Rise in Food Prices in 1998 & 1999 To Be Lowest Since Early 1990's

Large supplies of meats and a low general inflation rate in 1998 are benefiting and will likely continue to benefit consumers. With 8 months of Consumer Price Index (CPI) data already collected in 1998, the annual average food CPI is 2.1 percent above the first 8 months of 1997. Food prices are forecast to increase only 2 percent in 1998 and 2-2.5 percent in 1999. Such modest increases have not been seen since 1992 and 1993, when food prices increased only 1.2 and 2.2 percent. The general inflation rate for the all-items CPI is forecast to be only 1.7 percent in 1998 and 2.5-3 percent in 1999.

The sluggish export market for higher-price meat products and an end to El Niño's influence on fruit and vegetable prices have also contributed to lower-than-expected retail prices in 1998. Fruits and vegetables, which account for about 15 percent of the at-home component of the food CPI, are expected to increase 4-5 percent in 1998 due to weather-related fresh vegetable price increases, but this increase is lower than originally anticipated because of an earlier-than-expected end to El Niño-related weather patterns.

In the overall food CPI for 1998, fruit and vegetable price increases are mitigated by smaller increases and even decreases in other food categories. Cereals and bakery products, 16 percent of the at-home index, are forecast to increase 2 percent. Nonalcoholic beverages, 11.2 percent of the at-home index, are forecast to fall 0.7 percent in 1998 due to the larger coffee crop. Beef, pork, and poultry prices, which account for 19 percent of the food-at-home index, are forecast to fall about 2 percent.

Food accounts for 15 percent of the all-items CPI, and is among the most volatile of the consumer goods tracked by the Federal Government. Retail food price changes are underpinned by general economic factors and the relative shares of farm and marketing costs. In recent years, food price increases have been small because of the low general inflation rate; the larger share of the food dollar going to away-from-home purchases of food and the continued decline in the farm value share of the retail price for most food items—both of which increase the share of food costs, like wages, transportation, and marketing, that are most influenced by the general economy; and increasing economies of size in the farm sector.

The CPI for food measures both food purchased for preparation at home (at-home component) and purchases of food that is prepared away from home, usually at restaurants or fast-food establishments (away-from-home component). The at-home component of the CPI, which increased 2.6 percent in 1997, is forecast to increase as little as 1.5 percent in 1998 and only an additional 1-2 percent in 1999. The away-from-home component of the CPI, which increased 2.8 percent in 1997, is forecast to increase 2.6 percent in 1998.

Because the away-from-home component includes the costs of food preparation as well as the food items themselves, wages and other business expenses play a larger role in away-from-home prices. Higher wage costs in early 1998, influenced by a tighter than usual labor market, may have caused the away-from-home component to increase more than the 2.6 percent expected based on its steady climb since the minimum wage increases in 1996 and 1997. However, away-from-home food prices were held down by lower raw material and food costs, by competition among restaurants and fast-food establishments, and by Home Meal Replacement (fully or partially prepared foods) or meal solutions offered by supermarkets. In 1999, the away-from-home CPI is expected to increase at about the same rate, between 2.5 and 3 percent.

The smaller increases expected for the at-home food CPI in 1998 and 1999—less than 2 percent—are influenced primarily by agricultural factors rather than by the performance of the general economy. Large supplies of meats and a sluggish export market for higher-price meat products is dampening meat prices; adequate supplies are keeping the prices of fresh fruits and vegetables down; increased sugar production is slowing price growth for sugar and sweets; lower grain prices are affecting the prices of cereals and bakery products; and near-record Brazilian coffee production and strong competition in the soft drink and prepared food industries are keeping down prices for nonalcoholic beverages.

