Food & Marketing

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Food Price Increases for 1998 Could Be Lowest Since Early '90's

Consumers are expected to pay between 2 and 3 percent more for food in 1998 than in 1997. If the increase is closer to 2 percent, it could be the smallest rise in the Consumer Price Index (CPI) for food since the early 1990's—1.2 percent in 1992 and 2.2 percent in 1993. Last year's retail food price increase was 2.6 percent.

Modest rises in the food CPI are projected to continue, according to USDA's 1998-2007 baseline, increasing at an average rate of about 2.5 percent through 2007. This compares with an average rise of 3.1 percent in the general inflation rate projected for this period.

What determines whether this year's rise will be closer to 2 or to 3 percent are a number of factors that are as yet uncertain. The first is whether the sluggish export market for beef, pork, and poultry continues throughout 1998. The second concerns the duration of the El Niño phenomenon and related turbulent weather in fresh vegetable growing areas of Florida, California, Arizona, Texas, and Mexico. With beef, pork, and poultry accounting for 19 percent of the food-at-home CPI, and fruits and vegetables an additional 15 percent, these unknowns could have a major effect on food prices in 1998.

Underpinning retail food price changes are general economic developments in recent years and the relationship between farm and marketing costs. Food price increases have been limited by the low general inflation rate, which is forecast to increase 2-3 percent in 1998. Increasing economies of size in the farm sector have also helped slow growth in food production costs, but the farm-value share of the retail price for most food items has continued to decline, expected at just 24-25 cents of the food dollar in 1997 and 1998. Retail prices are thus determined more by processing and marketing costs, which generally parallel the general inflation rate and which tend to rise more slowly than farm costs.

Also, a growing share of the food dollar has been spent on purchases of food prepared away from home—over 47 percent for the past 2 years, compared with 39 percent in 1968 and 45 percent in 1978. Away-from-home food prices, which contain a large service component, are being held down by competition among restaurants and fast-food establishments.

The food-at-home CPI increase of 2.5 percent in 1997 was moderated by lower grain prices, large supplies of competing meats (a result of lower grain prices), adequate supplies of fresh fruits and vegetables, increased sugar production, and strong competition in the soft drink and prepared food industries. The 1997 price increase of 2.8 percent for food away from home was the largest since 1991 and was driven partly by tighter labor markets that have pushed up wages generally. However, continued strong competition among restaurants and fast-food establishments limited the pass-through of higher wage and raw materials costs to consumers. A limited pass-through is expected for early 1998, as labor and raw material costs have stabilized.

The revised CPI item structure implemented by the Bureau of Labor Statistics in December 1997 changes the relative importance, or weight, of some of the key food categories in terms of expenditure shares, which influences the all-food CPI. Meats, for example, which accounted for 12.2 percent of the all-food CPI under the previous structure, fell to 10.9 percent. Among the other major categories whose weights changed are fruits and vegetables—from 12.7 to 9.1 percent—and cereals and bakery products—from 9.2 to 10 percent.

The interplay of specific factors in the individual food CPI sectors helps explain the food price changes in 1997 and those expected in 1998.

Meats. Large meat supplies and reduced prospects for exports in 1998 are exerting downward pressure on U.S. livestock and poultry prices. The meat, poultry, and fish index, which increased 2.9 percent in 1997, is expected to drop as much as 2 percent in 1998. Large meat supplies, combined with currency devaluations in other countries and the need to find alternatives to sagging Asian markets, are making the U.S. a more attractive market for foreign exporters and challenging the U.S. in global markets. As a result, net exports of U.S. red meat are expected to shrink in 1998, adding to already abundant meat supplies competing for the U.S. consumer dollar.

- *Beef and veal.* After increasing a modest 1.7 percent in 1997, the CPI for beef and veal is expected to increase at about the same rate in 1998—between 0 and 2 percent—as large supplies of competing meats and less-than-robust international trade hold down price increases at least until late summer. Commercial beef production in 1998 is expected to fall less than 1 percent from 1997 levels, although per capita beef supplies are expected to rise fairly sharply as the Asian financial crisis and the strong U.S. dollar lower beef exports and increase imports. U.S. beef exports are likely to decline about 2 percent in 1998, as reduced sales to the Pacific Rim offset any increased sales to Mexico.

