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Marketing Bill Is the Largest Chunk of Food Expenditures

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While consumer food expenditures increased only 2.7 percent in 1991, food marketing costs—as measured by the marketing bill—rose 4.5 percent to $361 billion.

Over time, the marketing bill has been the driving force in food expenditure increases (fig. 1). Between 1981 and 1991, the marketing bill grew faster than the farm value, 75 percent compared to 24 percent, and now accounts for 78 percent of the cost of food.

The marketing bill includes consumer foodservice expenditures which are not included in USDA's market basket (see "1991 Rise in Retail Food Prices Was the Smallest Since 1985" elsewhere in this issue). Because the cost of preparing and serving food is a major part of the cost of food eaten away from home, the farm value derived from the marketing bill statistics is smaller than the corresponding market basket figure of 27 cents.

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Marketing Bill Measures Costs Beyond the Farm

The marketing bill includes costs associated with processing, wholesaling, distributing, and retailing of foods produced by U.S. farmers and eaten by U.S. consumers. It is the difference between the value farmers receive for the food and the amount consumers spend on food for consumption at and away from home. The marketing bill excludes expenditures for imported foods and seafoods.

There are several major causes underlying the growth in marketing costs. These include higher prices of marketing inputs, larger volume of food purchased by consumers, a higher percentage of food sold through restaurants and fast food outlets, and more value-added processing and packaging.

Figure 1
Rising Marketing Costs Take a Bigger Bite of Food Expenditures

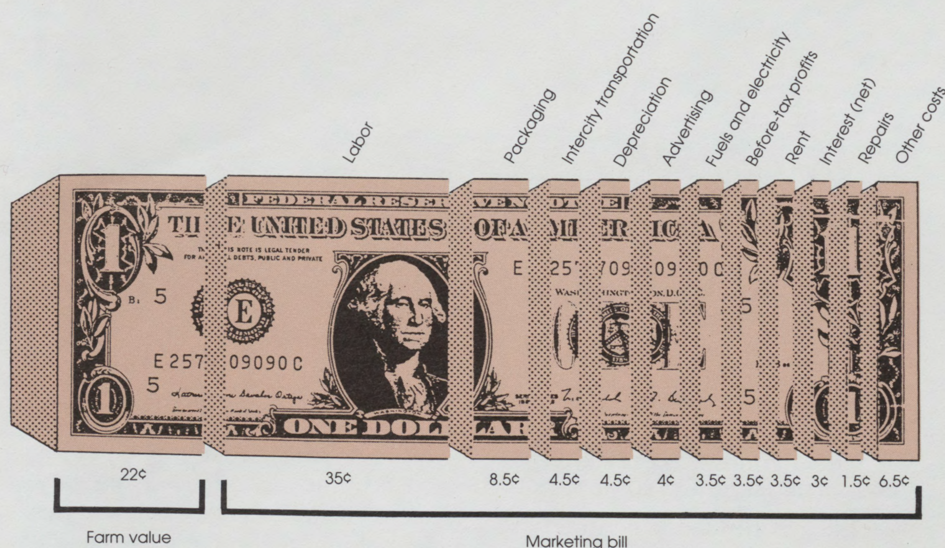
Labor Costs Largely Responsible for 1991 Marketing Bill Increase

Labor costs overshadow all other costs in the marketing bill (fig. 2). Rising labor costs have accounted for almost half the increase over the last decade and were largely responsible for the increase in 1991. Although labor costs grew almost 6 percent to $163 billion (table 1), this was below 1990's increase, as employment and wages rose at a slower pace. However, this increase was roughly equal to the average annual rise of the past 5 years.

Employment in the food industry grew only 0.13 percent last year, compared with an annual average 2.5-percent rise over the last 10 years. This small increase resulted from sluggish retail sales growth during the recession. Employment rose in food processing and distribution, but increases were much smaller than in recent years, particularly in eating places.

Average weekly earnings of workers in food processing rose 2.3 percent in 1991, slightly below 1990's increase. Also increasing at a slower pace were weekly earnings in food retailing, up 2 percent. However, weekly earnings in wholesaling rose faster in 1991, up 3.6 percent.