Meats. Total U.S. meat production is expected to increase about 1.5 percent in 1998, following a 2.7-percent increase in 1997. Production is also forecast up slightly again in 1999. Large meat supplies— combined with currency devalua-

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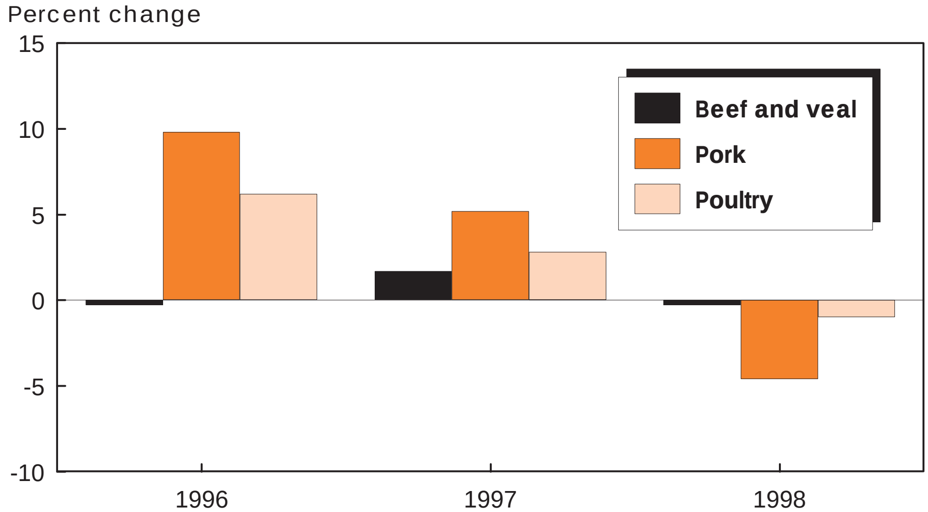
tions around the world, the changing composition of the meat trade, and the need to find alternatives to sagging Asian markets—are challenging U.S. meat exports in global markets, and in some cases, making the U.S. a more attractive market for foreign exporters. Meanwhile, the large supplies and reduced prospects for exports of higher-price meat products in 1998 and 1999 are exerting downward pressure on U.S. livestock and poultry prices.

Beef and veal. Large supplies of competing meat should hold prices steady in 1998, following a 1.7-percent increase in the beef CPI in 1997. After a forecast record beef production of 25.8 billion pounds in 1998, beef production is expected to drop about 7 percent in 1999. Reduced beef production in 1999, reflecting the sharply reduced cattle inventory, will result in higher retail beef prices. The CPI for beef and veal is expected to increase close to 3 percent in 1999, as large supplies of pork and poultry hold down a larger beef and veal price increase.

The retail beef market has grown increasingly competitive as efforts by chicken and pork producers to provide larger cut sizes, improved palatability, convenient packaging, and consistency of product for both white-meat chicken and pork loins make it difficult for beef producers to raise prices. Still, per capita beef consumption on a retail weight basis will be 68 pounds this year, up from 67 pounds last year and the largest since 1989. However, consumption is expected to drop to 63 pounds per capita in 1999, while expected per capita consumption of other meats will reach 150 pounds, another 2-percent gain in share of the meat market.

Pork. Commercial pork production is expected to be about 18.8 billion pounds in 1998, up 9 percent from a year earlier. With plentiful supplies of pork and competing meats throughout 1998, pork retail prices are expected to fall almost 5 percent in 1998, following a 5.2-percent rise in 1997. Although competing beef production is expected to drop sharply next year, continued large supplies of pork and poultry will likely moderate the decline to 2-3 percent in 1999.

Pork To Lead Retail Meat Price Declines in 1998



1998 forecast.
Economic Research Service, USDA

With abundant pork and reduced beef supplies, retailers will likely favor pork over beef for featuring at supermarkets. U.S. per capita pork consumption on a retail-weight basis may reach 52 pounds in 1998, with a record 54 pounds forecast for 1999. Large U.S. pork supplies and lower wholesale prices also boosted 1998 and 1999 export forecasts. The U.S. is expected to export 1.25 billion pounds of pork in 1998, an increase of 19 percent over the previous year. The forecast for 1999 is 1.3 billion pounds. The composition of exports, however, is shifting to lower-valued products.

