The Economic Downturn: A Transformative Event for the U.S. Food Marketing System?

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Presentation Overview

- Intersection of economic forces and their impacts on:
- consumer food assistance needs - food stamps (SNAP), food banks and
- demand for food/fresh produce - the products that you are in business to sell.
- The economic downturn has had a major effect on the food marketing system. More than originating new trends, it intensified pre-existing forces driving greater competition at all levels of the food system, such as, channel blurring. Margin pressure!
- This means ever more pressure for firms to increase productivity and efficiency in order to survive on lower net margins (margins that were usually already thin, including store-wide retail margins).
- 46.2 million people (nearly 1 in 7 Americans) were on food stamps in 2011 vs 17.3 million in 2000.
- It is not only the economy, but changes in public policy over the last two decades, which are driving expanded public food assistance expenditures. There is a story to tell.
Growth of Sales at Traditional Foodstores, 2000-2011, in Current and Constant Dollars (2000 base)

Consumer Behavior

- In 2009, the quantity of food sold in food stores declined.
- “I buy only what I need.” Consumers are increasingly concerned about waste.
- This is likely negatively impacting fresh produce buying patterns, in particular.
- Plus, consumption rates of fresh produce increase markedly with income level. So, more low income people means a challenging environment for the produce industry.
- Bifurcation of US consumers: high income consumers (about 18% of households earn >$100,000/yr) are loosening the reins again and spending at upscale retail outlets and for premium produce, including value-added produce.
- Meanwhile, lower and lower middle income consumers are very constrained, and there's more of them.
- Foodservice is only now recovering to pre-recession real $ sales; operators making sure to offer more lower price menu options today.
Food Industry Trends

- Shoppers more focused on finding the best value for specific items and willing to shop multiple channels to obtain.
- Shoppers migrating towards retailers with clearly defined value credentials (whether high or low end).
- Many retailers lowered prices to close the gap with discount competitors, squeezing store-wide margins.
- As of 2008 many retailers experienced numerous quarters of same store negative sales.
- Cost-cutting to maintain margins, seeking efficiency gains.
Food Industry Trends

• Lowering inventory levels, SKU RAT, painful lessons already.
• Retail corporate restructuring to eliminate duplication and generate cost savings.
• New pricing initiatives, and more targeted pricing to specific consumer segments using loyalty card data.
• Ongoing new format development, e.g., smaller, price impact or fresh food formats, including by traditional grocery retailers.
• Expansion of Target’s P-Fresh and Super Target formats, Walgreen’s entry into food, etc. If drug stores succeed with produce it should create new demand (opens up a new distribution channel with a huge number of outlets).
Food Industry Trends

• Retail corporate restructuring to eliminate duplication and generate cost savings.
• Store brand/private label growth.
• Private labels help retailers to increase consumer loyalty, many offering tiered private labels with different value propositions; all levels help retailers to combat discount retailers.
• Rapid emergence of social media as a tool for communicating value propositions to consumers; most retailers not fully exploiting. Great opportunities for retailers and shippers.
US Select Supermarket* Fresh Produce Dept. Performance During the Economic Downturn, % Change vs. Prior Year

*Excludes club stores, supercenters, part of conventional grocery and other alternative formats.

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Weekly $Sales/Store</td>
<td>3.3</td>
<td>2.0</td>
<td>3.2</td>
<td>4.3</td>
</tr>
<tr>
<td>Weekly Quantity Sold/Store</td>
<td>-3.6</td>
<td>-2.5</td>
<td>1.5</td>
<td>-1.1</td>
</tr>
</tbody>
</table>

Source: Perishables Group FreshFacts® powered by Nielsen
## Changes in Income of the Population during 2000 and 2010

<table>
<thead>
<tr>
<th>Population Characteristics</th>
<th>Year 2000*</th>
<th>Year 2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Million</td>
<td>Percent</td>
</tr>
<tr>
<td><strong>Total low-income population</strong> ****</td>
<td>79.3</td>
<td>28.8</td>
</tr>
<tr>
<td><strong>Total moderate/high-income population</strong></td>
<td>196.1</td>
<td>71.2</td>
</tr>
<tr>
<td><strong>Total population</strong></td>
<td>275.5</td>
<td></td>
</tr>
</tbody>
</table>

*Income data were missing for about 4.1 million people in 2000.
**Not all low-income people live below the poverty threshold.

