Food Marketing Costs Increased in 1994

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The 1994 economy yielded the largest aggregate employment growth of the last decade. Higher wages and salaries produced the strongest growth in per capita personal income since 1988—up 2.5 percent in real dollars (adjusted for inflation)—which spurred higher consumer expenditures for food.

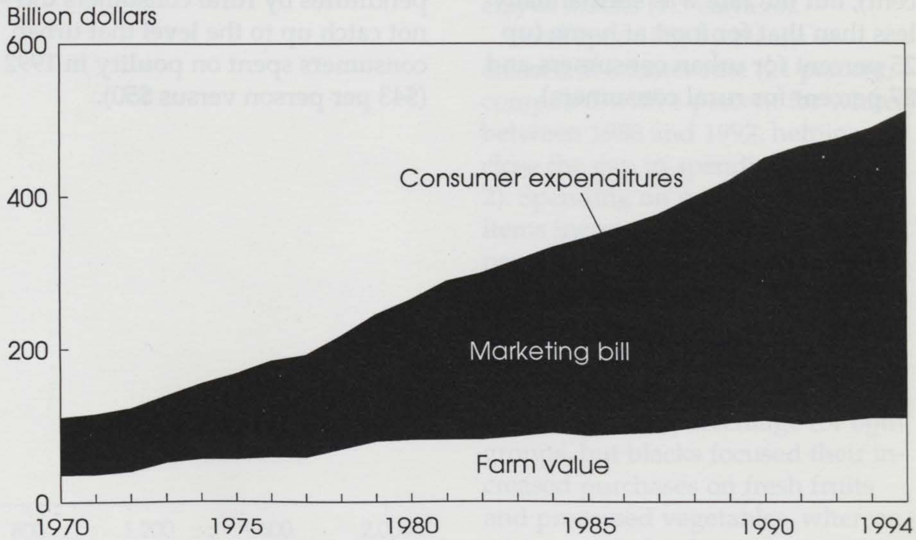
Sales of food purchased in grocery stores rose 0.4 percent in real dollars in 1994—a small increase, but a reversal of the 0.2-percent drop the previous year. Personal income growth was more strongly manifested at eating places, where real spending grew 5.2 percent. The growth in food spending translated into higher demand for the marketing and processing services that are required to bring food from the farmer to the consumer.

Nearly four-fifths of the $510.6 billion U.S. consumers spent for farm foods (excludes seafood and imports) in 1994 went to pay for marketing costs. The remaining 21 percent represented the farmers' share of food expenditures. Nominal consumer expenditures for farm foods have risen 54 percent since 1984. The marketing bill rose 66 percent over the past decade, while the farm value increased only 22 percent (fig. 1).

Food marketing costs are measured by the marketing bill, which represents the difference between the farm value of food produced on U.S. farms and the final cost to consumers at grocery stores and eating places. Such costs include labor, packaging, transportation, and energy, as well as other marketing services, such as advertising and promotion.

The cost of providing marketing services beyond the farm gate increased moderately in 1994, and continues to be the most persistent source of rising food expenditures. The marketing bill for domestic farm foods rose 5.6 percent in 1994 to $401 billion. Higher labor costs accounted for most of the rise. Costs of other inputs, such as energy and transportation, rose modestly, while packaging and profits posted strong increases. The 1994 rise in the marketing bill was larger than both the 2.8-percent increase in 1993 and the 5.2-percent average annual gain of the last 10 years.

Figure 1
Over Three-Quarters of 1994 Food Expenditures Went To Pay Marketing Costs



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

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Higher Labor Costs Fueled the Marketing Bill's Rise

Labor overshadows all other cost components of the marketing bill. Rising labor costs are responsible for half the increase in the marketing bill during the last 10 years, and are the primary factor underlying the 1994 increase.

Direct labor costs came to about $188.9 billion in 1994, or 37 percent of food expenditures (fig. 2). Direct labor costs include wages and salaries; employee benefits, such as health insurance; estimated earnings of proprietors and family workers; and tips. These costs do not include labor accounted for by other cost components, such as for-hire transportation of food or labor employed in the manufacturing and distribution of packaging supplies.

With higher wages and benefits, labor costs in the food industry rose about 6.1 percent in 1994, a higher gain than 1993's 5.7-percent rise. Hourly earnings increased 2.1 percent in food manufacturing, compared with a 2.6-percent hike in 1993. Average hourly earnings of foodstore workers rose 1.8 percent, a smaller increase than 1993's 2.9-percent rise. These smaller increases reflect wage-restraining provisions negotiated in labor contracts. On the other hand, wages for workers in eating and drinking places rose 2.2 percent, double the gain in 1993. Higher wages for foodservice workers reflect increased demand for labor in restaurants, which needed to pay higher salaries in order to attract and retain workers.