Poultry. The CPI for poultry may fall up to 1 percent in 1998 and fall slightly or show no change in 1999, following an increase of 2.8 percent in 1997. Broiler production is expected to increase 2 percent in 1998, following a 3.5-percent increase in 1997. Production is forecast to increase 5 percent in 1999, to 28.9 billion pounds. Turkey production is expected to decline in 1999 after 3 years of negative returns for turkey producers, with some turkey production facilities converting to chicken production.

Broiler producers are expected to remain cautious when making production decisions, as there will continue to be very large domestic meat supplies and uncertainty in the export market. U.S. poultry exports to Hong Kong are forecast to rebound in 1999 from the reduced levels of 1998, but they will likely remain below 1997. Poultry producers will face strong competition from U.S. pork exports—pork and poultry exports compete as a prime ingredient in processed products and sausage—and from foreign poultry producers.

Poultry is a cheaper source of meat protein than beef, and growth in poultry consumption has been especially strong in China, Russia, and Mexico in recent years. Even in a developed market such as the U.S., consumers are buying more poultry. Lower prices relative to red meats, the convenience of processed poultry products, and promotions of poultry products in the fast-food industry have all contributed to this trend. The fast food market has been an area of growth for U.S. poultry producers, especially for wings and skinless, boneless breast meat. Per capita broiler consumption on a retail basis will be 72.5 pounds in 1998 and could reach 76 pounds in 1999.

Other meats. The price movements of the highly processed meat items (hot dogs, bologna, sausages) and lamb/mutton that make up this category are influenced by the general inflation rate as well as the cost of the meat inputs. Given lower meat prices and low general inflation, retail prices of these products are expected to show no change in 1998, after a 2.8-percent increase in 1997. Price increases for beef products and a higher expected inflation rate in 1999 should lead to an increase of 2-3 percent in the prices of these products in 1999.

Fish and seafood. Over the last decade, U.S. per capita seafood consumption has remained relatively flat, at around 15 pounds, roughly 2 to 3 pounds less than turkey consumption. During this time, the source of supply has begun to shift away from wild harvest toward aquaculture (*AO* May 1998). Larger imports of shrimp, tilapia, and salmon, along with slower growth in U.S. catfish output, should lead to an increase of 2.8 percent in the fish and seafood retail price index for 1998. In 1999, the fish and seafood CPI is forecast up 3-4 percent.

Eggs. Retail egg prices have fallen this year due to a nearly 3-percent increase in production in 1998. During the summer months, a heat-related increase in production of medium eggs and a resulting temporary shortage of large eggs did not induce any significant retail price increases.

Egg production is expected to continue increasing in 1999, but at a slower rate of 2 percent. The CPI for eggs is expected to be down 3.3 percent in 1998, with another price decrease of 2 percent in 1999. Per capita egg consumption is forecast at 242.9 eggs in 1998 and 244.5 eggs in 1999. Egg exports are expected to reach 243 million dozen in 1999, up 3 percent from 1998's forecast of 232 million dozen. Higher projected shipments to Canada and rebounding exports to Hong Kong are expected to provide most of the increase.

Dairy products. Milk production rose only about 1 percent in the first half of 1998, hampered by poor-quality hay and alfalfa conditions. Declines in milk cow numbers, however, were mitigated by a continued increase in milk per cow. Strong demand for milkfat products such as cheese and ice cream led to higher consumer prices during the spring and summer and an expected 3.5-percent increase for the dairy products CPI in 1998. With milk production forecast to increase 2-3 percent next year, retail prices for dairy products are expected to increase less in 1999, from 0 to 2 percent.

