



## **Competition Leads to Food Price Deflation**

*By: Kevin Grier, Senior Market Analyst*

*George Morris Centre*

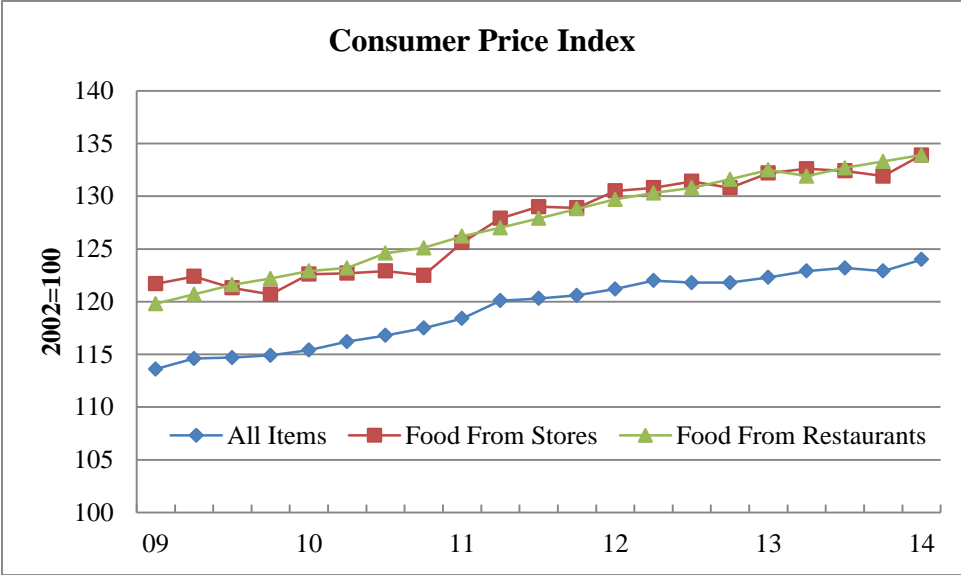
*May 2014*

### **Introduction**

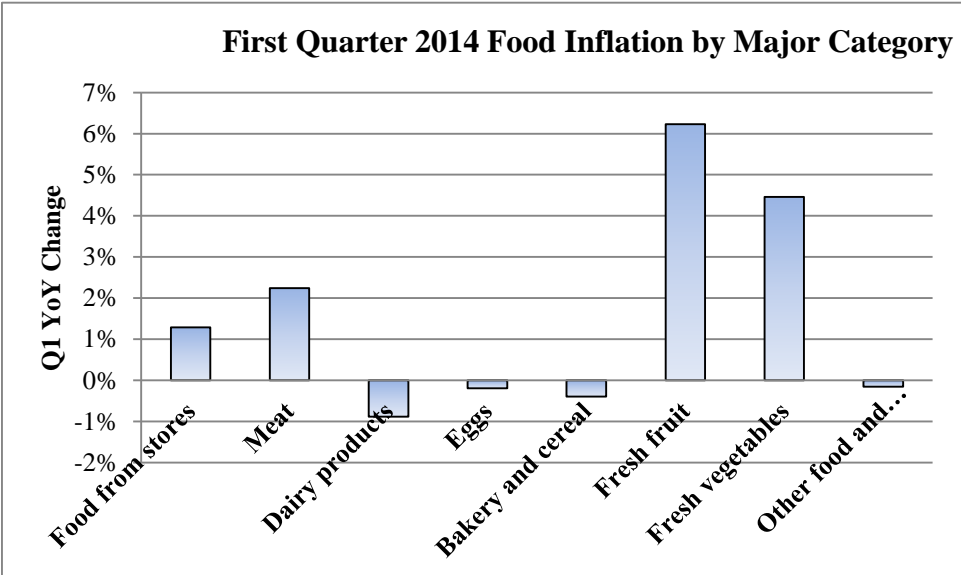
There has been considerable attention in the media about the sharp pricing increases in pork and beef prices. The pork and beef price increases are related to significant reductions in North American supplies. There has also been a focus on the drought in California and its impact on fruit and vegetable prices. Each of these events are very real and have had significant impact on the prices Canadians pay at the cash register at the grocery store. With that noted, though, overall food price inflation in Canada has only increased by a modest 1% in the first quarter of this year. That means that while some prices have been up sharply, others have actually declined. This paper looks at some of the surprising pricing dynamics at the grocery store in the first quarter.