- *Pork*. Forecasts of a 10-percent increase in pork production in 1998 should lead to the largest per capita consumption rate since 1994, increasing about 4 pounds from 1997 levels to almost 70 pounds per person. With expectations of plentiful supplies of pork and competing meats throughout 1998, pork retail prices are expected to fall 4-6 percent, following a 5.2-percent rise in 1997. U.S. pork exports in 1998 are expected to be 990 million pounds, off about 5 percent from 1997. Lower demand is expected in Asia, particularly in Japan, as a stronger U.S. dollar and lower priced Korean pork products erode U.S. market share.
- *Poultry*. Production of broiler meat in 1998 is expected to be almost 28.4 billion pounds, up 4 percent from 1997, while turkey production is expected to be down 1 percent following weak net returns in 1996 and 1997. During the past several months, export prospects for U.S. poultry have become less certain due to the continuing financial crisis in many Asian countries; currency depreciation against the U.S. dollar in Thailand and Brazil, which gives them a competitive price advantage over the U.S. in many major markets; and the outbreak of avian influenza in Hong Kong—and subsequent dampening of demand for all poultry products—which was the second-largest market for U.S. broilers and turkeys.

  As these conditions continue into 1998, broiler production increases will likely slow down from initial brisk levels. The CPI for poultry is expected to be unchanged, after increasing 2.8 percent in 1997.
- *Other meats*. The price movements of these highly processed food items (hot dogs, bologna, sausages) are influenced by the general inflation rate as well as the cost of the meat inputs. Retail prices of these products increased 2.8 percent in 1997, and are expected in 1998 to remain flat.

Changes in Food Price Indicators 1996 through 1998

Items	Relative importance[1]		1996	Final 1997	Forecast 1998
	—Percent—		—Percent change—		
All items			3.0	2.3	2 to 3
All food	100.0		3.3	2.6	2 to 3
Food away from home	37.1		2.5	2.8	2 to 3
Food at home	62.9	100.0	3.7	2.5	1 to 3
Meats	10.9	17.3	3.5	3.0	-2 to 0
Beef and veal	4.8	7.7	-0.3	1.7	0 to 2
Pork	3.8	6.1	9.8	5.2	-6 to -4
Other meats	2.2	3.5	3.6	2.8	-1 to 1
Poultry	3.2	5.1	6.2	2.8	-1 to 1
Fish and seafood	2.2	3.5	0.9	2.3	1 to 3
Eggs	0.8	1.3	18.0	-1.5	-1 to 1
Dairy products	6.8	10.8	7.0	2.4	0 to 2
Fats and oils	1.9	3.0	2.4	0.9	1 to 3
Fruits and vegetables	9.1	14.5	3.5	2.0	2 to 4
Fresh fruits and vegetables	7.0	11.1	2.8	1.7	3 to 5
Fresh fruits	3.6	5.7	7.1	0.8	2 to 4
Fresh vegetables	3.4	5.4	-2.0	2.9	3 to 5
Processed fruits and vegetables	2.1	3.4	5.0	2.4	1 to 3
Processed fruits	NA	NA	5.8	2.5	0 to 2
Processed vegetables	NA	NA	4.0	2.3	1 to 3
Sugar and sweets	2.5	3.9	4.5	2.9	1 to 3
Cereals and bakery products	10.0	15.9	3.9	2.1	1 to 3
Nonalcoholic beverages	7.0	11.2	-2.4	3.7	1 to 3
Other foods	8.5	13.5	3.4	3.2	2 to 4

[1]First column: Bureau of Labor Statistics estimated weights as share of all food, December 1997. Second column: weights as share of food at home, December 1997.
NA = Not available.
Sources: Historical data, Bureau of Labor Statistics; forecasts, Economic Research Service.
Economic Research Service, USDA

Fish and seafood. Almost 50 percent of fish and seafood consumed in the U.S. comes from imports. Imports for 1997 were up—salmon, shrimp, crawfish, mussels, tilapia, and oysters. Domestic production of catfish and trout was also up. In the 1990's, U.S. per capita seafood consumption has remained flat, between 14.8 and 15.2 pounds of edible meat per year, with population growth accounting for any increases in total domestic seafood consumption. The CPI for fish and seafood is expected up 1-3 percent in 1998, compared with 2.3 percent in 1997.

Eggs. Following volatile egg prices and a CPI increase of 18 percent in 1996, higher production and lower export levels during 1997 led to larger U.S. consumption of eggs and a drop of 1.5 percent in average retail prices. With table-egg production expected to increase further in 1998—by about 2 percent—consumption is expected to increase again, to the highest level since 1988. The CPI for eggs in 1998 is expected to be flat.

Dairy products. Higher milk production, along with modest dairy product demand, led to a 2.4-percent CPI increase in 1997. Production in 1997 rose about 1 percent from 1996 levels, with demand up and feed costs down. Increased output led to large U.S. commercial dairy stocks, particularly of nonfat dry milk and American cheese. With milk output expected to increase slightly this year, retail prices for dairy products are forecast to increase from 0 to 2 percent in 1998.

