Make Informed Decisions
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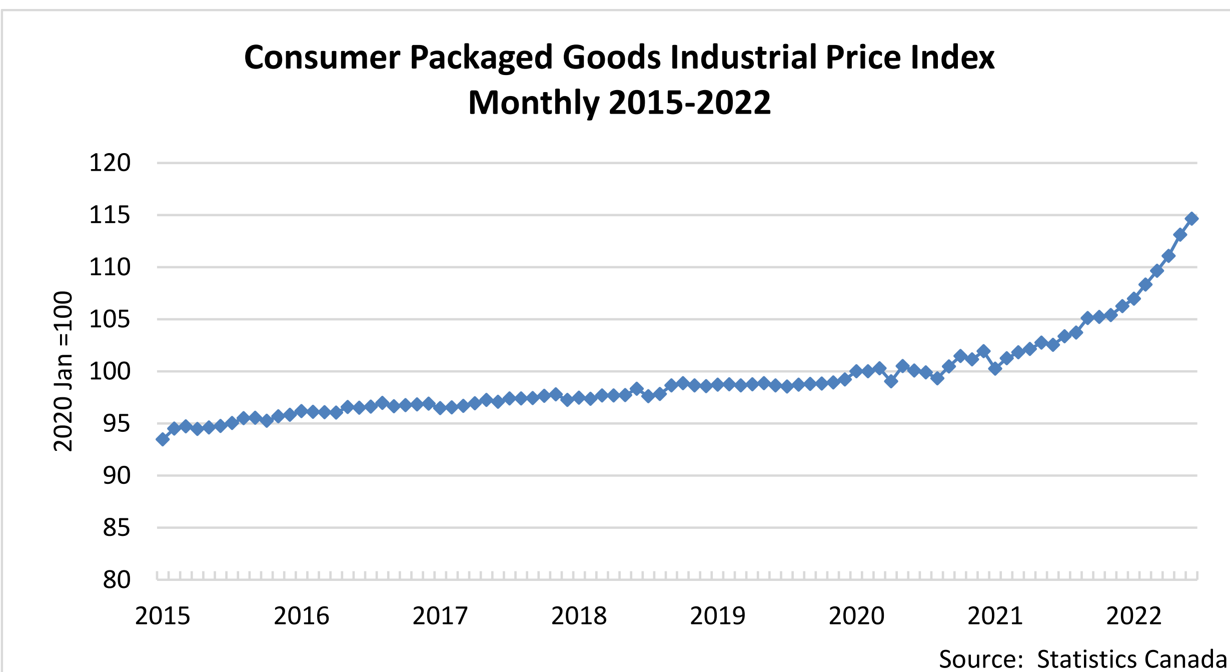
The Cost-Price Disconnect

The Statistics Canada Industrial Product Price Index (IPPI) measures price changes for commodities sold by manufacturers operating in Canada. The prices collected are for goods sold at the factory gate. They exclude all indirect taxes, such as sales taxes and tariffs. They also exclude any transportation service and any distribution services performed by the retail or wholesale trade industries.

The index measures the movement in prices for manufactured goods produced in Canada, destined for domestic or export consumption. Fees, discounts, and penalties will be included in the index where the manufacturer considers them to be representative.

