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The Impact of Higher Commodity Prices on Food Price Inflation

- **The US consumer has faced little or no food inflation pressures since the early 80s**
 - **Food inflation as measured by the CPI averaged 2.9% between 1982 and 2006, and just 2.3% during 1997-2006**
- **But food inflation began to accelerate in the past year, with the CPI-Food rose by 4.9% during 2007**
- **We appear to entering a period of time for food inflation very similar to the 70s**
 - **During the 70s, the average price of most food input prices jumped to a new plateau during the early 70s – including corn jumping from its post-WWII average of \$1.24 to a new plateau near \$2.50**
 - **The CPI-Food rose by an average of nearly 9% between 1972 and 1981 -- this includes an increase of 20% during 1973 and 12% during 1974**
- **Food inflation has been benign since 1982, as there have been commodity price spikes but no sustained increase in commodity inputs (as we experienced during the 70s)**
 - **The response of food industry participants to short term prices spikes over the past 25 years has been to protect market share at the expense of margins**
 - **And thus since 1982 there is little correlation between food inflation and these short-term price spikes**
 - **But with a sustained increase in prices (as we are currently experiencing), food inflation is no longer expected to remain in check, and food industry participants will raise prices in the coming years to maintain margins**
- **We have experienced a sharp, and I believe sustained rise in commodity prices in recent years to a new plateau**
 - **Crude oil over \$90, corn/soybean/wheat prices doubling**
 - **There have been several key drivers of this sustained rise in commodity prices, including strong global economic growth,**

China's emergence as a major contributor to global economic growth, a weak US dollar, and the use of food to produce fuel

- **World coarse grain demand has risen sharply in recent years --*We either have to slow demand or increase the number of acres***
- **During the next 5 years we will see higher food inflation, as the impact of higher commodity prices will be passed on to consumers**
 - **The CPI-Food is forecast to rise at an average annual rate of 7.5% during 2008-2012**
 - **This contrasts sharply with the opinion of others, who suggest no impact of higher commodity prices upon food inflation**
- **Anecdotal Evidence: What Food Industry Purchasing Executives Are Saying About Food Inflation – In a recent AES survey of purchasing executives, opinions about food inflation revealed some strong and consistent beliefs about what to expect in 2008 and beyond:**
 - **More than 90% believe 2007 was the most challenging year they have faced, and more than 90% believe 2008 will be equally or more challenging than 2007**
 - **More than 90% believe the increase in food costs we have seen will be sustained over time**
 - **Around 75% indicate they have begun to reflect higher costs in consumer prices, but more increases are forthcoming in the next year**
 - **Among the causes of the increased food input prices, over 70% mentioned global economic growth and a weak US dollar, but over 90% indicated ethanol was a primary driver of the rise in food input prices**