Food Marketing Costs Rose Modestly in 1993

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Marketing costs are by far the largest chunk of food expenditures. Over three-fourths of what U.S. consumers spent for food in 1993 went to pay for marketing, and only 22 percent represented the farm value of food. While the cost of providing marketing services beyond the farm gate increased modestly in 1993 due to the slow pace of the economic recovery, it continues to be the most persistent source of rising food expenditures.

Food expenditures are divided into two main components: the farm value and the marketing bill. The farm value is a measure of the payments farmers receive for their raw commodities used in food purchased by consumers at foodstores and eating places. The marketing bill represents the difference between the farm value of food produced on U.S. farms and the final cost to consumers. Such costs of processing agricultural commodities into food and bringing them from the farm to the dinner table include labor, packaging, transportation, and energy.

Eating Out Drives Spending Increases

Consumers spent $491 billion for food originating on U.S. farms in 1993 (table 1). (This amount was less than the $617 billion total that U.S. consumers spent on all food because it excludes expenditures for seafood and imported foods. See "1993 Food Spending Picked Up" in this issue for a discussion of total food expenditures.) Consumer expenditures for food in 1993 rose approximately 3.5 percent. This rise was up just 1 percent over 1992's smallest increase of the last decade, and roughly the same as in 1991. Shoppers actively sought values at grocery stores and restrained the rise in expenditures by buying more store brands and using more coupons.

Over three-fourths of what U.S. consumers spent for food in 1993 went to pay for the cost of marketing. Higher labor costs accounted for most of the rise in the marketing bill. Costs of other inputs—such as packaging, energy, and transportation—rose modestly.

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Table 1

Labor Costs Make Up the Largest Share of Food Expenditures

Component	1980	1990	1992	1993
		Billion dollars		
Labor[1]	81.5	154.0	168.4	177.6
Packaging materials	21.0	36.5	39.2	40.5
Intercity transportation[2]	13.0	19.8	20.6	21.1
Fuels and electricity	9.0	15.2	16.7	17.3
Pre-tax corporate profits	9.9	14.8	15.7	15.3
Advertising	7.9	18.5	19.4	19.8
Depreciation	8.4	17.6	18.5	19.1
Net interest	3.7	14.6	15.3	15.8
Net rent	7.3	15.0	15.9	16.4
Repairs	3.9	6.7	7.0	7.3
Total marketing bill	182.7	343.6	369.4	382.1
Farm value	81.7	106.2	105.1	109.2
Consumer food expenditures	264.4	449.8	474.5	491.3

Notes: [1]Includes employees' wages/salaries and health and welfare benefits. [2]Excludes local hauling charges.

About 54 percent of consumers' food dollars went to retail grocery stores. The remaining share was spent on food away from home, which represents the retail value of food served in public eating places, hospitals, schools, and other institutions. The division between spending on food at home and away from home in 1993 was about the same as in 1992. The away-from-home share of consumer food expenditures has increased steadily over the years, from about 35 percent in 1973 and 41 percent in 1983 to 46 percent in 1993.

Spending on food away from home grew more quickly than food purchases at grocery stores. Sales data reported by the U.S. Census Bureau suggest that not only are expenditures for food away from home rising over the years, but consumers are purchasing greater quantities of food in eating places. Sales at eating places rose 5.7 percent in 1993. When adjusted for the rise in menu prices, 1993 sales were still 3.9 percent higher than those in 1992. Meanwhile, consumers purchased roughly the same quantities of food for at-home consumption in 1993 as in 1992. Expenditures at grocery stores increased 2.6 percent, but they were unchanged once adjusted for inflation.

Several explanations can be offered for the larger real growth in away-from-home food sales in 1993. First, menu prices posted the smallest increases in 29 years. And, the wave of value meals offered by fast food chains has increased sales. Second, with higher employment levels increasing household income and reducing the amount of time available to prepare food, consumers purchased a higher percentage of meals at restaurants—a return to the spending pattern prevalent before the 1990-91 recession.