### **Modest Increases in Food Prices**

First quarter Consumer Price Index data shows that the increase in the price of food purchased from stores is lagging behind the overall rate of inflation. According to Statistics Canada data, the overall rate of inflation increased in the first quarter by 1.4%, compared to the first quarter of 2013. The price of food purchased from stores increased by 1.3% in the quarter compared to last year, while restaurant prices increased by 1.1% over the same period. Over the past five years through the first quarter of 2014, all items have increased by 9% compared to 10% for food from stores.



Looking within the food numbers to the more specific commodities shows that the Q1 food inflation was driven largely by fresh meat and produce. Fresh fruit and vegetables increased by about 4-6% in the first quarter this year, compared to 2013. Meat increased by just over 2%. The price increases in those items would have been driven by supply challenges mostly, and by the immediate cost impact of the depreciated Canadian dollar.

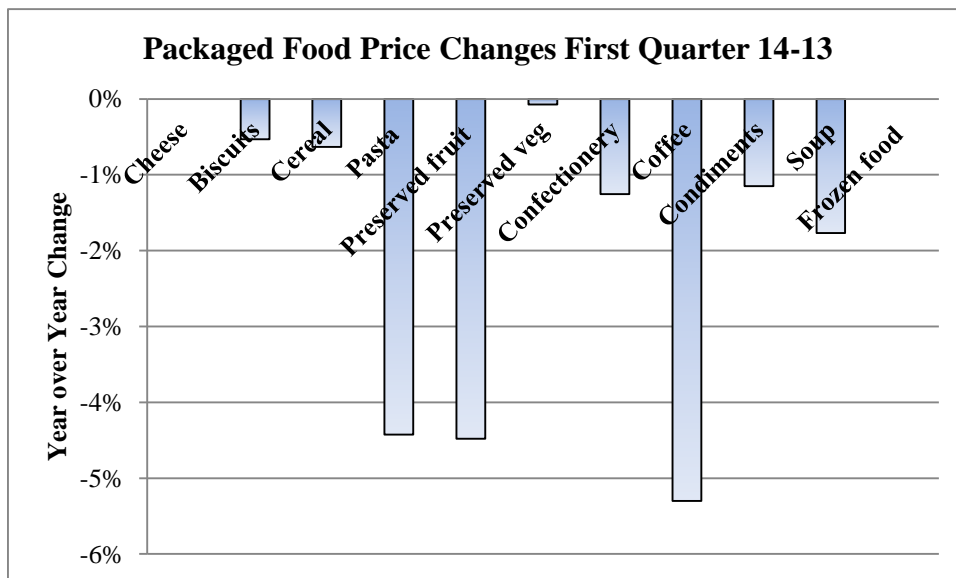


In other words, whatever little inflation there is at the grocery level it is being driven by fresh meat and produce. Grocers have been taking an immediate hit by taking on higher costs due to reduced supply and the depreciated C\$. As a result, they have been gradually pushing the shelf prices higher.