Fats and oils. Since fats and oils are highly processed food items, their prices are influenced by the general inflation rate as

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well as by U.S. and world supplies of vegetable oils. The CPI for fats and oils is expected to increase a modest 1-3 percent in 1998, following a rise of just 0.9 percent in 1997.

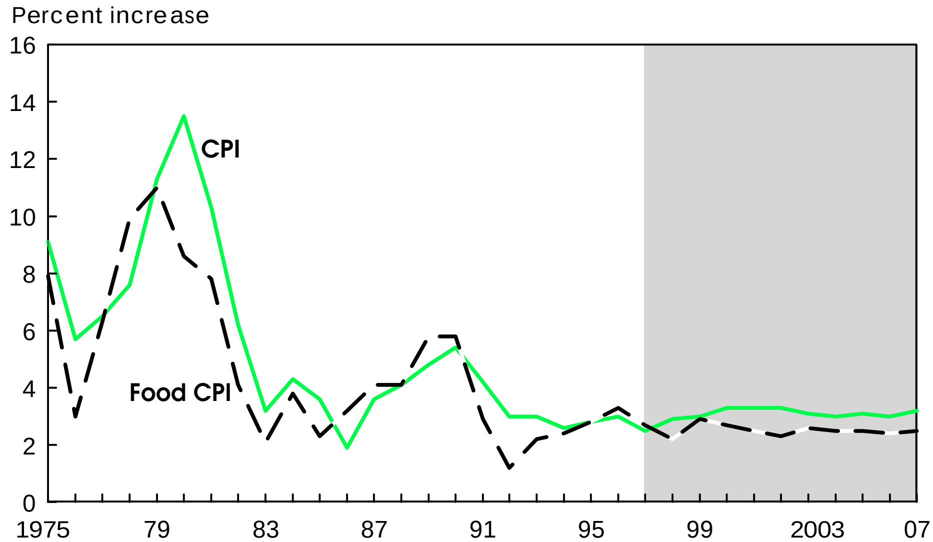
Fruits and vegetables. Plentiful supplies of both domestic and imported fruits and vegetables limited retail price increases in 1997. But higher prices for potatoes, onions, and cabbage due to lower stocks and strong exports, along with delayed plantings, could result in periods of short supplies and elevated prices through spring 1998. (See "Briefs," page 6, for a discussion of this year's weather impacts on horticultural crops.)

- *Fresh fruits.* Total fruit-bearing acreage has increased steadily for the past 5 years. Citrus fruit acreage has expanded as replantings in Florida following the late-1980's freezes have begun to bear fruit. These trees, which include oranges and grapefruit, will produce increasingly larger crops into the early 2000's. California has also expanded its orange production area, with most of its crop going for fresh use; Florida's oranges are used mainly for juice.

  Supplies of summer fruits were also abundant in 1997, bringing about generally lower increases in prices and expanded export opportunities. California, the largest U.S. producer of peaches, produced another bumper crop in 1997. Supplies of nectarines, plums, apricots, and sweet cherries were also abundant in 1997. Apple production was down about 2 percent in 1997, with a smaller Washington crop and smaller fruit size in North Carolina and Virginia. Supplies of bananas, which are virtually all imported, were ample during the past 2 years.

  Despite heavier-then-normal rains in California and Florida this winter, citrus fruits were already developed by the time the stormy weather began, although the rains have hampered harvesting activities for this year's large orange crops. The 1998 peach crop in the southeastern U.S. could be significantly reduced as a result of 3 consecutive days of freezing temperatures in mid-March, although peaches are a small component of total fruit production. The fresh fruit index, which increased a modest 0.8 percent in 1997, is expected to increase 2-4 percent in 1998, with strong U.S. demand expected to continue and exports projected to rise.

Growth in Food Prices To Remain Near General Inflation Rate



1998 forecast; 1999-2007 projected.
Sources: Bureau of Labor Statistics, U.S. Department of Labor; forecasts and projections, Economic Research Service
Economic Research Service, USDA

- *Fresh vegetables*. Growing conditions in the major fresh vegetable producing areas were mixed in 1997. A January freeze in Florida resulted in minimum damage to several fresh-market vegetables—squash, snap beans, green peppers, eggplant, and tomatoes—with the impact on retail prices for these items less than originally expected. Fresh-market vegetables grown in States not affected by the freeze are potatoes, lettuce, onions, celery, broccoli, cauliflower, and cabbage.

