

AgLetter



RETAIL FOOD PRICES AND EXPENDITURES

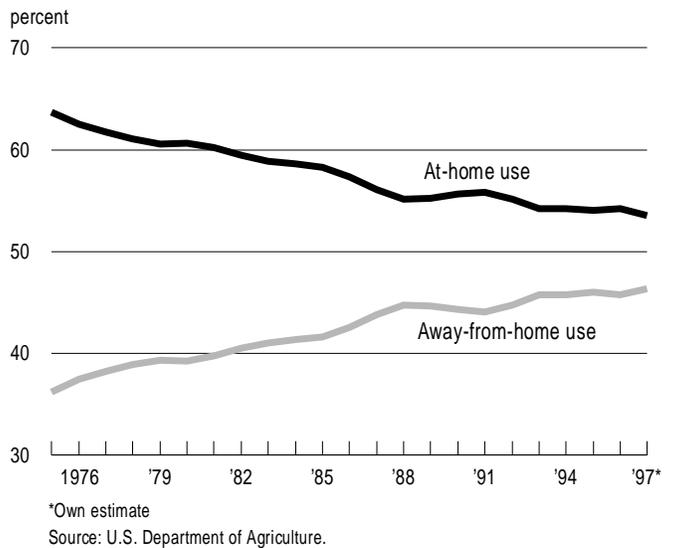
The rise in retail food prices slowed appreciably last year. The slowing stemmed primarily from ample supplies of most food products and from the abating inflationary pressures on the costs of processing and distributing raw food commodities beyond the farm gate. Aside from the added uncertainties relating to El Niño and to the so-called Asian crisis, the same factors suggest that 1998 will mark another year of modest gains in retail food prices.

As reported by the Bureau of Labor Statistics, the index of retail food prices in 1997 averaged 2.6 percent higher than the year before. That marked a slowing from the 3.3 percent gain the year before and it was the smallest average rise in food prices in three years. However, that measure still portrays food prices as rising faster than the 2.3 percent gain registered by the overall Consumer Price Index last year. An alternative measure using fourth quarter-to-fourth quarter comparisons casts last year's food price rise in a better light relative to other items purchased by consumers and it more accurately portrays the slowing that occurred during the year. On this basis, the rise in retail food prices slowed from 4.2 percent in 1996 to a five-year low of 1.7 percent last year, slightly less than the similarly calculated 1.9 percent rise in overall consumer prices.

Two components make-up the index of retail food prices. Food for at-home use accounts for about 63 percent of the weighting in the overall food price index while food for consumption away from home represents the other 37 percent. Since the early 1990s, the rise for the food at-home component had consistently exceeded that for the away-from-home component. From 1992 through 1996, the rise in retail prices for food at home averaged 3.1 percent (fourth quarter-to-fourth quarter basis) while that for food away from home averaged 2.1 percent. However, that pattern was broken last year when at-home food prices rose only 1.2 percent while away-from-home food prices rose 2.6 percent.

Food price trends are a major factor influencing overall food expenditures. Other contributing factors include population growth and the growing preferences

Share of food expenditures for at-home use continues to trend lower



of consumers for added processing and easier-to-fix meals. According to estimates compiled by the U.S. Department of Agriculture, food expenditures rose at a compound annual rate of about 5 percent over the past decade and now surpass \$700 billion a year. The bulk (83 percent) of those expenditures are made by families and individuals. Another 16 percent are made by governments and businesses while the remaining 1 percent represents expenditures made to produce food for at-home use. The food expenditures by families and individuals (plus the foods acquired with food stamps and vouchers provided by the Women, Infants and Children Program) now absorb less than 11 percent of all disposable personal income. The share of disposable personal income spent on food by families and individuals has drifted steadily lower over the years, falling from about 20 percent in the early 1950s and about 14 percent in the mid 1970s.

A little over half (54 percent) of all food expenditures are for foods destined to be consumed at home. The remaining share (46 percent) represents expenditures for foods consumed away from home. (Because away-from-home expenditures include outlays for more extensive preparations and services than is the case for food consumed at

home, industry analysts believe the quantity shares of food consumption closer approximate two-thirds at-home and one-third away from home.) Over the years, several factors—including the declining real price of raw food commodities, the growing affluence of most food buyers, the trend toward two-income families, and the desire for more leisure-time activities—have encouraged consumers to seek foods with added processing and preparation. This trend has been evident in all types of food expenditures, but more so in the away-from-home component. Accordingly, growth in the away-from-home component has outpaced that for at-home use. Thirty years ago, the split in food expenditures was two-thirds for at-home use and one-third for use away from home.

Most food consumed in the United States originates domestically. A large share of the expenditures on domestically-originated foods represents the cost of transporting, processing, and packaging the raw food commodities beyond the farm gate. In 1996, this so-called food marketing bill approximated \$425 billion and it accounted for over 75 percent of all consumer expenditures on domestically-produced farm foods (excluding fish and seafood). Nearly half of the food marketing bill reflected the cost of labor. Packaging materials accounted for an additional 11 percent. The remaining 40 percent was about equally distributed between transportation, corporate profits, advertising, fuels and electricity, depreciation, rent, taxes, and other (including interest and repairs).