Farm Value Rose

The farm-value component of food expenditures rose about $4 billion to $109 billion in 1993. This 3.9-percent increase was slightly larger than in 1992. Much of the 1993 increase stems from higher prices for broilers and fats and oils, and larger cash receipts for fruit, vegetables, and tree nuts. The farm value of commodities represented 22 percent of consumers' food expenditures in 1993, unchanged from 1992 but down from 24 percent in 1990.

The farm value is a much smaller part of expenditures for food eaten away from home than for food bought at grocery stores, because the cost of preparing and serving food is a major part of the cost of food eaten away from home. The 1993 farm value accounted for about 16 percent of expenditures for food away from home, compared with about 26 percent for food at home.

The farm value share varies greatly among foods, depending on the degree of processing and the amount of services required to move a commodity through the marketing system. Animal products generally have the highest ratios of farm value to retail price, and the more highly processed crop products have the lowest (table 2). For example, the 1993 farm value of eggs (a commodity requiring little processing) represented 58 percent of retail prices. On the other hand, the farm value of cereal and bakery products (which require a great deal of processing and marketing) accounted for only 6 percent of retail prices.

Table 2

Farm Value Share Is the Smallest for Highly Processed Foods

Food	Retail price	Farm value	Farm value share of retail price
	-----Dollars-----		*Percent*
Animal products:			
Eggs, Grade A large, 1 doz.	0.91	0.53	58
Beef, Choice, 1 lb.	2.93	1.64	56
Chicken, broiler, 1 lb.	.89	.48	54
Milk, 1/2 gal.	1.39	.58	42
Fruit and vegetables:			
Fresh—			
Apples, Red Delicious, 1 lb.	.83	.19	23
Potatoes, 10 lbs.	3.48	.81	23
Oranges, California, 1 lb.	.59	.13	21
Lettuce, 1 lb.	.66	.12	18
Processed—			
Frozen orange juice concentrate, 12 fl. oz.	1.22	.40	33
Frozen peas, 1 lb.	.90	.13	15
Canned whole tomatoes, 17-oz. can	.47	.04	9
Crop products:			
Flour, wheat, 5 lbs.	1.17	.33	28
Margarine, 1 lb.	.80	.19	24
Prepared foods:			
Bread, 1 lb.	.75	.05	6
Corn flakes, 18-oz. box	1.54	.09	6

Note: 1993 data.

Marketing Bill Up Modestly

The marketing bill for domestic farm foods rose 3.4 percent to $382 billion in 1993, the result of only small-to-moderate price increases for most inputs purchased by the food industry. The 1993 rise was larger than the 1.6-percent increase in 1992, but smaller than the 5.2-percent annual average gain of the last 10 years. Higher labor costs accounted for most of the rise in the marketing bill. Costs of other inputs—such as packaging, energy, and transportation—rose modestly. Profits dropped slightly.

Consumer expenditures for farm foods have risen 56 percent since 1983, with marketing costs the most persistent source of rising food expenditures. The marketing bill rose 66 percent during this period, while the farm value increased only 28 percent (fig. 1).