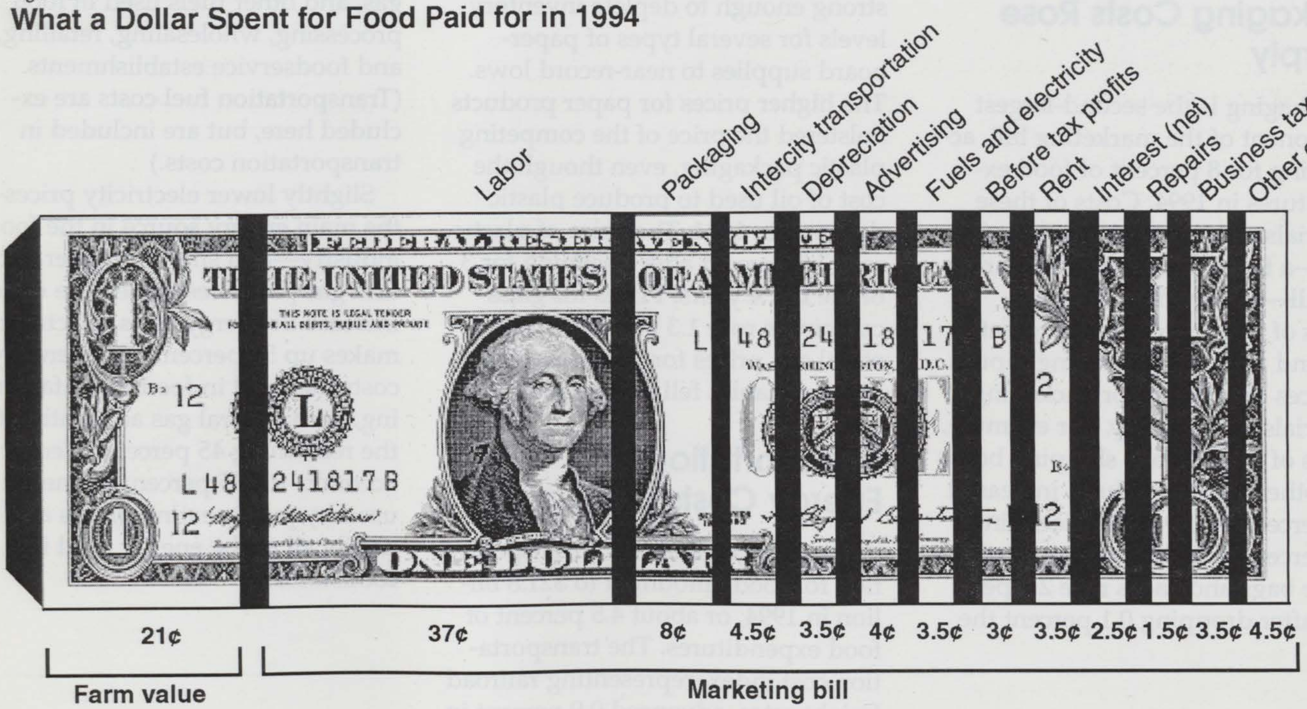
In 1994, food industry employment increased 2.3 percent to 12.8 million people, a slightly smaller gain than in 1993. About 25 percent worked for foodstores, 13 percent for food manufacturing firms, and 7 percent for food wholesalers. More than half, 7.1 million people, were employed by eating places.

Employment in eating and drinking places shot up 3.6 percent in 1994, the largest employment increase in the food industry. In fact, this sector experienced the second-largest rise in employment of any U.S. industry in 1994, behind only employment agencies and other hiring services. The labor-intensive nature of foodservice has meant strong employment growth in order to meet the demand for convenience food and restaurant meals.

By contrast, food retailing employment rose about 1.1 percent in 1994, reflecting relatively flat retail sales and managerial efforts to restrain cost increases. Food manufacturing employment fell 0.5 percent, as higher labor productivity and increased use of technology alleviated the need for additional hirings.

The cost of benefits increased 7.0 percent, because of higher pensions and escalating health-insurance premiums due to rising medical costs. However, the 5.2-percent increase in the Consumer Price Index for medical services in 1994 was smaller than both the 6.5-percent increase

Figure 2
What a Dollar Spent for Food Paid for in 1994



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

Table 1
Labor Makes Up the Largest Share of Food Marketing Costs

Component	1980	1985	1990	1993	1994
			Billion dollars		
Labor[1]	81.5	115.6	154.0	178.0	188.7
Packaging materials	21.0	26.9	36.5	39.4	42.1
Rail and truck transportation[2]	13.0	16.5	19.8	21.2	21.8
Fuels and electricity	9.0	13.1	15.2	17.2	17.9
Pretax corporate profits	9.9	10.4	13.2	14.2	16.0
Advertising	7.3	12.5	17.1	18.3	18.9
Depreciation	7.8	15.4	16.3	16.8	17.4
Net interest	3.4	6.1	13.5	13.1	13.5
Net rent	6.8	9.3	13.9	17.0	17.8
Repairs	3.6	4.8	6.2	6.8	7.1
Business taxes	8.3	11.7	15.7	17.6	18.3
Other costs	11.1	16.7	22.2	20.0	21.5
Total marketing bill	182.7	259.0	343.6	379.6	401.0

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

recorded in 1993 and the 7.2-percent average annual increase over the last 10 years.