Prices of inputs represented in the food marketing bill, on average, closely parallel overall inflationary trends. As such, the abating inflationary pressures in recent years, in conjunction with the highly competitive nature of the food market, have helped to moderate the rise in retail food prices. The overall price index for inputs included in the food marketing bill rose less than 1 percent in 1996 and only a little over 1.5 percent in 1997, well short of annual gains that averaged 2.8 percent the prior two years. A downturn in prices of packaging and container materials, especially for paper boxes, accounted for much of the slower rise. But lower rental rates and lower prices for transportation and supplies also contributed to the slowing of the past couple of years.

The relative balance between the demand for, and the supply of food is the other major factor influencing short-run changes in retail food prices. And since food demand tends to be more stable, food price swings more typically reflect the greater variability in food supplies. Following some temporary disruptions in 1996, evidence of a rebuilding in supplies of several key food products helped to moderate food price pressures in 1997 and give promise of continued moderate gains for this year. This

Percent change in retail food prices*

	1995	1996	1997	1998**
All food	2.9	3.3	2.6	2 to 3
Away from home	2.3	2.5	2.8	2 to 3
At home	3.2	3.7	2.5	1 to 3
Red meats	0.1	3.5	3.0	-2 to 0
Beef	-0.8	-0.3	1.7	0 to 2
Pork	0.7	9.9	5.2	-6 to -4
Poultry	1.4	6.2	2.8	-1 to 1
Fish & seafood	4.8	0.9	2.3	1 to 3
Eggs	5.4	18.0	-1.5	-1 to 1
Dairy products	0.8	7.0	2.4	0 to 2
Fruits & vegetables	7.7	3.5	1.9	2 to 4
Fresh fruits	8.8	7.1	0.8	2 to 4
Fresh vegetables	12.1	-2.0	2.8	3 to 5
Processed fruits & vegetables	2.3	5.0	2.4	1 to 3
Cereals & bakery products	2.7	3.9	2.1	1 to 3
Fats & oils	2.8	2.4	0.9	1 to 3
Sugar & sweets	1.7	4.5	2.9	1 to 3
Nonalcoholic beverages	6.9	-2.4	3.7	1 to 3
Other prepared foods	2.4	3.4	3.2	2 to 4

*Based on average annual indices.

**USDA forecasts.

Source: Bureau of Labor Statistics and U.S. Department of Agriculture.

is particularly true in the meat, poultry, and milk complex which—together with fish and seafood—accounts for about 40 percent of the relative expenditure weighting among the components that make up the index of retail prices of foods for at-home use.

Per capita consumption of all meats has drifted slowly upwards over the years, rising about one-half a percentage point annually. In contrast, per capita production of all meats, on a trade-adjusted basis, drifted lower from 1995 through 1997, culminating in some price pressures that were especially apparent for pork in 1996. However, a recovery in production during the second half of 1997, coupled with a slowing in what had been very rapid growth in the small share of production shipped to overseas markets triggered a rebuilding in domestic supplies and an easing in retail meat prices. The easing was apparent for both red meats and poultry. After posting year-over-year gains of about 5 percent from the fourth quarter of 1996 through the first half of last year, retail prices of red meats in the fourth quarter of 1997 were unchanged from the year before. Both pork and beef prices were at, or below, the year-earlier level in the fourth quarter. Poultry prices, which posted a 7.7 percent year-over-year gain in the fourth quarter of 1996, also lagged year-earlier levels during the fourth quarter of 1997. A large increase in pork production and the Asian-related reversal in U.S. meat-trade prospects suggest that per capita domestic meat supplies for 1998 will be up 3 percent and at a new high. As such, USDA analysts believe red meat prices this year

will average lower than last year while poultry prices may be little changed.

Per capita consumption of eggs leveled off in recent years after trending lower in the 1970s and the 1980s. Retail egg prices nevertheless tend to be quite volatile as temporary supply disruptions and/or spurts in exports can trigger wide price swings in this staple of cooking and consumer diets. Such factors contributed to an 18 percent jump in egg prices in 1996. But since then, conditions have shifted more to the benefit of consumers. Production gains were comparatively modest last year but widened in the fourth quarter. That plus the USDA's projection of a 2.6 percent rise in production this year suggests that egg prices in 1998 may hold close to the lower average posted in 1997.

The upward pressures on retail dairy product prices moderated considerably last spring and summer after posting a large gain in 1996. Milk production that year declined slightly due to very high feed costs and poor quality forage. Production turned up modestly in 1997 but the supply/demand balance for most dairy products remained tight this fall and winter. With milk production expected to be virtually unchanged this year, that tightness could persist for several more months. Per capita consumption of milk has been relatively flat over the years as declines in fluid milk consumption were offset with gains in the amount of milk used in cheeses and other dairy products. For 1998, USDA analysts believe retail prices of dairy products will remain quite volatile and average somewhat higher than last year.