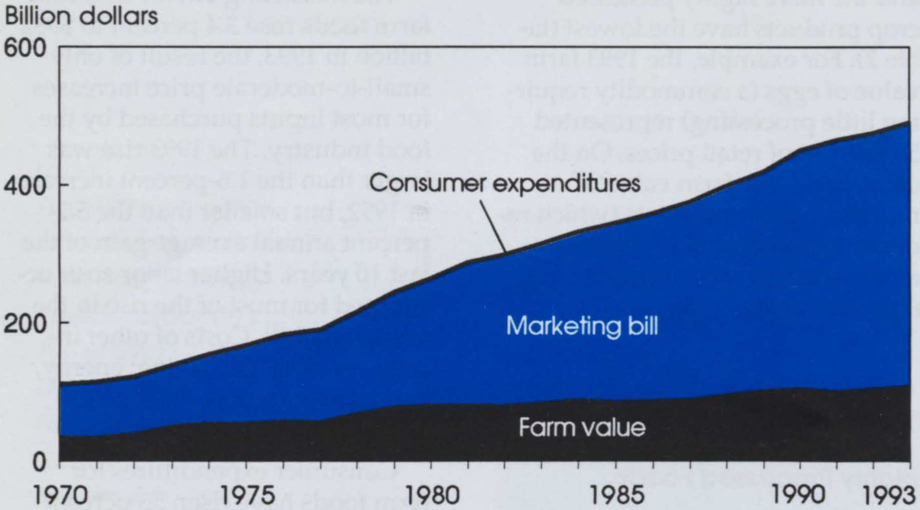
Labor Costs: The Main Catalyst

Labor costs overshadow all other components of the marketing bill. Rising labor costs are responsible for nearly half the increase in the marketing bill during the last 10 years, and are the primary factor underlying the 3.4-percent increase in 1993.

Direct labor costs came to about $177.6 billion in 1993, or 36 percent of food expenditures (fig. 2). Direct labor costs include wages and salaries; employee benefits, such as group health insurance; estimated earnings of proprietors and family workers; and tips. These costs do not include labor engaged in for-hire transportation of food or labor employed in the manufacturing and distribution of supplies.

1993 saw the largest increase in food industry employment since 1988—up 2.5 percent, with 12.6 million workers processing and distributing food. More than half (6.8

Figure 1
Marketing Costs Accounted For Over Three-Quarters of 1993 Food Expenditures



Note: Data are for foods of U.S. farm origin purchased by or for consumers for consumption both at home and away from home.

million people) worked in eating places. Employment jumped nearly 4.0 percent in eating places, reflecting larger sales of meals away from home. Foodstores employed 3.2 million people, food processors 1.7 million, and food wholesalers about 870,000.

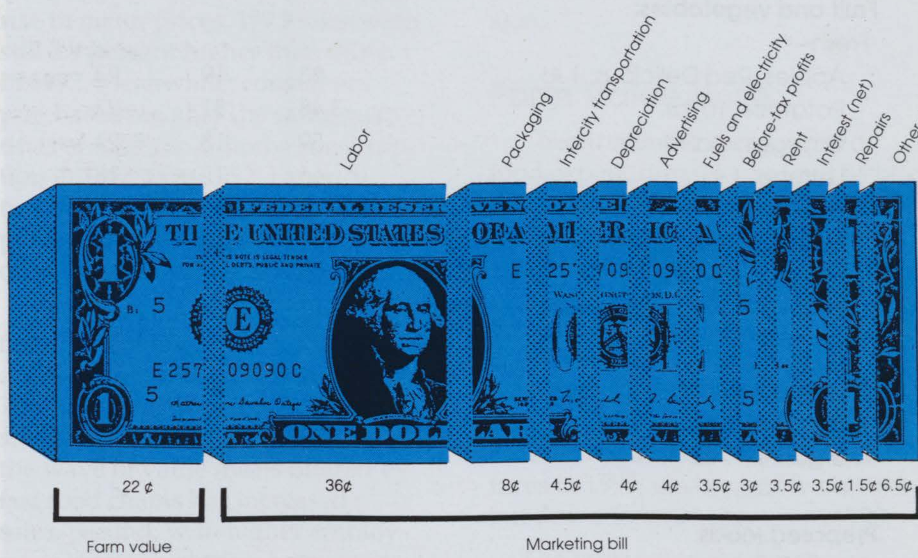
Food retailing employment rose about 1.0 percent in 1993, reflecting flat retail sales and managerial efforts to restrain cost increases. Food manufacturing employment fell 0.3 percent, as higher labor productivity and increased use of technology alleviated the need for additional hirings.

With higher wages and benefits, labor costs in the food industry rose about 5.5 percent in 1993, a faster rate of gain than 1992's 4.7-percent rise. Employees of food wholesaling firms saw their wages rise the fastest, 3.5 percent, in 1993. Hourly earnings increased 2.4 percent in food manufacturing, compared with 2.9 percent in 1992. Earnings of foodstore workers rose 3.2 percent, up from 2.2 percent in 1992. The 1993 rise for manufacturing employees was 0.5 percent below the previous year. Wages for workers in eating and drinking places rose only 1.1 percent, about half the 2.1-percent increase in 1992.

