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Inflation in the Global Food System

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Farrelly & Mitchell is a food and agri-business consultancy empowering some of the world's most ambitious companies and agencies to make the right decisions. Our work across the global food system gives us a unique bird's-eye perspective. In this article we sift through the some of the current figures on inflationary pressures facing global food systems, the factors that have led to this and the outlook for the future.

What is happening?

World food prices rose by 28% in 2021 to their highest level in a decade and hopes for a return to more stable market conditions this year are slim according to the U.N.'s food agency. The Food and Agriculture Organization's (FAO) food price index, which tracks the most globally traded food commodities, averaged 125.7 points in 2021, the highest since 2011 (131.9 points).

In the U.S., food retail prices have risen due to the pandemic and are forecast to continue to rise. Supermarket prices are expected to rise for staples including pasta, condiments, soups, cookies, produce, dairy products and meats. The inflation rate was 7.0% in December 2021 — the highest in 39 years.

Data released in 2021 by the U.S. Department of Labor reveals that the overall Consumer Price Index (CPI) rose by 5.3% on an annual basis in August 2021 and food inflation by 3.7% in the same period. Beef and veal prices increased by 12.2% and pork prices by 9.8% while prices of poultry such as chicken and turkey rose by 7% year-on-year.

In Canada, meat is the category most impacted by price hikes. According to Statistics Canada, meat prices increased by about 10% over the last 6 months. Grocery prices continued to climb in December, rising 5.7% year over year, the largest annual increase since November 2011. Prices have also increased for fresh fruit (+5.6%), including apples (+6.7%), oranges (+6.6%) and bananas (+2.5%) on a year-over-year basis. This is being driven by unfavourable weather conditions as well as supply chain disruptions.

In the UK, a combination of the Covid-19 pandemic and the ongoing impact of Brexit is causing issues at major ports, slowing down food and drink imports leading to shortages. Retail prices rose by their fastest rate in almost three years in the run-up to Christmas 2021 amid the highest rate of inflation for fresh food in a decade. All shop prices rose by 0.8% in December compared with the previous year, following a 0.3 % increase recorded in November, according to BRC-NielsenIQ Shop Price Index. The increase was driven by a 2.4% rise in food prices in December, compared with 1.1% in November. Fresh food inflation accelerated significantly to 3% in December, more than double the 1.2% recorded in November, the highest inflation rate since April 2013, according to the British Retail Consortium.

Food producers and supermarkets have warned of rising prices because of significantly higher labour costs caused by shortages of factory workers and HGV drivers. Industry experts expect food inflation to continue to rise to about 5% during 2022 as companies face higher raw material costs. They also expect a steep increase in the cost of sourcing products from overseas because of a tenfold surge in shipping costs and extra administrative pressures since Brexit.

What are the underlying causes?

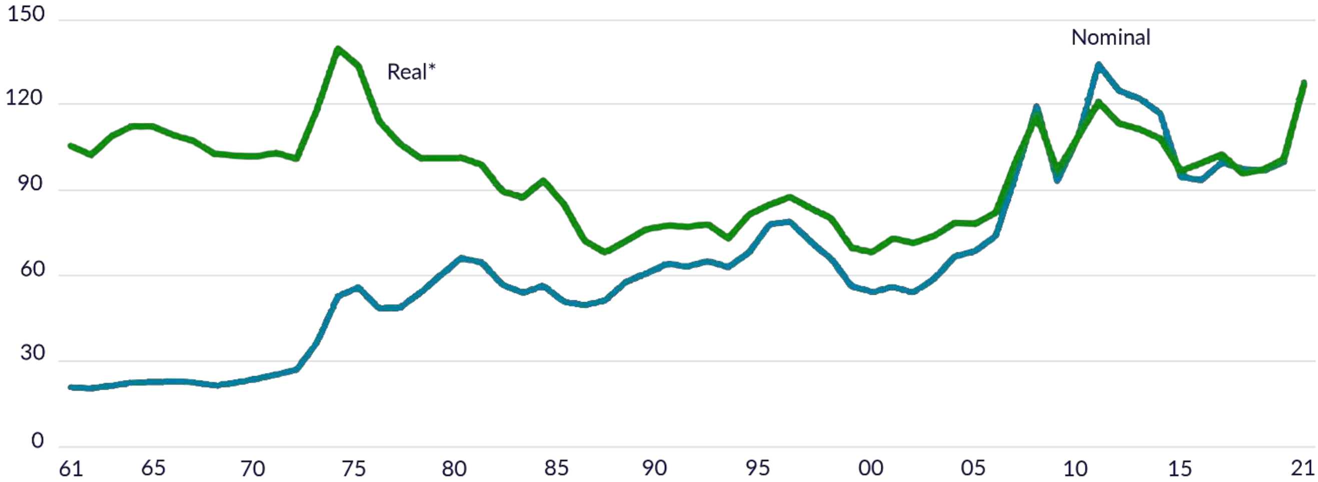
Four main factors are driving the current rise in food prices:

- A shortage of labour;
- A shortage of food due to reduced agricultural production and supply/demand imbalances;
- Rising commodity and input prices;
- Limited supply chain capacity.

Recovering demand and severe labour shortages across food manufacturing, agriculture, warehousing, distribution and hospitality have led many firms to increase wages, which can be expected to feed through into prices in the months ahead.

In the U.S. supply bottlenecks include high feed costs, logistics problems and labour shortages. The White House is also blaming a lack of competition in the meat supply chain. Other causes of price instability include extreme weather, particularly heat and drought that have curtailed crop yields over the last year.

FAO Food Price Index in nominal and real terms



**The real price index is the nominal price index deflated by the World Bank Manufactures Unit Value Index (MUV)*
Source: FAO

According to Nestle soybean oil prices in August 2021 were 80% up on the same time last year due to a poor U.S. soy crop in 2020. There was also a surge in exports along with COVID outbreaks at meatpacking plants, and finally, volatile consumer eating patterns amid the difficulties of the health crisis also had an impact.

Ben Brown, Agricultural and Applied Economics Senior Research Associate, University of Missouri, attributes rising prices primarily to higher fuel prices and trucker shortages, recovery from the pandemic and the rising cost of plastic and aluminium containers.

Travel restrictions due to Covid-19 impacted the availability of farm labour during 2020/21. For example, Australian farmers rely on seasonal workers from the Pacific Islands to supplement their harvest workforce. Farmers in some Australian states reported having no way of accessing this supplementary workforce this year. In the UK supply bottlenecks and lorry driver shortages even led to milk being dumped and a cull of pigs due to staff shortages in the meat processing sector.

No sign of prices easing

As the Covid-19 pandemic persists and impacts on supply continue, there is no sign of prices easing.

Greggs, a UK food-to-go retailer, said its costs were rising due to government-mandated hikes to the minimum wage and rising prices for ingredients. According to outgoing CEO Roger Whiteside:

This year is a more challenging year than most because you've got inflation coming at you from both the ingredient side and from the labour side.

The end of cheap food

What are the long-term prospects for food prices? World food prices were relatively constant from 1985 to the early 2000s but spiked in the period 2008-2012, which led to well-publicized food shortages. According to Canadian analyst Dr Sylvian Charebois:

We're slowly departing an era of cheap food. Instead of seeing households spend say 9 or 10% of their budget in Canada-- in the U.S. it's actually much lower than that, but in Canada it's about 9-10% - you could see that percentage go to 12, 13, even 14% in a few years from now.

Future considerations

Prices have risen again due to the pandemic and other supply disruptions and this is not likely to ease soon. The Covid crisis has exposed major weaknesses within food supply chains. Higher food prices and labour shortages will accelerate trends towards increased investment in AgTech and automation.

However, for those sectors which are reliant on skilled manual labour and where automation is not feasible, wages will undoubtedly have to rise. Logistical issues and higher fuel costs may drive retailers to look for shorter supply chains, and some farmers will look at selling directly to the consumer.

Higher commodity and food prices will also lead to food security moving back up the political agenda alongside the need to produce food more sustainably.

Expert insight

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