  Growing conditions normalized during the spring and summer months, but the weather did an about-face in the last quarter of 1997. Torrential rains in Florida; rain and cold in the desert areas of California, Arizona, and Texas; and an unusual December freeze in west Mexico led to lower supplies and higher retail prices for tomatoes, bell peppers, lettuce, and broccoli.

  In addition to the price effects of the weather-related problems, U.S. growers reduced harvested area from a year earlier for some fresh-market vegetables and for potatoes (both processed and fresh), raising prices in fall 1997 from a year earlier. On an annual basis, fresh vegetable retail prices increased 2.9 percent in 1997. Prices in 1998 are expected to increase 3-5 percent. Prices in the first half of the year are likely to average about 10-15 percent higher than a year earlier due to periods of weather-related supply shortages in the wake of heavy rains in California. The magnitude of the annual increase depends on several factors: continuation of the unsettled weather patterns related to a strong El Niño through spring; 1998 plantings; and expected higher prices for potatoes, which account for the highest expenditure share of the vegetable CPI.

- *Processed fruits and vegetables.* Contract acreage for the five leading processing vegetables (tomatoes, sweet corn, snap beans, green peas, and cucumbers) was down 3 percent in 1997, after a 9-percent decline in planted acreage a year earlier. However, processed vegetable prices increased a modest 2.3 percent in 1997 and are expected to increase a modest 1-3 percent in 1998 because of plentiful supplies. Processing tomato supplies are expected up 10 percent, and supplies of corn, beans, and peas are expected about the same as 1997. The ready availability of supplies also kept the CPI increase for processed fruits to 2.5 percent in 1997, with an expected increase of 0-2 percent in 1998.

Sugar and sweets. Domestic sugar production was down 2 percent to 7.2 million tons in 1996/97 but is projected up 9 percent in 1997/98; higher sugarbeet prices and lower prices for competing crops led to acreage increases in both years. Lower retail prices for selected sugar-related food items in 1997 held the sugar and sweets CPI to under 3 percent. Although U.S. sugar consumption has grown by about 1.9 percent per year since 1985/86 and industrial use of sugar has risen, the CPI increase is projected at a moderate 1-3 percent in 1998.

Cereals and bakery products account for a large portion of the at-home food CPI—almost 16 percent. While significantly higher grain prices contributed to higher retail prices for selected bakery products in 1996, grain prices came down in 1997. Moreover, most of the costs to produce cereal and bread products are for processing and marketing—more than 90 percent in most cases—making grain and other farm ingredients a generally minor cost consideration. Competition for market share among the three leading breakfast cereal manufacturers led to a drop of 9.7 percent in the cereal component of the index from 1995 to 1996, with an additional decrease of 1.4 percent from 1996 to 1997. With competition among producers expected to continue, the CPI for cereals and bakery products is expected to rise by just 1-3 percent in 1998, following the 1997 increase of 2.1 percent.

Nonalcoholic beverages. Coffee and carbonated beverages are the two major components, accounting for 32 and 50 percent of the nonalcoholic beverages index. Lower coffee prices drove the index down by 2.4 percent in 1996, but the index moved up again in 1997—by 3.7 percent—reflecting a jump of 12.6 percent in coffee prices. Speculation about a smaller 1997/98 coffee crop in Brazil (the largest Arabica coffee producer), and an uncertain labor situation in Colombia, led to sharp increases in green coffee costs on the world market in spring and summer 1997. These price increases, combined with low U.S. coffee stocks, produced wholesale price fluctuations that translated into higher retail prices for 6 months of the year.

A 1.4-percent drop in carbonated beverage prices mitigated the increase in the nonalcoholic beverages index in 1997. Competition in the soft drink industry between the two major competitors peaked during the summer months, continued through the end of the year, and led to the reduction in carbonated beverage prices. Moreover, prices of Robusta coffee beans, the primary ingredient in retail-store coffee blends, increased less sharply than prices for Arabica beans, which are used in gourmet coffees. Smaller increases in Robusta prices along with the drop in the carbonated beverages index checked what might have been a larger increase in the nonalcoholic beverages price index in 1997. With coffee prices continuing to decline since August 1997, the CPI for nonalcoholic beverages is expected to increase 1-3 percent in 1998.

Other foods. Other miscellaneous foods are highly processed and largely affected by changes in the all-items CPI. These products include frozen dinners, pizzas, and precooked frozen meats. Competition among these products and from the away-from-home market should continue to dampen retail price increases for items in this category. In 1997, the CPI for this category increased 3.2 percent and is expected to increase 2-4 percent in 1998.

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