Wage supplements increased because of rising health-insurance premiums and pensions. The rising cost of medical care pushed up health insurance costs. However, the 6.5-percent increase in the Consumer Price Index (CPI) for medical services in 1993 was smaller than the 7.3- percent average annual increase over the last 10 years.

The Employment Cost Index (ECI), a quarterly series published by the Bureau of Labor Statistics, measures labor compensation and further illustrates developments in labor costs. The index for foodstores rose 2.9 percent in 1993, smaller than the 3.8-percent gain in 1992. The 1993 increase included a 2.5-percent wage and salary gain, also smaller than the 3.3-percent rise for 1992. The ECI indicates that compensation costs rose more than wages and salaries in 1993 because the cost of benefits rose more than wage rates. Although not reported

Figure 2
About One Third of Consumers' Food Dollars Went To Pay Food Marketing Labor Costs in 1993



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

separately, the increase in benefit costs was probably about 4.5 percent in 1993, or 1.8 times the rise in the wage rate of foodstore workers. Labor compensation rose slower in foodstores than the 3.6-percent increase in private industry as a whole.

Foodstores used several methods to cut labor costs in 1993. Of the 29 major union contracts negotiated last year, over half provided for lump-sum payments or back-loaded wage structures.

Lump-sum payments were a popular method of restraining labor cost increases during the mid-1980's, but have been less prevalent in recent years. These payments restrain labor cost increases by holding down the wage base used to calculate benefits and pensions. Moreover, contracts with lump-sum provisions generally provide for smaller wage-rate changes than do contracts without lump-sum coverage. Back-loaded contracts provide lower wage increases in the first year of a contract than in subsequent years. Back-loaded contracts dampen wages by basing increases in the later years of a contract on a lower initial wage.

Retailers also continued to cut costs by making extensive use of part-time employees, which likely held down the rise in hourly earnings in food retailing.

Labor Productivity Also Up

Labor productivity in food manufacturing has increased moderately. Output per unit of labor in seven food manufacturing industries for which data are available rose an average of 2.2 percent annually from 1981 to 1991 (table 3). These increases generally resulted from higher output and a slightly lower number of hours worked, mainly because of widespread mechanization and technological improvements. Labor productivity among those seven industries has increased the most in grain milling and fluid milk processing. However, productivity has grown erratically for most food processing industries, partly because of fluctu-

Table 3

Food Industry Labor Productivity Up, But Uneven

	Food manufacturing							Retail food stores	Eating and drinking places
Year	Meat-packing plants	Poultry dressing and processing	Fluid milk	Preserved fruit and vegetables	Grain mill products	Bakery products	Sugar		
	Index of output per employee hour (1987=100)								
1980	82.2	77.8	74.7	83.7	70.4	81.5	84.7	107.5	106.5
1981	86.0	85.5	77.2	82.4	74.2	83.7	83.6	104.2	103.9
1982	90.2	92.4	81.6	89.6	80.9	89.8	76.6	102.2	103.5
1983	94.1	96.9	86.1	92.1	83.7	93.4	82.3	102.1	102.5
1984	96.7	96.1	89.4	93.4	88.6	93.9	82.5	102.4	98.9
1985	101.1	98.2	92.2	94.6	93.8	95.5	85.9	102.4	96.2
1986	99.2	93.9	96.4	98.6	94.5	101.1	88.5	102.0	99.2
1987	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1988	100.6	95.3	104.0	98.7	100.0	92.7	97.4	98.1	103.0
1989	91.5	100.1	106.8	97.9	99.8	92.4	92.7	95.4	102.9
1990	91.1	106.1	108.0	97.7	104.1	93.8	93.9	94.6	104.6
1991	94.6	112.5	110.8	99.9	104.6	90.5	97.0	93.8	106.1
1992*	97.3	NA	112.5	NA	NA	89.9	101.9	94.5	104.6

Notes: NA = Not available. *Preliminary. Some historical data were revised. Source: U.S. Department of Labor, Bureau of Labor Statistics.

ating output and business conditions.

