Food Inflation Everywhere, But Not A Bit In CPI (Yet)

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Reported **U.S. food inflation has been a paltry 1.6% over the last 12 months, one of the lowest growth rates in food & beverage CPI since late 2010**. However, ConvergEx's Nick Colas notes that the severe drought in the Midwest over the summer of 2012 will likely drive up food costs this year 3-4% across the board, by the USDA's estimates. These headline numbers, however, **don't accurately reflect the prices of the real "basket of goods"** that we bring to the checkout counter every week at the grocery store. Consequently, Colas warns, the CPI report doesn't necessarily mirror the increase in our grocery bill. Nor does it take into account different food choices (e.g. healthy vs. junk food), farm prices, or demographics, all of which the USDA publishes separately. The actual, visible inflation at the checkout counter may lead the American consumer to think – perhaps inaccurately – that overall CPI is rising or falling at a similar pace. For a more detailed, accurate reflection of food CPI, then, we have to aggregate all of these indicators to see how they compare to overall CPI. In short, inflationary expectations may well be set to rise dramatically in 2013: **"shopping cart inflation" was upwards of 1.3% last month, almost double the 0.7% overall CPI.**

Via Nick Colas, ConvergEx,

I have the pleasure of being the primary grocery shopper and cook when I return home to New Jersey to visit my parents, a "privilege" my mother happily bestows upon me when I arrive. Both of my parents recently became vegans – with the rare exception of pizza, of course – in an effort to improve their health and cut the risk for future disease. While I can attest to the fact that the vegan lifestyle has vastly improved both, unfortunately I cannot say the same for their wallets. When we made the switch from steak to tofu and from hamburgers to stir-fries, the weekly grocery bill was suddenly higher. Turns out the "vegan" foods – mainly fruits, veggies, grains, and beans – add up much faster than lunchmeat and frozen entrees.

In hindsight, the higher grocery bill shouldn't have come as a surprise: prices are higher, and increase faster, in certain foods rather than others. The expected results from the drought last summer are only one example: corn, poultry, and produce prices are expected to surge as the corn shortage comes full circle. The USDA's food CPI forecast for 2013, which you can find here, predicts a 3-4% rise in its basket of goods in 2013, with dairy product and fresh fruit & vegetable prices rising more than 4%. These foods supposedly make up 13.3% of the USDA's "basket" (in relative importance) for the year.

Unfortunately, these weightings don't seem to accurately represent the real world baskets Americans bring to the checkout at their local supermarkets. The top 10 purchased items in US food stores, according to various surveys, are (1) milk, (2) bread, (3) eggs, (4) beef, (5) chicken, (6) cereal, (7) salty snacks, (8) lettuce, (9) cheese, and (10) non-alcoholic beverages (juice and soda). While the USDA reports only 0.1% food inflation (seasonally-adjusted) for February 2013, these top items actually rose an average of 1.3% over last month. It would seem, then, that our shopping carts are getting more expensive than the headlines numbers might indicate. If, as these surveys suggest, we purchase items growing faster in price more often than those that decline or stagnate, these foods could have a disproportionate – and in this case, inflationary – impact on what we expect overall inflation to be. This is what economists call, unsurprisingly, "Inflationary expectations" and everyone from Fed Chairman Bernanke on down to the most junior staffer at a regional Fed worry intensely over these popular perceptions of future inflation.

We perused the USDA CPI data to find out which food (or foods) is costing us more, and which might help us save a

few bucks. Healthy eaters beware: the data is not on your side.

Lettuce and apples have risen the most in price compared to February 2012, up 24.5% and 11.1%, respectively. Both items are, admittedly, out of season in February; but remember, these are like-month comparisons. The rising cost of lettuce in particular may hurt the American consumer, as it is one of the most frequently purchased items. Lean meats have also grown much more in price than their more "fattening" counterparts: chicken is up 5.0% over last year and turkey 5.1%, while pork is down -1.5% and ham up only 1.0%.

Lettuce, hot dogs and fresh fruit grew the most in price from January to February 2013, up 6.4% on average.