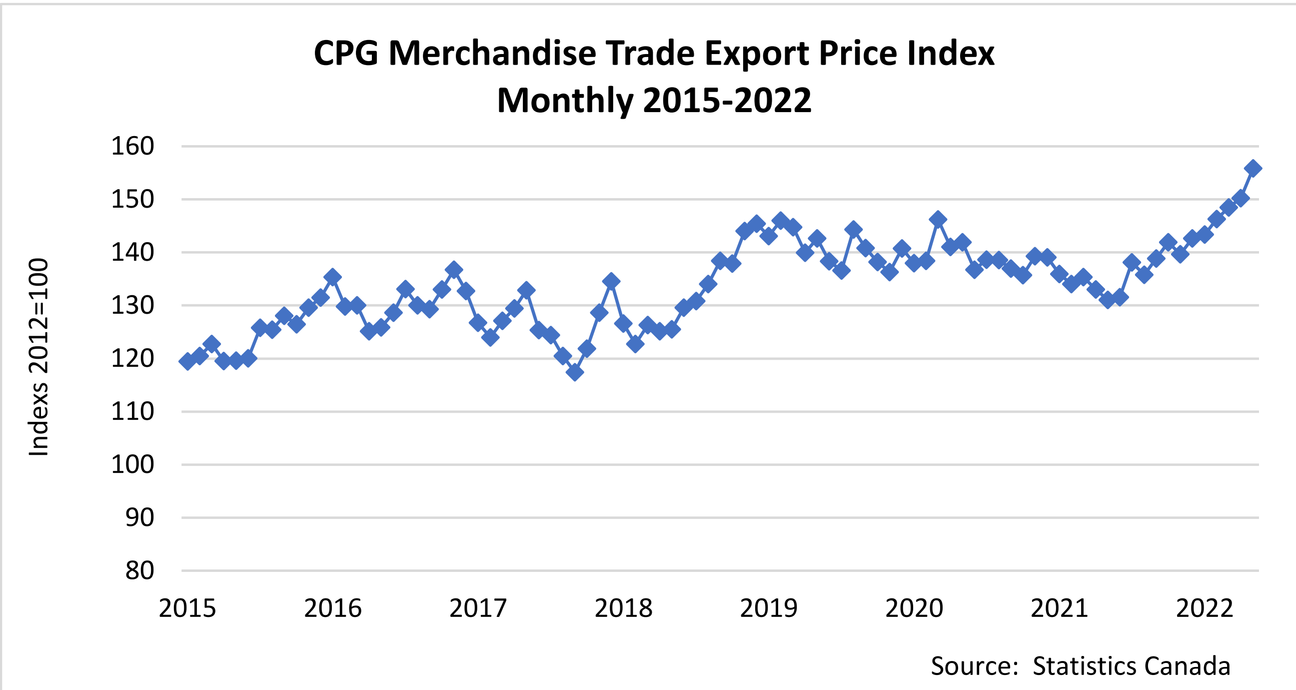
Docile to Unyielding

From the beginning of 2015 through the beginning of 2020 the Industrial Product Price Index calculation for consumer-packaged food goods (CPG), increased by 7%. Going back from 2010 to 2020, the IPPI for CPG increased 17%. Meanwhile, from the beginning of 2020 to June 2022 the CPG IPPI increased 15%. The June year over year CPG IPPI increased by 11.8%. The essential message is that the price increases passed from Canadian CPG manufacturers to grocers have been very docile up until 2021. From that point the increases have been opposite of docile: unyielding.



As noted in the definition above, the IPPI includes both domestic and export sales. In addition to the total IPPI, StatsCan also tabulates and reports an export sales price index. That can be seen as a subset of the total IPPI.

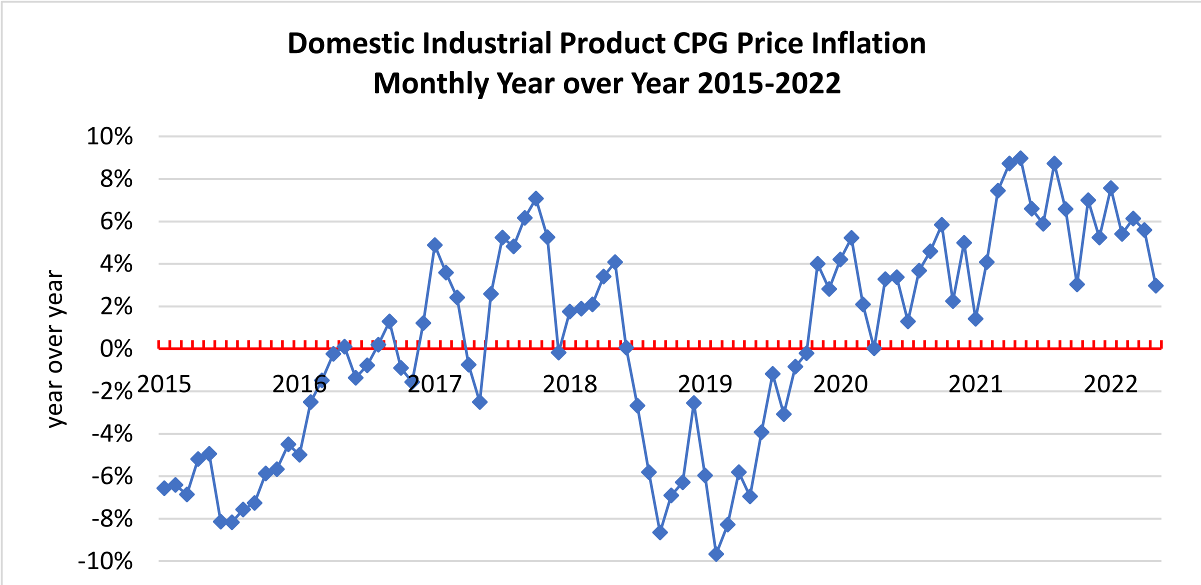
As shown on the graph below, export pricing for CPG manufacturers in Canada has been more volatile than the overall IPPI for both domestic and export pricing. That makes sense given currency fluctuations and possibly less stable export versus domestic marketing relationships.