Figure 2
Over Three-quarters of Every Dollar Spent on Food Goes To Pay Marketing Costs[1]



[1]Includes food eaten at home and away from home. Other costs include property taxes and insurance, accounting and professional services, promotion, bad debts, and miscellaneous items.

Rising Health Care Costs a Growing Concern

The biggest issue affecting the food industry labor picture is health benefits. They account for 20 to 25 percent of the industry's labor costs and have been the top issue on the bargaining table since 1990.

Costs of providing health benefits are escalating rapidly. The Consumer Price Index (CPI) for medical services rose almost 9 percent in 1991, and has risen an average of 8 percent per year over the last decade. Health benefits may take anywhere from 10 to 30 percent of the cash available in union contracts.

Employers are using a number of measures to contain health-care costs. These include requiring second opinions prior to surgery, approval from insurance carriers prior to surgery, and participation in health maintenance organizations (HMO's). Employers also shifted some of the costs directly to employees by means of deductibles and copayments. Some plans reduced benefits, while others required employees to pay a larger share of the premium.

Despite these efforts at containment, however, high health care costs are expected to impact the food industry for some time to come.

Labor Contracts

Labor contracts have an important impact on the overall food industry wage structure, even though union memberships may account for as little as one-third of total food industry employment. These contracts are generally in effect for 3 years and can be used to gauge short-term labor cost trends.

There are two types of labor contracts: front-loaded and back-loaded. Front-loaded contracts provide the largest wage adjustment in the first year of the contract. These settlements compound the amount of the percentage increase in the later years of the contract. By contrast, back-loaded contracts provide lower wage increases in the first year, compared with subsequent years. Back-loaded contracts dampen wages by basing increases in the later years of a contract on a lower initial wage. These contracts were preva-

Table 1
Higher Labor Costs Boost 1991 Marketing Costs

Component	1975	1980	1985	1989	1990	1991
			Billion dollars			
Labor[1]	48.3	81.5	115.6	145.1	154.0	163.0
Packaging materials	13.3	21.0	26.9	35.2	36.5	38.1
Rail and truck transportation[2]	8.4	13.0	16.5	18.6	19.8	20.4
Fuels and electricity	4.6	9.0	13.1	14.8	15.2	16.3
Pre-tax corporate profits	7.1	9.9	10.4	12.2	14.2	15.1
Other[3]	29.7	48.3	76.5	89.7	103.9	107.7
Total marketing bill	111.4	182.7	259.0	315.6	343.6	360.6

[1]Includes employees' wages or salaries and health and welfare benefits. [2]Excludes local hauling charges. [3]Includes depreciation, rent, advertising and promotion, interest, taxes, licenses, insurance, and professional services.

lent in the mid-1980's, as food industry firms sought to control costs.

In 1991, front-loaded contracts dominated bargaining agreements covering food manufacturing and retailing—just as they had in 1990. The Bureau of Labor Statistics reports that the average adjustment for food manufacturing workers was 4.1 percent in the first year and 3.2 percent annually over the life of the contract. For foodstore workers, wage increases averaged 3.7 percent during the first year and 3.4 percent annually over the life of the contract.

Two-tiered wage contracts—in which workers hired after a specified date receive lower wages or fewer benefits—continue to be phased out. Both labor and management have noted the reduced productivity from employees on lower wage tiers. The phasing out of this wage structure, developed during the mid-1980's, is also creating upward pressure on labor costs as the wages of junior employees are brought into line with those of their more senior colleagues.

Lump-sum payments granted in lieu of wage increases were a popular method of containing labor costs in the mid-1980's. These payments restrain labor cost increases by holding down the wage base used to calculate benefits and pensions. Only 20 percent of the workers covered by 1991 contract negotiations received lump-sum payments.

The minimum wage increased from $3.80 an hour to $4.25 an hour on April 1, 1991. Its biggest impact has been on the nonunionized segment of the industry—especially eating places. This segment of the food industry makes up 53 percent of total sector employment, and has most of the minimum-wage workers.

Recession Minimizes Packaging Cost Increases

Packaging is the second-largest component of the marketing bill, accounting for 8.5 percent of the food dollar. Costs of these materials rose 4.4 percent last year, the second smallest increase in 10 years (the 3.7-percent rise in 1990 was the smallest).