Changes in Food Price Indicators 1997 through 1999

Items	Relative weights[1]		1997	Forecast 1998	Forecast 1999
	—Percent—		—Percent change—		
All items			2.3	1.7	2.5 to 3
All food	100.0		2.6	2.0	2 to 2.5
Food away from home	37.1		2.8	2.6	2.5 to 3
Food at home	62.9	100.0	2.5	1.5	1 to 2
Meats	10.9	17.3	3.0	-2.0	1 to 3
Beef and veal	4.8	7.7	1.7	-0.6	2 to 3
Pork	3.8	6.1	5.2	-4.6	-3 to -2
Other meats	2.2	3.5	2.8	-0.8	2 to 3
Poultry	3.2	5.1	2.8	-0.8	-1 to 1
Fish and seafood	2.2	3.5	2.3	2.8	3 to 4
Eggs	0.8	1.3	-1.5	-3.3	-2 to 0
Dairy products	6.8	10.8	2.4	3.5	0 to 2
Fats and oils	1.9	3.0	0.9	2.6	3 to 4
Fruits and vegetables	9.1	14.5	2.0	4.7	2 to 4
Fresh fruits and vegetables	7.0	11.1	1.7	4.9	2 to 4
Fresh fruits	3.6	5.7	0.8	2.8	2 to 4
Fresh vegetables	3.4	5.4	2.9	8.0	0 to 2
Processed fruits and vegetables	2.1	3.4	2.4	3.8	2 to 4
Sugar and sweets	2.5	3.9	2.9	1.6	1 to 3
Cereals and bakery products	10.0	15.9	2.1	2.0	2 to 4
Nonalcoholic beverages	7.0	11.2	3.7	-0.7	-2 to 0
Other foods	8.5	13.5	3.2	2.8	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.
Sources: Historical data, Bureau of Labor Statistics; forecasts, Economic Research Service.

Economic Research Service, USDA

Fats and oils. The December 1997 BLS revision to the CPI item structure (*AO* April 1998) transferred butter from the dairy products category to the fats and oils category. As a result, the volatile movement of butter prices during the summer caused upward pressure on the CPI for fats and oils, which are expected to increase 2.6 percent in 1998, following a modest rise of 0.9 percent in 1997.

Butter and margarine are now combined into one category, comprising 31 percent of the fats and oils index. The other components of the index—vegetable oils, salad dressings, and peanut butter—are highly processed food items. Their price changes are influenced more by movement in the general inflation rate and U.S. and world supplies of oil products than by farm product input costs. The CPI for fats and oils is expected to increase 3-4 percent in 1999, reflecting expectations for the general inflation rate.

Fresh fruits. Heavy rains in February and hailstorms in late March and early April affected the 1998 production of stone fruits, especially plums and nectarines, in California— a major production region for peaches, plums, and nectarines. Additionally, a 3-day freeze in South Carolina and Georgia during the second week of March brought significant bloom damage to early peach varieties in these key producing States. Smaller peach shipments from the Southeast, coupled with delay in all stone fruit development in California, pushed up retail prices during the early part of the stone fruit season.

However, 1998 fall apple supplies are likely to be up and should keep the increase in the 1998 fruit CPI to 2.8 percent. Weather has been favorable for the Western and Central U.S., particularly in Washington, which produces about half of the Nation's apples, and in Michigan, the largest apple-producing State in the Central region. Apples account for almost 19 percent of the fresh fruit index.

In addition, citrus fruit acreage has expanded as replantings in Florida following the late-1980's freezes have begun to bear fruit. These trees, including oranges

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and grapefruit, will produce increasingly larger crops into the early 2000's. California has also expanded its orange production area. California's oranges are mostly for fresh use, while Florida's oranges are mainly used for juice. Citrus fruits comprise over 21 percent of the fresh fruit index. Bananas account for over 19 percent of the fresh fruit index, and supplies are ample in 1998.

U.S. demand for fresh fruit is expected to continue strong and exports are projected to rise. As a result, the fresh fruit index is expected to increase 2-4 percent in 1999, on top of an increase of 2.8 percent in 1998.

Fresh vegetables. Growing conditions were mixed in 1998 as a result of El Niño-related weather patterns. Torrential rains in Florida during the last quarter of 1997; rain and cold in the desert areas of California, Arizona, and Texas; and an unusual December 1997 freeze in west Mexico reduced fresh vegetable supplies and boosted retail prices early in 1998. Prices in the first half of the year were 14.6 percent higher than a year earlier. U.S. growers also reduced harvested area from a year earlier for some fresh-market vegetables and for potatoes as a result of lower grower prices in 1996 and 1997, contributing to shorter supplies and stronger retail prices.

