third possibility. They worked well in World War II, but not so well in the 1970s, when they were half-baked and badly executed.

## **Conclusion**

Congress and the administration have the power to stop corporations who are enjoying the highest profits in 70 years from raising their prices, which is requiring American workers and consumers to subsidize wealthy investors. It is preferable for Congress and the administration take direct action against this rather than for the Federal Reserve to raise interest rates to slow the economy and risk another recession, which will harm average working people.