Potatoes, sweeteners, and bread products, on the other hand, are less expensive than they were just last year, down an average of -4.6%. Lamb and mutton products are the single cheapest item in comparison to last February, down -16.6%; coffee is also surprisingly lower, down -4.1%. The products that fill out the less-expensive group, however, are not necessarily what you might consider "healthy": butter, sugar, and fats & oils, are all among the top "losers" in price.

Compared to the month prior, tomatoes, frozen fish, and peanut butter have declined the most in price, down an average of -3.8%.

It may also cost you to be "health-conscious" when choosing different iterations of a certain product, according to the BLS's CPI data. Wheat bread, for example, rises in price much faster than white bread, and buying whole milk is becoming more expensive than less-fat versions. Fresh produce is constantly climbing in price (especially out-of-season fruits and veggies), while frozen and canned versions are dropping in cost. Unfortunately, health-conscious is not akin to price-conscious.

While food away from home typically climbs at a faster rate than food at home (+2.3% over last year vs. 1.6% for at-home), the USDA predicts that home-cooked food will actually grow faster in 2013: 3-4% vs. 2.5-3.5%. Fresh produce and dairy products are expected to be the most expensive in 2013 compared to last year, up 3.5%-4.5%. Somewhat surprisingly, though, poultry prices are not expected to grow more than the market basket as a whole, despite worries of a surge thanks to the corn shortage.

Finally, according to the USDA's farm price spread reports, retail prices at grocery stores in 2012 were well on their way back to pre-recession highs in 2011 (the latest data available). By this unwelcome measure the U.S. economy has clearly "recovered" quite well.
A little information about our food consumption habits might be able to tell us where our grocery bills are headed as well. The USDA conducted a National Health and Nutrition Examination Survey in 2002, and has updated figures on food availability and consumption each year since: the latest data available was released in September 2012. Consumption data, which is parceled out by several demographic parameters, is the most useful as somewhat of an alternative indicator for our activity at the grocery store. Our main findings were not what we expected, to say the least:

Poundage-wise, Americans take in the majority of our food in fruits and vegetables, followed closely by dairy products. The single most-consumed item by weight is milk; oranges come second. This data point is surprising, given the stories of declining milk consumption, like this one from the WSJ. It is also notable considering neither of these two items is one of the top purchased items at grocery stores.

The biggest food consumers, based on poundage of food eaten per year, are Caucasian, college-educated, high-

income male adults between the ages of 20 and 39 who maintain a healthy weight. According to the data, high-income households (300% above the poverty line) consume 13% more pounds of food each year; males eat 24% more than females; and college-educated persons eat 22% more than those with less than a high school diploma. Those identifying as Hispanic tend to eat the most at home, while Caucasians eat the most away from home.

Most surprisingly, persons with a "healthy weight" eat 7% more pounds of food per year than obese persons. The key here, as you might expect, is substance: obese persons eat the least fruit and more meat than overweight or healthy-weight people. Interestingly, though, they come up to par on veggies, fats & oils, and grains.

These observations, combined with the data from the USDA's CPI, point to one simple conclusion: we're all going to feel (and might already be feeling) the pinch at the grocery store, even if we don't elsewhere. Some of us, according to the USDA data, may feel it more than others: those with male children between the ages of 2-11, for example, might expect to spend a bit more on produce, as these kids are the single biggest consumers of those quickly inflating apples in the country. College-educated women between the ages of 40-59, meanwhile, might find themselves eating less salad: the biggest consumers of lettuce may not enjoy a 25% increase in price.

All of this analysis ultimately comes back around to that econo-geeky topic of "Inflationary expectations." Though food CPI is certainly the most tangible inflation indicator to most Americans, it is important to know it is not the only one; there's a reason the BLS prints an "all items less food" number. That's not to say it should be ignored, of course. It wouldn't do to overlook price increases in the commodities that take up a full 15% of our income, on average. We just may need to extrapolate it from how we view inflation overall. And if there is a real bout of food inflation brewing – with some major demographics feeling a distinct pinch – **that may well be**

enough to change the level of consumers' expectations for future price increase in and out of the grocery store.