Subsequent plantings of normal acreage and improved weather during the remainder of the year will mitigate much of that early price rise. However, weather-related delayed harvests are expected to lead to higher prices for potatoes, which cannot be replanted, contributing to an increase in the fresh vegetable CPI of 8 percent in 1998. With normal weather and growing conditions in 1999, supplies should become abundant again, leading to a forecast change in the fresh vegetable CPI for 1999 of no more than 2 percent.

Processed fruits and vegetables. Retail prices for processed fruits and vegetables in 1998 and 1999 are largely determined by the previous year's production and resulting supplies. Vegetable production for processing declined 8 percent in 1997, mostly due to reduced processing tomato output. Contract acreage for the five leading processing vegetables (tomatoes, sweet corn, snap beans, green peas, and cucumbers) was down 3 percent in 1997, but is expected to be up 1 percent in 1998 to 1.4 million acres.

Total supplies of canned vegetables have been down the last 2 years because of lower wholesale prices, which have discouraged processors from increasing contract acres. Although frozen vegetable supplies increased 2 percent in 1997, the resulting larger stocks led to lower wholesale prices for frozen vegetables in the first half of 1998. Although processed vegetable supplies were less in 1998, abundant supplies of processed fruits kept the CPI increase for processed fruits and vegetables to 3.8 percent for 1998. The expected increase for 1999 is 2-4 percent.

Sugar and sweets. Domestic sugar production was up 9 percent in 1997/98 because of acreage increases for sugarbeets. 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 increased production, along with a lower general inflation rate, held the 1998 sugar and sweets CPI to a 1.6-percent increase. Continued growth in sugar deliveries to the expanding bakery and breakfast cereal sector should offset or exceed the 1998/99 sugar production increase of 1 percent, leading to a 1999 CPI increase for sugar and sweets of 1-3 percent.

Cereals and bakery products. This food category accounts for a large portion of the at-home food CPI—almost 16 percent. With grain prices lower this year and inflation-related processing costs at low levels, the CPI for cereals and bakery products increased only 2 percent in 1998. Most of the costs—more than 90 percent in most cases—to produce cereal and bakery products are for processing and marketing, making grain and other farm ingredients a minor cost consideration. Competition for market share among the leading breakfast cereal manufacturers led to decreases in the cereal CPI in 1996 and 1997, with a small increase of 1 percent expected in 1998. While competition among producers and consumer demand for bakery products is expected to continue, the 1999 CPI is forecast to increase 2-4 percent due to higher inflation next year.

Nonalcoholic beverages. Coffee and carbonated beverages are the two major components of this category, accounting for 28 and 38 percent of the nonalcoholic beverage index. Competition in the soft drink industry resulting in lower consumer prices continued throughout 1998, and lower coffee prices during the last half of 1998 are due to a projected near-record coffee crop in Brazil.

The largest producer of Arabica coffee beans, Brazil's annual production has alternated between good and bad years since 1994. Coffee trees have finally recovered from the effects of a freeze in 1994, and the current crop has benefited from excellent weather for growth and maturing of the beans. The current large Brazilian crop is forcing other coffee-producing countries to cut prices, possibly leading to lower U.S. retail prices for coffee next year. In the U.S. market, price and country of origin are important factors for coffee importers, as coffee consumers have shifted toward higher-quality coffee.

With retail coffee prices on the decline and soft drink prices lower throughout this year, the CPI for nonalcoholic beverages should fall slightly in 1998 and remain unchanged in 1999.

Other foods. Items in this category are highly processed and primarily affected by changes in the all-items CPI. These products include soups, frozen dinners, pizzas, snacks, baby food, and precooked frozen meats. Although demand for prepared products continues to increase, competition among these products and from the away-from-home food market should lead to an increase in the CPI for these foods of 2.8 percent in 1998. Continued growth in this category next year would indicate a CPI increase of 2-4 percent in 1999.

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