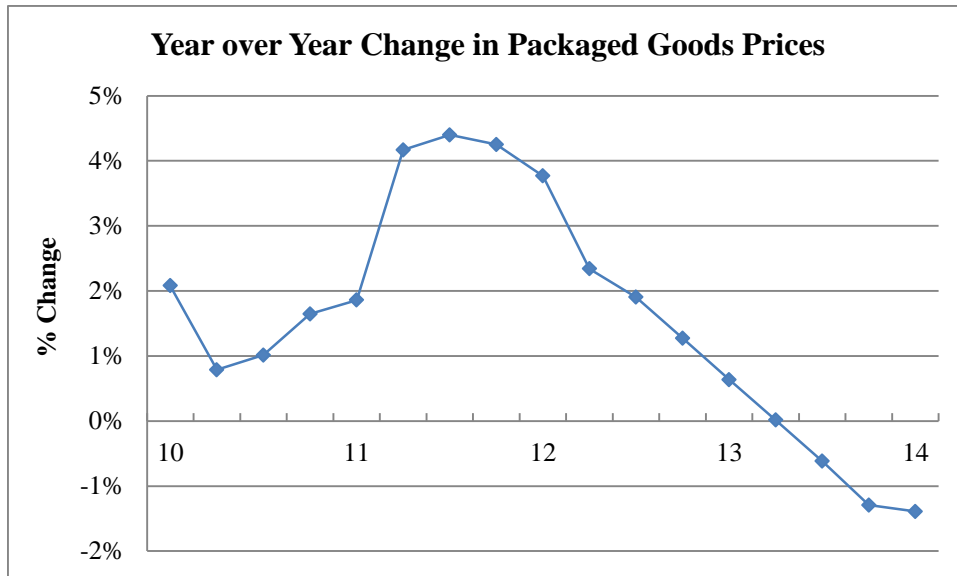
## Pricing Deflation for Packaged Goods!

What is, perhaps, more interesting is the fact that it is only the fresh commodity-based items that are driving pricing. The other broad-based categories, surprisingly including eggs and dairy, are showing year over year declines.

Looking deeper into the packaged goods pricing reveals that grocers have been enduring pricing *deflation* in 2014. From cheese to pasta, cereal, canned goods and frozen foods, prices have declined materially in the first quarter of 2014 compared to last year.



As a last point with regard to this development, the year over year decline is a relatively new occurrence. The year over year quarterly decline in packaged goods pricing as reported by StatsCan started in the third quarter of 2013. With that noted, the order of magnitude of the decline has been steadily widening.

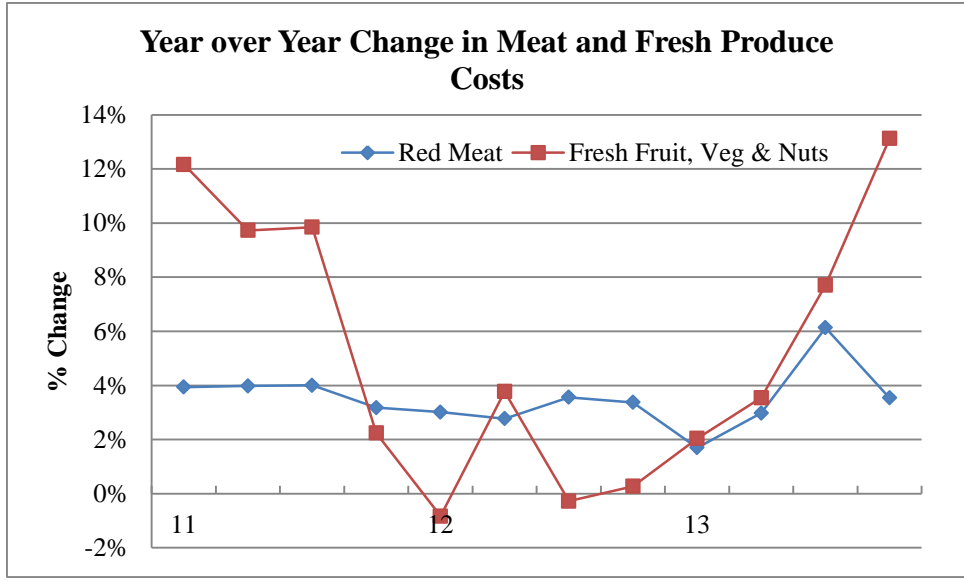


In summary, on the price or revenue side, modest inflation at retail is being entirely driven by meat and produce price increases. The middle of the store and even the dairy aisle is seeing price deflation at grocery. Those developments then turn the attention more closely to the cost side of the grocer equation.

