WEEKLY OUTLOOK
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CONSUMER DEMAND AND FOOD PRICES

CONSUMER DEMAND IN THE ECONOMY essentially is determined by incomes and prices. The nominal income (unadjusted for inflation) in the United States has been growing consistently for years. Over the last decade, the growth rate has averaged 9.9 percent per year. However, these gains are somewhat illusory. The growth of real income (adjusted for inflation) has averaged only 3.4 percent per year since 1969. During one of those years, 1974, real income actually declined by about 1.5 percent.

Within the last year and a half, concerns about income levels and prices have increased in the public's mind. Since the first quarter of 1979, real disposable income per person in the United States has decreased by 2.5 percent, despite nominal increases in income in each of the 6 quarters since then totaling 10 percent. The problem is that the general price level as measured by the consumer price index has increased by about 21 percent. The result is that as real income declines, the ability of consumers to purchase goods is also reduced.

Within the larger concern about incomes and prices, the mass media often portray increases in food prices as one of the primary culprits in the level of inflation and in the erosion of income. Food prices have increased substantially during the last several years and are likely to continue to do so. In 1978, consumer prices for food rose 10 percent; in 1979, 9 percent. By the end of this year the rise in food prices is expected to be another 9 percent. The USDA is projecting an increase of 10 percent for 1981.

Each of these increases in food prices needs to be considered in the context of overall inflation to determine the degree of responsibility food prices have in eroding income. The consumer price index for all items increased 7.6 percent in 1978, 11.4 percent in 1979, and is expected to increase by over 12 percent in 1980. Food's contribution to these increases is determined by its own price increases and by the proportion of the consumer's budget allocated to food.

Consumers spend about 18.8 percent of their income on food. This proportion has been relatively stable since the late 1960's although it edged up slightly during the 1970's. Based on that proportion, a rise of 10 percent in food prices represents 1.9 percentage points of the overall inflation rate. Thus, in 1978 when food prices rose by 10 percent, that rise contributed about 1.9 percentage points to the overall inflation rate of 7.6 percent, or 25 percent of the total. In 1979 and probably in 1980, the situation is reversed, with food-price increases contributing less than their budget share (18 and 15.9 percent, respectively) to the general inflation rate.

Other items contribute to the general inflation rate, too, as measured by their weight in the budget: housing, 29 percent; transportation, 18 percent; fuel and utilities, 6.5 percent. Clearly, these items have been and will continue to be significant in terms of the general rate of inflation, along with food.

In summary, general consumer demand in the economy is largely controlled by income levels. In turn, income is influenced by inflation as well as other factors. The relative stability of food expenditures as a proportion of the consumer budget indicates that increases in food prices have not altered consumer demand for other items in the budget in a major way, on the average. However, they are a significant contributor to the overall rate of inflation.

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