

# Food Inflation May Rise to 3% to 4% in 2013 After Drought

*By Alan Bjerga -*

U.S. consumers may pay 3 percent to 4 percent more for food next year, as the effects of the country's worst drought since the 1950s work their way onto supermarket shelves, the Department of Agriculture said in its first forecast for 2013.

Beef may rise as much as 5 percent in response to tight supplies of corn, which is used to feed cattle, the USDA said today in a [report](#) on its website. The price of the grain, the country's biggest crop, has surged more than 50 percent since June 15. Food prices will rise 2.5 percent to 3.5 percent this year, the agency said, leaving its 2012 estimate unchanged.

Corn and soybean futures both reached record highs this week on the Chicago Board of Trade, and wheat touched its highest since 2008 as the dry conditions worsened in the Midwest and Great Plains. The drought that prompted the USDA to declare natural disasters in almost 1,300 counties in 29 states -- about a third of the country's total -- may lead to the smallest corn harvest since 2006, Doan Advisory Services Co. said July 23.

"The transmission of commodity price changes into retail prices typically takes several months to occur, and most of the impact of the drought is expected to be realized in 2013," said Richard Volpe, the USDA's food economist, wrote in [a note](#) accompanying the forecast.

## Purchasing Power

Higher commodity prices may affect everything from meat purchased by [McDonald's Corp. \(MCD\)](#) to the grain bought by [General Mills Inc. \(GIS\)](#) to the sweeteners used by [Coca-Cola Co. \(KO\)](#). More expensive food has already eroded purchasing power at Save-A-Lot stores operated by [SuperValu Inc. \(SVU\)](#), the third-biggest U.S. grocery chain, Craig Herkert, the chief executive officer of the [Eden Prairie](#), Minnesota-based company, said in a conference call with analysts July 11.

Still, higher crop prices may not immediately be reflected on store shelves. McDonald's, the world's largest restaurant chain, has lowered its estimated 2012 increase in grocery costs to 3.5 percent to 4.5 percent from 4.5 percent to 5.5 percent, Peter J. Bensen, the chief financial officer of [Oak Brook](#), Illinois-based McDonald's, said on a conference call with analysts July 23. The company bought grain and other commodities before the drought-induced rally, locking in lower prices.

## 'Fairly Tame'

"Food-price inflation is actually going to be fairly tame for the rest of the year," said Bob Young, chief economist for the [American Farm Bureau Federation](#). Higher fruit and vegetable costs caused by frosts early in the year have already been built into pricing, and increased costs for corn and soybeans, used in livestock rations, may not affect the price of many meat products quickly because of the life cycles of the animals being fed, he said.

The earliest price increases may be seen in poultry meat and eggs, which come from birds with shorter lives that are raised almost entirely on corn, said Bill Lapp, a former chief economist for [ConAgra Foods Inc.](#)

[\(CAG\)](#) and the president of Advanced Economic Solutions in Omaha, [Nebraska](#). The USDA today said egg prices will rise as much as 4 percent in 2012, up from its projection for this year of 1 percent to 2 percent.

## Meat Forecast

Dairy, pork and beef, all produced by animals that are on feed longer, will follow, Lapp said before today's report, raising food inflation next year to 4.5 percent, about 2 percentage points more than it would otherwise have been. The effect will carry over into 2014, adding half a percentage point to the previously expected jump in prices, he said.

Beef may even see a short-term decline, Lapp said, as meatpackers slaughter animals earlier to avoid the higher corn costs, temporarily increasing supply. The USDA today lowered its forecast for increases in beef prices for 2012 half a percentage point to 3.5 percent to 4.5 percent.

Still, the reduced beef supply may increase pressure on prices in the longer term, since the U.S. cattle herd, which on July 1 was at its lowest for the date since 1973, may shrink further, he said.

The drought in the U.S., the biggest corn exporter, may push up food prices worldwide, possibly discouraging central banks from easing monetary policy, Merrill Lynch Health Management said yesterday in a report. In the U.S., because nutrition accounts for only about a seventh of the [Consumer Price Index](#), the impact of rising costs on overall inflation may be small, according to Paul Dales, senior U.S. economist for London-based Capital Economics Ltd.

## Lag Time

"It can take up to nine months for rises in agricultural commodity prices to filter through into higher food prices in the stores," Dales wrote yesterday in a note to investors. Dales also said food inflation may rise to about 4.5 percent.

"The upshot is that the recent drought will not be a disaster for the American economy as a whole," he wrote. "Coming at a time when the economic recovery is faltering, even a small loss of output in a small sector is a further hindrance."

Retail-food costs rose 3.7 percent in 2011, according to the USDA. Consumer prices have increased 1 percent so far this year, the government said.