Fruits and vegetables account for another sizable portion of the expenditure weighting used to calculate the at-home component of retail food prices. But an updated re-weighting of the overall Consumer Price Index will lower the contribution of this component to at-home food prices to 15 percent this year from 20 percent last year. Prices for the "fresh market" component, which substantially outweighs the processed component of fruit and vegetable prices, often exhibit wide swings as the brief shelf life for many of these items restricts supplies in the very short run to seasonal harvest patterns. Many of these items have very short growing periods and multiple production cycles within a year. Yet weather disruptions during any part of the planting, growing, or harvesting season, coupled with the tenderness of the plants and the strong emphasis on visual quality for this component of the food basket can cause major short-run supply gaps that often translate into wide price swings. In addition, growing consumer preferences have translated into a steady uptrend in per capita consumption of fresh fruits and vegetables, as well as in fruit juices and processed vegetables. Relatively few weather disruptions last year,

at least until the fall, helped moderate the pressures on fresh fruit prices. Fresh vegetable prices, however, exhibited considerable upward pressure late in the year. Because of the vagaries of weather, it is extremely difficult to forecast fruit and vegetables supplies, especially for the fresh-market component. This is particularly true this year as El Niño weather conditions on the West Coast and in the Southeast are already causing concerns about short-run supply gaps for some items. In acknowledgment of this, the latest USDA forecast suggests the fruit and vegetable component may register the biggest food price gain this year.

Retail prices for cereals and bakery products—which account for about 15 percent of the weighting for at-home food prices—have recorded fairly steady gains in recent years, averaging 3.7 percent since 1990. Last year's rise of 2.1 percent was the smallest for this component of food prices since 1977. Cereal prices actually declined for the second straight year in 1997, largely reflecting the refocused competition for market share among leading cereal manufacturers. Paced by ready-to-eat cereals, the cereal and bakery products component of the food basket has enjoyed substantial growth in per capita consumption over the years, even exceeding that for fruits and vegetables. While production of grains is important in the retail price trends of this component, the price of bulk grains represents a very minor share of what consumers spend on cereals and bakery products. The costs of processing, packaging and distribution account for the bulk of the retail value of these products. As such, trends in overall inflation tend to be a major force in year-to-year changes in retail prices of cereals and bakery products. Accordingly, the USDA projects this year's rise in retail prices for cereals and bakery products will be close to that of a year ago.

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SELECTED AGRICULTURAL ECONOMIC INDICATORS

	Latest period	Value	Percent change from		
			Prior period	Year ago	Two years ago
Prices received by farmers (<i>index, 1990-92=100</i>)	February	100	-2.9	-5	-6
Crops (<i>index, 1990-92=100</i>)	February	108	-1.8	-4	-12
Corn (\$ per bu.)	February	2.50	-2.3	-6	-26
Hay (\$ per ton)	February	97.20	-0.9	-5	23
Soybeans (\$ per bu.)	February	6.63	-0.9	-10	-5
Wheat (\$ per bu.)	February	3.36	0.9	-14	-33
Livestock and products (<i>index, 1990-92=100</i>)	February	93	-1.1	-5	0
Barrows and gilts (\$ per cwt.)	February	35.80	-1.9	-32	-24
Steers and heifers (\$ per cwt.)	February	62.70	-5.1	-4	3
Milk (\$ per cwt.)	February	14.70	0.0	9	6
Eggs (¢ per doz.)	February	64.7	-12.6	-15	-15
Consumer prices (<i>index, 1982-84=100</i>)	February	162	0.2	1	5
Food	February	159	-0.3	2	6
Production or stocks					
Corn stocks (<i>mil. bu.</i>)	December 1	7,230	N.A.	5	18
Soybean stocks (<i>mil. bu.</i>)	December 1	1,995	N.A.	9	9
Wheat stocks (<i>mil. bu.</i>)	December 1	1,615	N.A.	32	21
Beef production (<i>bil. lb.</i>)	January	2.16	6.6	-3	-3
Pork production (<i>bil. lb.</i>)	January	1.63	-0.4	12	5
Milk production* (<i>bil. lb.</i>)	February	10.5	-7.6	1	0
Receipts from farm marketings (<i>mil. dol.</i>)	October	25,061	20.3	-5	4
Crops**	October	15,907	64.9	-5	12
Livestock	October	7,542	-7.9	-7	-3
Government payments	October	1,612	-46.4	6	-20
Agricultural exports (<i>mil. dol.</i>)	December	5,243	-4.3	0	-2
Corn (<i>mil. bu.</i>)	December	141	17.0	-25	-24
Soybeans (<i>mil. bu.</i>)	December	120	-21.0	-1	34
Wheat (<i>mil. bu.</i>)	December	84	3.5	58	-18
Farm machinery sales (<i>units</i>)					
Tractors, over 40 HP	February	5,132	-2.5	-4	16
40 to 100 HP	February	2,930	13.0	1	23
100 HP or more	February	2,202	-17.6	-11	8
Combines	February	493	-29.3	55	39

N.A. Not applicable

*20 selected states.

**Includes net CCC loans.



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