### **Cost Performance**

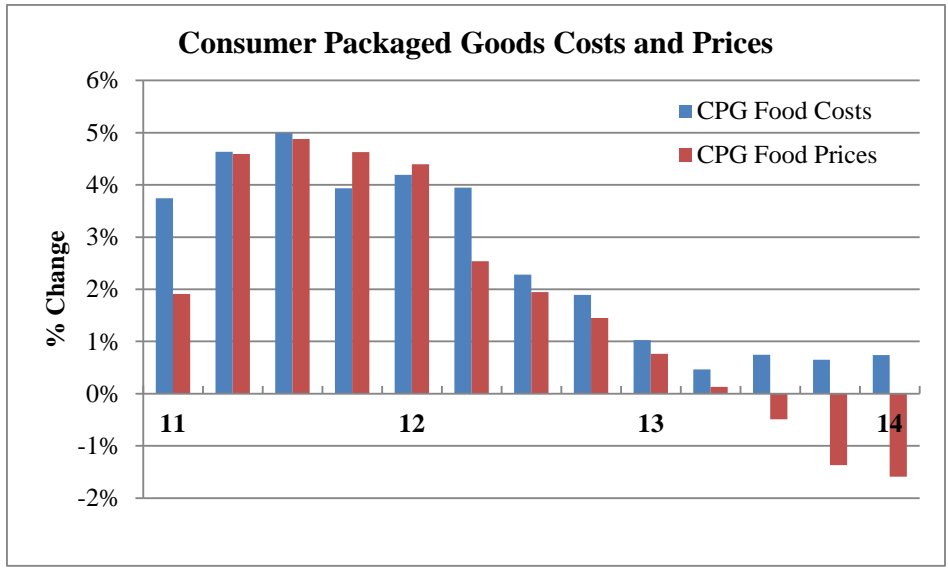
First with regard to meat, it is noted that in the last quarter of 2013, meat product costs to grocers increased about 4%, compared to the last quarter of 2012. Grocers would have been trying to pass those costs along in the first quarter of 2014, but succeeded in gaining only a 2% increase in meat prices, according to StatsCan. With regard to produce, fourth quarter 2013 produce costs increased in Canada by 12-14%. In the first quarter of 2014 grocers only succeeded in increasing produce prices by 4-6%. In other words, grocers had not been able to pass along all of the 2013 fourth quarter cost increases for meat and produce, as of the first quarter of 2014.

Furthermore, in the first quarter of 2014, meat prices at the packer-grocer level have increased by about 20% for beef and over 50% for pork. Fresh produce pricing has increased by about 30% in the first quarter. Both the first quarter meat and produce costs are supply driven increases, which grocers have simply had to absorb. Grocers will be trying to force produce and meat pricing higher in the second and third quarters in order to recoup these increases.



**The Squeeze is On**

The point of note is, while grocery inflation is being driven by meat and produce, the reality is that the inflation is far behind the costs that the grocer has to pay to supply these products. The other key point, of course, is that there is deflation occurring at the packaged goods level. While there is deflation at the packaged goods level at retail, the cost increases, while moderating, are still positive. Packaged goods cost increases have moderated over the past year or two from about 4-5% down to less than one percent. Grocers are clearly losing or being squeezed on those transactions as well.



The bottom line is that the pricing data for the first quarter and the latter part of last year are simply a reflection of the competitive situation facing grocers. There is no other logical explanation for packaged goods pricing declines, or the inability to pass along fresh product price increases.

*A version of this report first appeared in the April edition of the George Morris Centre publication, Grocery Trade Review. For a free two month trial to the report, please email [kevin@georgemorris.org](mailto:kevin@georgemorris.org)*

The George Morris Centre is Canada's leading economic agri-food research organization. We offer research, consulting and custom education to the private sector, government, producer groups and organizations that have a commercial interest in agriculture, food and related policies. We are the go-to source for trustworthy and unbiased information that helps leaders make informed decisions.