Source: Access to Affordable and Nutritious Food: Updated Estimates of Distance to Supermarkets Using 2010 Data / ERR-143, ERS, USDA
Changes in the USDA's Supplemental Nutrition Assistance Program (SNAP) - What's the Story?

• SNAP is one of the largest federal means-tested entitlement programs; providing $72 billion in benefits in 2011. Administered by USDA.
• Average SNAP benefit/household $289 in 2010.
• In 2011, 15.9% of Americans were living in poverty and 22.5% of children. (The rates for Monterey County are 17.1% and 24.5%, respectively; 12.4 and 17.6% for San Benito County; and 14.9 and 18.5% for Santa Cruz County.)
• Half of SNAP recipients are children, consistent over time.
• Changes in the economy clearly affect the number of participants.
• However, public policy changes are a very important part of the story!
• Welfare reform in 1996 also made major changes in SNAP, tightening eligibility and benefits, and increasing obstacles to qualify. The changes generally complicated program administration. SNAP benefits for legal immigrants were eliminated.

Changes in SNAP – What's the Story?

• As of '96, states were penalized for funding ineligible people so states erred on the side of caution.
• For example, special attention was placed on the working poor, so households with one wage-earner often had to be recertified every 3 months (to ensure they were indeed needy/eligible).
• In some cases bureaucrats were conducting in-home interviews.
• Average benefit levels were also reduced so many eligible and needy consumers no longer participated – it wasn't worth the hassle.
• By 2000 it became apparent that programmatic issues/obstacles were reducing food security and food demand, a concern for agriculture.
• A series of legislative actions since 2000, including the 2002 Farm Bill, have streamlined access, reduced burdens to qualify and expanded eligibility and participation.
• Basically, in the first half of the 2000's, Congress started giving back the SNAP benefits it took away as part of welfare reform in 1996, including SNAP access for legal immigrants.

Changes in SNAP - What's the Story?

- The 2008 Farm Bill further increased participation, in part due to changes designed to help/encourage vs penalize working-poor families.
- Many states were allowed to move to qualification criteria that were income-based vs a combination of assets and income. For example, autos and retirement accounts were excluded.
- Dollar benefit levels were enhanced in 2009 with the passage of the American Recovery and Reinvestment Act (ARRA), as a response to the worst economic downturn since the Great Depression.
- Maximum benefit levels were increased by 14%; on average households received $46 more per month.
- SNAP funds are spent immediately and go into the economy and help to support food demand.
- The ARRA funds are temporary, expiring Nov. 2013. This may increase pressure on food banks.
- Today 67% of people eligible for SNAP are participating.
- Policy changes (described earlier) have contributed to SNAP participation increasing at a faster rate than the growth in the rate of poverty.

Changes in SNAP - What's the Story?

• Between 2007-2010, unemployment rose from 4.6-9.6%, the number of people in poverty grew 26%, and the SNAP caseload increased 56%.
• When welfare reform was enacted about 37% of households getting SNAP benefits also received cash assistance and only 10% had no other source of income besides SNAP.
• The '96 welfare reform act reduced cash payments (welfare assistance dollars).
• In FY 2010, only 8% of SNAP households were receiving cash welfare assistance and nearly 20% had no other source of income.
• Between 2000-2009, SNAP contributed to an ave. annual decline in the depth of poverty of 10.3%, and 15.5% for children.
• Bottom line for SNAP:
  • SNAP has become a much more important part of the safety net.
  • Without the growth in SNAP, food demand would have been lower, including for fresh produce.

The number of people living in poverty, SNAP participants and the unemployment rate all bottomed out in 2000. The number of SNAP participants and the unemployment rate were less closely linked over the last decade. The number of people in poverty grew even when unemployment declined, and greater SNAP access/benefits contributed to growth in SNAP participation then as well.