From the beginning of 2015 to the beginning of 2020, the export index for CPG increased by 15%. From the beginning of 2020 to May 2022 (latest), the index increased by 13%. The year over year increase from May 2022 to May 2021 was up 18.9%. The year over year export increase far exceeded the year over year increase in the total CPG IPPI.

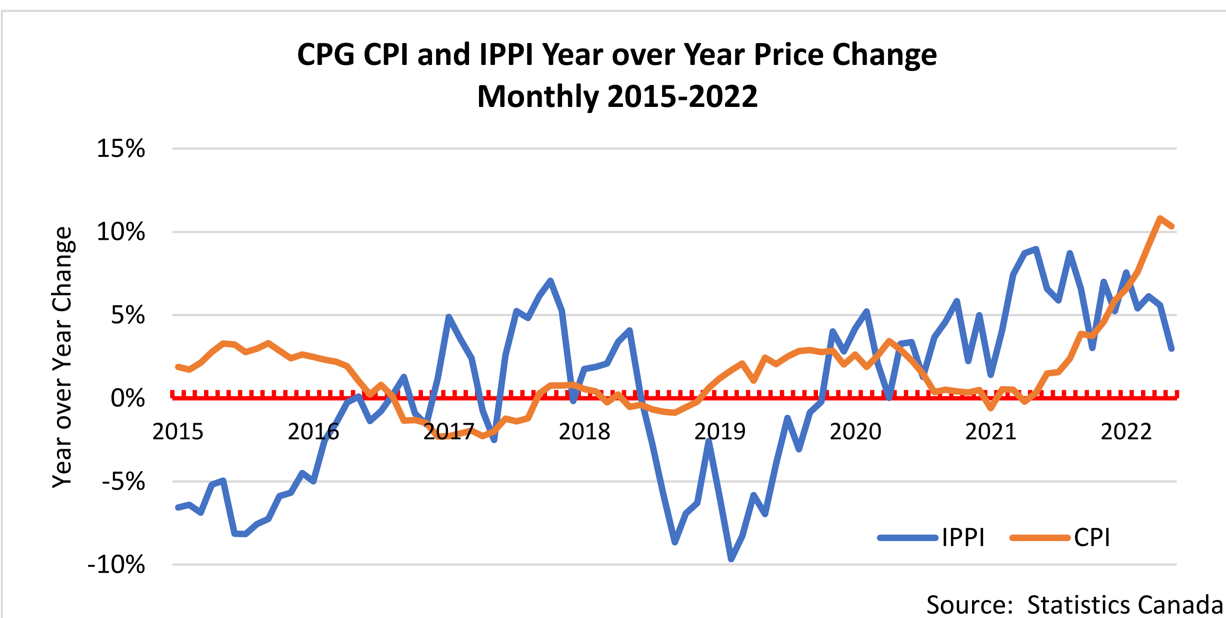
Domestic CPG Manufacturer Price Increases

StatsCan does not report an IPPI for domestic sales only. Nevertheless, based on the total IPPI in combination with the export inflation performance, the domestic price movement can be calculated. Since 2015 domestic Canadian CPG manufacturers have experienced two periods of price deflation in 2015/16 and 2018/19 in the domestic market. From 2020 through 2022, the CPG manufacturers in Canada have seen a prolonged period of price increases in the domestic market.



