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Food prices, substitutability, and shoppers

October 15, 2012; 22:56 pm by Bill Bishop (/blog-2?filter_type%3D950020%26filter%3D1321)

Food prices strongly affect the growth of the overall market, as well as the growth available to individual companies. We turned to Brian Todd, President of The Food Institute (http://www.foodinstitute.com/aboutus.cfm) , to get the most up-to-date facts on food prices as well as expert foresight. Brian is a long-time food professional and is frequently quoted on the outlook for food prices and other issues related to food from farm to fork.

BMC: How long has The Food Institute tracked food pricing, and are there any lessons learned that you can share?

Todd: From our New Jersey headquarters, the non-profit Food Institute has been tracking food prices since 1928, so we've seen it all – inflation, deflation, and almost everything in between. Over time, we've learned from our 2,000 or so members that the toughest period for retailers occurs when prices are flat or going down, so the turbulence in today's market isn't surprising. However, we've never seen a period where prices have been flat or declining for this length of time – more than three years in a row – so it's hard to draw lessons from history in this situation.

What caught your attention in the Supermarket News 2012 Analyst Roundtable (http://supermarketnews.com/news/bleak-expectations-financial-pressures-worry-supermarket-analysts?page=2) ?

I was struck by the talk about "the shrinking pie." People are literally spending less on food, but it's not clear where the dollars are going. Other types of retailers, such as dollar stores and hard discounters, have experienced sales increases, but these increases don't begin to match the decline in supermarket sales. The "shrinking pie" isn't something we've heard a lot about up to this point, and I don't think it will be easy for those involved in the supermarket business to accept because it leads to sobering conclusions.

I was also struck by the "trust factor." Among younger shoppers, it appears that traditional supermarkets are losing out to mass merchandisers (who market to them vigorously). These days, young people trust mass merchandisers more than they trust supermarkets. I think it's likely supermarkets will gain in the trust department as they age. Local supermarkets will be more of a draw as this age group has families.

What categories of food are included in the price data you work with?

The Food Institute studies all the ways food goes to market, not just supermarkets.

- We produce a "real growth calculation" by looking at the actual mix of products moving through today's supermarket. For this we bring in measures of price changes beyond the CPI for food to more accurately estimate inflation for the mix of supermarket sales.
- We monitor changes in the price of food at the wholesale level so that we can forecast retail price changes. It turns out that it usually takes three months for wholesale increases to be reflected at retail. We call this our food price tracker, and we publish the results every month.
- We also estimate the percentage of food sales in non-supermarket channels to better understand where the sales lost by supermarkets are going. This is called "food share of alternative retailers."

What's the outlook for food price increases over the next year?

It's always risky to predict the future, and this year everyone seems to be waiting for the last kernel of corn to be harvested before making their forecast, but I'll give it a try. It appears that food prices will not go up significantly this year; however, it could be a different story in 2013. By then carryover will be at much lower levels due to drought conditions, so prices will be particularly volatile. Even if commodity

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food prices do go up in 2013, it's hard to say how much of this will be passed on to shoppers.

If food prices do go up, what's the likely impact on retail growth?

This a hard question to answer because food products are so "substitutable." People truly have a lot of choices in terms of brands and stores and price points, and this means shoppers can easily find alternatives that will help them avoid the impact of price increases. Will shoppers choose to accept certain price increases and continue to buy items? Or will they try to dodge the increases by purchasing substitute products? Only time will tell, so it's hard to anticipate the impact on retail growth.

Do you see the growing use of technology by shoppers affecting the way people adjust to food price increases?

Yes, and this point came up in the roundtable. It seems to me that it's connected with the idea that there's a high degree of substitutability in food purchasing, both in terms of products and places to buy.

- In some cases, technology can help reduce the impact of price increases. Safeway's "Just 4 U" (and similar personalized promotion systems) show shoppers discounts on the products they buy most often, and this should help to insulate people from the impact of short-term price inflation.
- In other cases, technology can expand the number of shopping oportunities. The scannable/shoppable signs for grocery products that Ahold is putting in subways and train stations are an example of how technology is making it easier for shoppers to have more choices for where – and how – they shop.

Is there anything you might have wanted to hear more about in the 2012 Roundtable?

They did a great job. The only thing I might have wished for was a little more coverage on the aggressive growth of food sales in both drug and dollar stores. This is particularly of interest on the West Coast, where dollar stores are expanding aggressively in urban and suburban markets and really growing their food sales.

People are using drug and dollar store outlets more and more frequently, and this will have a noticeable impact on where food shopping happens. Looking at this larger picture would be helpful. It's hard to know if this is a long-term trend, or if the sales that grocery stores have lost to these channels will come back when the economy changes.

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Bill Bishop said:

Price changes over the next year will have a major impact on sales growth, but Brian also points out a more troubling issue. Has food spending actually dropped over the last several years and if so when, if ever, can we expect it to return to pre-2008 levels?

Answering this means unbundling the impact of overall price changes from the adjustments households have made to losses in real income. Getting this answer is important because it will reveal how 21st century shoppers are "redefining" what they mean by "value for money". When we better understand this, it will highlight the changes needed to win a greater share of their wallets. What are some of the ways to begin to answer this question?

October 18, 2012 10:15 am

Leigh Sparks (/leigh-sparks) said:

One of the questions that is regularly posed over here is whether the recent rise in the market shares of Aldi and Lidl (after a couple of decades of trying to break into the UK) is a game change or a recession blip? In Bill's words is there a fundamental redefiing of value for money going on? Answers on a virtual postcard please - but I feel the answer is the former. I feel this from the sense of permanance in their rise and long term chanegd behaviour and from the reactions from main stream retailers at their value end of the retailer brand e.g. Waitrose, Tesco, Asda etc.

October 25, 2012 3:10 am

Bill Bishop said:

Leigh, I think you have it right; i.e. it's a game change driven by price differences too large to ignore. In Chicago, a 15 oz. can of pumpkin costs 99 cents at Aldi, while the same private label product in conventional supermarkets is priced at $1.49 to $1.59. We needed twenty cans and saved at least $10 on that one item.

October 29, 2012 7:57 am

Brian Todd (/brian-todd) said:

The difficult market for food retailing continues as the Bureau of Economic Analysis reported last week that personal consumer expenditures for food in the third quarter were up only 1.7% from the same quarter last year -- just slightly above the 1.4% inflation rate in the same period, indicating no real growth in food sales and further adding to the question, Where Are The Food Sales Going?http://www.foodinstitute.com/economic.cfm

October 29, 2012 10:34 am

Bill Bishop said:

Brian - One reason that overall food sales may be lower is the growing number of shoppers who are no longer being influenced by the weekly circular. These shoppers either aren't reading the paper or newspapers aren't available to them, and they're not looking in their mailboxes for another way to get the circular.

This means that there is unquestionably a growing "marketing communications gap" that's influencing how people shop. There are two ways to close this gap; i.e. 1. Ramp up the effectiveness of digital communications with your shoppers or 2. Build a store that's so different; e.g. Trader Joe's, that you don't need a weekly circular.

November 1, 2012 10:30 am