SNAP = Supplemental Nutrition Assistance Program.

Note: April 2013 unemployment rate of 7.5% so improving but Q1 2013 economic growth rate of just 2.4% not strong enough to quickly reduce the unemployment rate.
Food Deserts or Food Access Trends, Mixed Picture

• Food deserts are a rising topic of discussion. A major USDA study looked at whether this was a growing problem and found:
  • More people live in low-income areas and are >1 mile from the nearest supermarket, 9.7% of the population in 2010 vs 8.4 percent in 2006.
  • But the rate of car ownership improved over the last decade, improving food buying options for low income people.
  • Only 1.8% of all households didn't have a vehicle and were >1 mile from a supermarket in 2010, vs 2.3% in 2006.
  • More retailers are testing stores in food deserts, Walmart example.
  • My interpretation is that food access is not worsening significantly despite the economy and that it is not a major problem.

Source: Access to Affordable and Nutritious Food, ERR 143, USDA/ERS, November 2012.
Consumers and Fresh Produce

- Growing consumer awareness of the health and wellness benefits of fresh produce is lagging consumption, especially for lower and middle income consumers.
- Forces are in play to change this (MyPlate, salad bars in schools, PBH, govt and private efforts to increase awareness of the health benefits of fruits and veg, etc).
- In the meantime, let's look at how important income is to food and produce consumption. This emphasizes how important economic and personal income growth are to a rebound in produce demand.
The Economic Downturn and its Effect on Fresh Produce

• Troubled times in US retailing, margin squeeze transmitted upstream to produce suppliers.
• Fresh produce has not shown a consistent recovery since 2008.
• Pressure on shippers to differentiate products and services all the while food safety/traceability, sustainability/social responsibility costs rising.
• Firms at all levels of the food marketing system must become even more efficient to survive on pressured margins.
• Most fresh produce items are sold without UPC bar codes which has contributed to less-intensive use of data. Growth in packaging and scannable bar codes as part of PTI implementation are changing this.
• Information technology holds potential for both internal firm-level and system-wide efficiency gains.
• We can become more efficient, including reducing shrink through better coordination of supply and demand. This will make produce more affordable to more consumers.
### Estimated Range of Losses in the U.S. Fresh Produce Distribution System

<table>
<thead>
<tr>
<th>Activity</th>
<th>Percent Losses</th>
</tr>
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<tbody>
<tr>
<td>Distribution</td>
<td>2.80 – 5.00</td>
</tr>
<tr>
<td>Transportation</td>
<td>2.50 – 5.03</td>
</tr>
<tr>
<td>Wholesaling</td>
<td>2.74 – 6.58</td>
</tr>
<tr>
<td>Retailing</td>
<td>9.04 – 16.61</td>
</tr>
<tr>
<td>System losses</td>
<td>9.04 – 16.61</td>
</tr>
</tbody>
</table>

Percentage losses are based on dollar values of losses in each phase of distribution as a % of the wholesale value of products entering the distribution system.


**Update: 2010**

*Guestimate by Roberta Cook, Preliminary: 9-12% or $11-15 billion.*
The Food Industry Challenge

• Getting the right product to the right consumer at the right place and price.
• Requires ability to use large data sets, including retailer customer loyalty card.
• Requires collaboration between suppliers and retailers, including to improve promotional efficiency.
• Shippers increasingly involved in category development but most not assisting with individual store shelf-set recommendations.
• Success will reduce food system-wide shrink.
Conclusions

• Until the economy generates more jobs the demand for food assistance programs will be high.
• Fresh produce faces challenges during an economic downturn and a quick recovery is not anticipated, meaning:
  • Firms at all levels of the fresh produce supply chain must take management practices to a higher level
  • Better information technology is a necessary but not sufficient condition for meeting today's/future standards for efficiency
  • Firms must develop cultures of continuous improvement and innovation
  • Understanding consumer segments as they relate to preferences for a product/retail format is vital
  • Competitive pressure on retailers means on-going margin pressure for suppliers as well.