Disconnect Between Costs and Prices at Retail

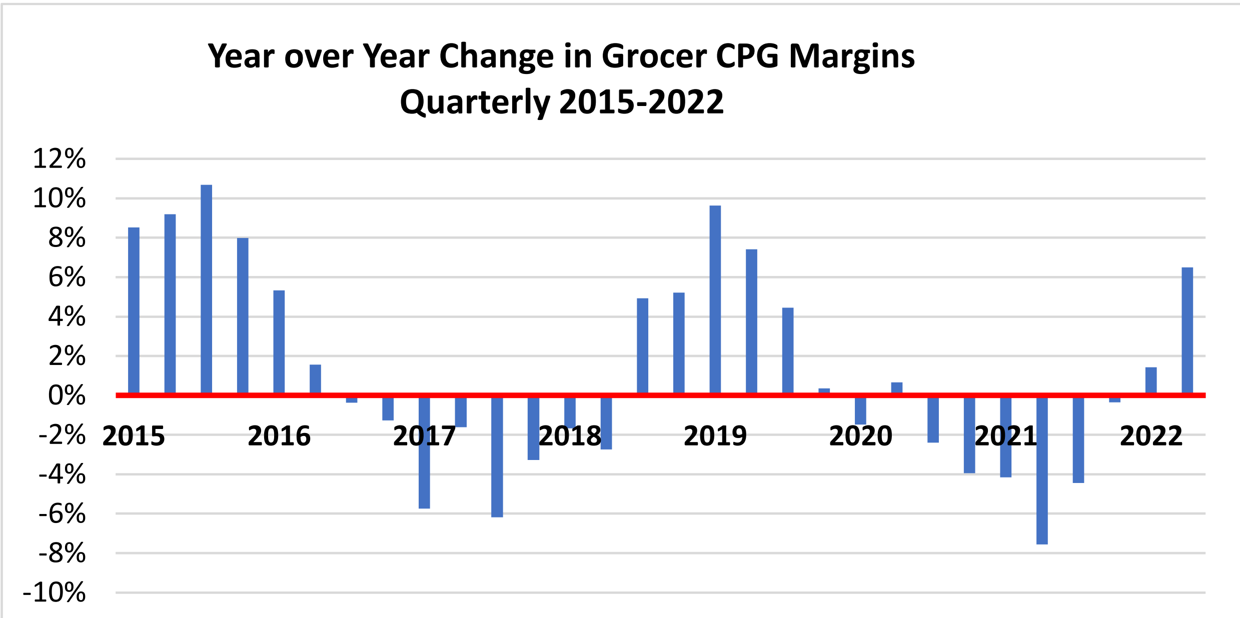
Making a connection between the IPPI at the manufacturer-retailer level and the CPI at the consumer level is not straight forward. There is little or no statistical correlation between the rate of inflation for the consumer-packaged goods IPPI and the CPI rates of inflation. That is, from a statistical perspective, the increase or decrease in manufacturer CPG prices do not have a direct causal impact on the retail CPG prices for consumers. With that said, it would be naïve to assert that the significant CPG costing increases at the manufacturer-grocer interchange since 2020, has not had a direct connection to the increase in consumer prices (see graph below).



Since 2020 the inflation rate of the domestic IPPI for CPG has generally exceeded the CPG CPI inflation. It is only since 2022 that the CPI has notably exceeded the IPPI for CPG. In other words, for much of the lockdown period, the grocer's price increases look to have lagged those of the manufacturer for domestic CPG.

Margin Impact

Based on the 2020-2022 year over year changes in grocer CPG costs versus the changes in consumer pricing, it appears that grocers are beginning to gain margin on the cost of those goods. That 2022 gain on the cost of the CPG sold, is after a near continual decline in margins over the 2020 to 2021 period.



Why it Matters

There is a disconnect between the CPG costs of goods sold and the consumer price of those products. This is not to say that costs do not drive price, eventually. It does say, however, that merchandising and competitive strategy also have a major role. Sometimes to the benefit of margins and sometimes not.

A version of this note first appeared in the June edition of Grocery Trade Report. If you are interest in a trial subscription, email, kevin@kevingrier.com

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July 2022