Sales of microwaveable products, packaged foods, and other convenience foods requiring specialized packaging rose slowly due to the recession, and caused weak growth in aggregate sales of packaging materials.

Helping to hold down packaging expenses was a 1-percent drop in the price of paper boxes. Prices for paper products are the largest component (40 percent) of packaging costs. The price of linerboard, the major paper box input, declined as manufacturers discounted prices to reduce excessive inventories resulting from sluggish sales.

Plastic prices were also lower. Plastic containers and wrapping materials make up nearly 20 percent of food packaging costs.

As a petroleum derivative, plastic became costlier to produce when higher crude oil prices stemming from the Persian Gulf War drove up plastic prices during the first three quarters of 1991. In the fourth quarter, plastic prices dropped dramatically due to declining crude oil prices. The net result was a 0.5-percent decline in plastic prices for the year.

Metal cans and glass containers account for the remaining 20 percent, and were largely responsible for higher food packaging costs. Metal can prices were up 3 percent and glass containers rose by 4 percent.

Energy Bill Higher

Energy costs, which represent 3.5 percent of total retail food expenditures, rose 7 percent to about $16 billion in 1991. The energy bill included only the costs of electricity, natural gas, and other fuels used in food processing, wholesaling, retailing, and foodservice establishments. Transportation fuel

costs, except for those incurred for food wholesaling, were excluded.

Higher energy costs resulted largely from expansion in the food industry. A 6.4-percent rise in the price of electricity used by food marketing firms also contributed to higher energy costs. However, this increase was somewhat mitigated by a 0.6-percent drop in the price of natural gas due to abundant supplies resulting from a mild winter.

Food retailing and foodservice account for about two-thirds of energy costs incurred by the food industry. About 85 percent of this cost comes from the use of electricity. The food processing sector is responsible for another 20 percent of the total energy bill. Electricity accounts for 55 percent of food manufacturing energy costs, with natural gas making up the remaining 45 percent. The Persian Gulf crisis had only a limited effect on the cost of processing and retailing food because higher oil prices do not significantly affect natural gas and electricity costs.

While energy's percentage increase was greater than the remaining components, its relatively small size mitigates its impact on aggregate food marketing costs.

Transportation Costs Rose Little

Intercity truck and rail transportation costs for farm foods amounted to $20.4 billion in 1991, or about 4.5 percent of retail food expenditures. Railroad freight rates for hauling food products rose about 4 percent in 1991, while operating costs of trucks hauling produce fell 3.1 percent in 1991. The cost of labor and fuel—which account for approximately 45 percent of trucking costs—declined 7.5 percent. Most other expenses fell slightly or remained constant.

Although costs were lower, truck rates for shipping fresh produce remained nearly constant. Competition among different groups of truckers—including individuals who own and operate trucks; trucking companies; and companies that transport their own products, but haul produce on return trips—have held down truck rates. However, higher demand for trucking services—as indicated by a 1-percent increase in shipments of fresh fruit and vegetables—offset lower costs. Therefore, increased marketings were mostly responsible for the small rise in the cost of transporting food.

Profits Growth Slowed

Before-tax profits accounted for over $15 billion, or 3.5 percent of the marketing bill in 1991. This amounts to a 6-percent increase in profits, compared with the 16-percent jump in 1990.

Despite slow sales growth, the industry was able to maintain its profit margins. Helping to keep up margins was the industry's ability to recover somewhat from high debt and interest payments from earlier leveraged buyouts, which squeezed margins during the late 1980's.

Aggregate profit margins were larger for food manufacturers due to modest product price increases, lower farm commodity costs, and modest increases in production and marketing costs. Also, streamlined food processing operations increased worker productivity, allowing manufacturers to hold down labor costs.

Food retailers continued to achieve greater efficiencies through the use of technology for inventory management and merchandising. Retailers control labor costs, their largest operating expense, by using checkout scanners and computer programs that assist in labor scheduling.

Finally, retailers have increased profits by building bigger stores to give more space to high-margin products (such as perishables) and service departments (such as bakeries and instore delicatessens). ■