Output per unit of labor among supermarkets declined each year between 1985 and 1991. In 1992, output of foodstores rose 0.3 percent, while hours worked dropped 0.5 percent, resulting in a small productivity increase of 0.7 percent. Some store operations have become more efficient over the past decade because of computer-assisted checkouts, data processing systems, and new store formats (such as warehouse stores) which incur lower operating expenses than do supermarkets. Warehouse stores offer a limited assortment of products and provide fewer services, thereby reducing labor requirements and fostering higher sales per unit of labor.

On the other hand, many food retailers have expanded their service-oriented operations (such as delicatessens, salad bars, and instore bakeries)—thus labor requirements—in response to consumer demand for convenience.

Labor productivity among eating and drinking places slipped 1.4 percent in 1992, but has risen slightly since 1985. The recent decline is due to a rise in hours worked of about 1.8 percent, while output increased only 0.4 percent.

Packaging, Energy, and Transportation Rose Little

Packaging is the second-largest component of the marketing bill, accounting for 8 percent of food expenditures. Costs of these materials rose about 3.3 percent last year (roughly the same rate of increase as the marketing bill), mainly because of greater use of shipping boxes, food containers, and plastic materials.

The price of most major packaging materials rose little or declined. For example, the price of paperboard shipping boxes and other paper products declined 0.6 percent in 1993, while the price of paper bags and sacks dropped 0.1 percent. These decreases reflected large paperboard supplies stemming from excess production and inventory levels. At the same time, the price of plastic fell 0.6 percent. Plastic is an oil derivative and became cheaper to produce in the last few years due to lower crude oil prices. The price of glass containers rose 0.5 percent, while metal can prices remained about the same as in 1992.

Intercity truck and rail transportation for farm foods amounted to $21.1 billion in 1993, or about 4.5 percent of retail food expenditures. The transportation cost index, representing railroad freight rates, advanced 0.9 percent in 1993, slightly more than the gain recorded in 1992. Most foods shipped by railroad are canned and bottled products. Operating costs of trucks hauling produce increased 2.6 percent in 1993, pushing up truck rates for shipping fresh produce in most corridors. Fuel and labor accounted for half of total truck operating costs. Trucking wages rose 3.4 percent, while fuel costs slipped 2.9 percent. Other expense items—depreciation and maintenance, overhead, licenses, and insurance—rose an average of 3.6 percent.

The 1993 energy bill for food marketing came to about $17.3 billion, or about 3.5 percent of retail food expenditures. That is up 3.6 percent since 1992, slightly greater than the increase in the marketing bill. Natural gas prices jumped 6.8 percent and were largely responsible for higher energy costs, while electricity prices rose only 1.6 percent.

Energy costs for processing and retailing food are primarily affected by natural gas and electricity prices. Electricity makes up 55 percent of the energy costs incurred in food manufacturing, with natural gas accounting for the remaining 45 percent. Electricity accounts for 85 percent of energy used by public eating places and nearly all of the energy used in foodstores.

Profits Fell in 1993

U.S. firms generated approximately $15.3 billion in pre-tax profits from manufacturing and marketing food, a 2.5-percent drop from 1992. 1993 profits made up about 3 percent of food spending.

Lower profit margins for food retailers were primarily responsible for the decline in profits. Profit margins of retail food chains averaged 1.6 percent of food sales, slightly less than last year's margin of 1.8 percent. Most of the drop occurred in the first quarter of 1993, and was due to a write-off against income of post-retirement benefits other than pensions. Profit margins for these stores were higher during the remainder of 1993.

The growth in profit margins of retail food chains in the rest of the year mainly reflected the gradual strengthening in the economy and technological improvements. Retailers continued to make greater use of technology—particularly checkout scanning, satellite communications, and more sophisticated merchandising and labor scheduling systems—to control labor costs, their largest operating expense.

Food manufacturing profits rose slightly, following modest price increases and nearly stable costs of raw materials. Food manufacturers have also been able to hold down costs with gains in labor productivity. However, manufacturing profits were tempered by increased consumer purchases of less costly store-label foods, which cut into sales and profits of the manufacturers of brand-name foods. ■