Packaging Costs Rose Sharply

Packaging is the second-largest component of the marketing bill, accounting for 8 percent of food expenditures in 1994. Costs of these materials rose about 6.9 percent in 1994—a faster pace than the marketing bill—mainly due to higher prices of raw materials and greater demand for most packaging inputs.

Prices of most major packaging materials rose sharply. For example, prices of paperboard shipping boxes and other paper products increased 4.7 percent in 1994 after declining 0.6 percent in 1993, and prices of paper bags and sacks rose 2.5 percent after dropping 0.1 percent the previous year. These increases reflected a stronger demand for paperboard materials used to package consumer nondurables—demand strong enough to deplete inventory levels for several types of paperboard supplies to near-record lows. The higher prices for paper products bolstered the price of the competing plastic packaging, even though the cost of oil used to produce plastic dropped in 1994. The price of plastic rose 1.3 percent after declining for 3 of the last 4 years. Prices for glass containers rose 1.3 percent, while metal can prices for processed fruits and vegetables fell 3.5 percent.

Transportation and Energy Costs Up Slightly

Intercity rail and truck transportation for food amounted to $21.8 billion in 1994, or about 4.5 percent of food expenditures. The transportation cost index, representing railroad freight rates, advanced 0.9 percent in 1994, slightly more than the gain recorded in 1993. Most foods shipped by railroad are canned and bottled products.

Trucking rates, as measured by the Bureau of Labor Statistics, grew 2.2 percent due to higher operating costs and the stronger economy. For example, operating costs of trucks hauling produce were 0.6 percent higher in 1994, with fuel and labor accounting for 44 percent of the total. Trucking wages rose 1.7 percent, half of the increase in 1993, while fuel costs slipped 2 percent. Other trucking expenses—depreciation and maintenance, overhead, licenses, and insurance—rose an average of 0.6 percent, compared with a 3.6-percent increase in 1993. These trucking expenses were restrained by small increases in overhead expenses and largely unchanged maintenance costs.

The 1994 energy bill for food marketing increased 4.1 percent to about $17.9 billion, a slower pace than the increase in the marketing bill. Energy costs again comprised about 3.5 percent of retail food expenditures in 1994. The energy bill includes only the costs of electricity, natural gas, and other fuels used in food processing, wholesaling, retailing, and foodservice establishments. (Transportation fuel costs are excluded here, but are included in transportation costs.)

Slightly lower electricity prices—the main energy source in the food industry—and slightly higher natural gas prices restrained the overall increase in energy costs. 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 Rose Sharply in 1994

U.S. corporations earned approximately $16 billion in pre-Federal-income-tax profits from manufacturing and marketing food, a 12.7-percent jump from 1993. In 1994, about 3 cents of every food dollar went to pretax corporate profits.

Food retailers' profits were 67 percent higher in 1994 than in 1993, as profits rebounded from 1993's unusually low levels. Profits were reduced in 1993 as the result of a first-quarter write-off against income of post-retirement benefits, which lowered reported profits for the entire year.

The stronger economy, technological improvements, and increased sales of store labels and prepared foods (deli items, salad bars) also stimulated higher 1994 retail profits. Retailers continued to make greater use of technology—particularly checkout scanning, satellite communications, and more sophisticated merchandising and labor scheduling systems—to increase efficiency and control labor costs, their largest operating expense. 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.

Food manufacturers have also been able to hold down costs with gains in labor productivity. Profits rose for many food manufacturing companies in 1994. However, manufacturers' profits continue to be tempered by increased consumer purchases of less costly store-label foods, which cut into sales and profits of manufacturers' brand-name foods. Moreover, an extensive restructuring by a major food processor resulted in a major net income loss, which produced a 0.7-percent decline in aggregate 1994 food manufacturing industry profits.

Food wholesaling profits also declined, slipping 8 percent from 1993. This drop reflected decreased sales by wholesalers to their biggest clients, independent grocery stores. Independent grocery stores have been losing sales to supercenters that offer both food and an extensive line of other retail merchandise.

Restaurant chains' profits rose 7 percent in 1994, reflecting stronger sales growth. Foodservice continues to capture an expanding share of total food expenditures. However, the demand for convenience is also being seen at grocery stores, where prepared foods are accounting for higher percentages of supermarket sales. The distinction between the retail (at-home) and foodservice (away-from-home) markets has become increasingly blurred as these two segments compete for the consumer's food dollar. ■