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Winners and Losers in the Grocery Industry from Deflation

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We're in the midst of one of the longest periods of food price deflation in more than 50 years. USDA reports that the consumer price index has been negative on a year-over-year basis since December 2015, causing severe pressure on same-store sales growth. Retail beef prices have declined in some areas by nearly 8 percent, with pork and poultry on a similar (but slightly less steep) downward trend. USDA predicts we could see up to a 19 percent decline in the CPI for eggs in 2016, and the dairy sector is in dire enough straits that USDA Secretary Tom Vilsack has authorized two rounds of government purchases of surplus cheese. It doesn't look like this trend is likely to let up in the near future.

This certainly is not the first time that the industry has had to face declining food prices, but an interesting plot twist this time around is that this deflationary period is taking place during an economic recovery, not during a recession. This is creating some unique winners and losers across the supply chain.

Winner – Consumers
The biggest winners are consumers, who are experiencing lower prices on a host of products. There have been stories around the country of eggs selling for a dollar a dozen and other deals that seem too good to be true.

Winner – Retailers That Can Work With Consumers to Tell a "Savings Story"
Retailers are finding that they need to be aggressive in working with consumers to help them take advantage of price savings. Retailers who can tell a strong savings story with their customers will clearly emerge from this deflationary period stronger.

Loser – Retail Margins
This round of deflation has its roots in farm country, but farm production only accounts for about 15.9 percent of the average food dollar, and this number decreases as the role of food processing in a finished food increases (see infographic).

Operating a grocery business is vastly different than it was a decade ago with an onslaught of new competitive channels, a cantankerous regulatory environment and the fact that food shopping has become a team sport among households, making it more difficult to pinpoint your customers. Some retailers are pushing prices even lower as a means to drive traffic into their stores. The end result is that already tight margins are being decimated.

Loser – Farm Country
Even as retailers struggle to address the impact of deflation on their margins and the industry as a whole, they cannot afford to ignore the longer term effects on farm country. Whenever this period of deflation comes to an end, the supply chain is likely to look different than when it started.

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