Box 7
Recent developments in euro area food prices

Developments in food prices have reinforced the pattern of euro area inflation driven by energy prices in recent quarters. This holds in respect of both the decline in the contribution to headline inflation in 2014 and its rebound during the first few months of 2015 (see Chart A) – a pattern of decrease and recovery visible in prices of both unprocessed and processed food. As food price inflation can be subject to considerable volatility, this box examines the factors behind recent developments in order to gain a better understanding of the rebound.

Recent movements in unprocessed food price inflation are largely explained by developments in fruit and vegetable prices. These account for most of the decline in the annual growth rate (from around 5% in mid-2013 to a historic low of almost -3% in mid-2014) and most of the rebound to positive growth rates (of around 2% in mid-2015; see Chart B). Seasonal factors typically play an important role here. Much of the decline in fruit and vegetable prices in early 2014 reflects the mild winter of 2013-14 in conjunction with the unwinding of earlier upward impacts resulting from adverse weather conditions. The rebound to positive annual growth rates in the first half of 2015 thus reflects both the relatively subdued price developments one year earlier and the relatively strong price movements in 2015 (see Chart C).

Recent movements in processed food price inflation are explained by different factors. First, the upturn in early 2015 partly reflects a somewhat larger contribution from tobacco prices, which are often subject to the impact of tax measures (see Chart D). Second, like energy prices, processed food prices can be heavily influenced by developments in international commodity prices. Nevertheless, for the euro area, EU internal market prices measured at the farm gate rather than international commodity prices are typically more relevant for the pass-through to consumer food prices. Both international food prices and EU internal

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**Chart A**
Contribution of food price developments to HICP inflation

(annual percentage changes; percentage points)

![Chart A](image)

Sources: Eurostat and ECB calculations.
Note: Latest observations are for August 2015 (flash estimates).

**Chart B**
Unprocessed food price inflation

(annual percentage changes; percentage points)

![Chart B](image)

Sources: Eurostat and ECB calculations.
Note: No breakdown is yet available for the latest observations, which are for August 2015 (flash estimates).
market prices (see Chart E) have declined since 2014 and showed tentative signs of stabilisation in early 2015. Downward pressure on commodity prices and also prices of processed food continues to come in particular from the respective dairy components, which are currently also subject to special influences. Barring further decreases in commodity prices, a fading out of such factors should make the rebound in processed food prices more sustained.

A special factor currently affecting food price inflation (both in terms of unprocessed and processed food products) is the Russian ban on imports from the European Union. The Russian ban became effective in mid-2014 and may have prevented a stronger recovery in food prices. Indeed, anecdotal evidence at the time pointed to a negative impact on prices of unprocessed food such as apples and processed food such as dairy products. However, the European Commission responded by activating support measures for perishable fruit and vegetables which may have mitigated the downward pressure on prices resulting from an excess supply of such goods.\(^1\) The extension of the Russian embargo and the mitigating support measures should continue to dampen prices of unprocessed foods.

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\(^1\) In early August 2014, in line with the Common Agricultural Policy (CAP), the European Commission announced emergency market support measures for perishable fruit and vegetables, which have been used to purchase fruit and vegetables at full price from farmers, or to compensate them for not harvesting their produce. On 30 July 2015 these measures were extended for another year, until 30 June 2016.
The expiration of EU milk output quotas in March 2015 is a special factor that has affected prices of dairy products in particular. During the past few years, in anticipation of the abolition of these quotas, EU dairy farmers increased their production for world export markets and thus raised their exposure to changes in global demand. Presently, increased competition and excess supply in the wake of lower demand from Russia and some emerging economies are weighing on prices. If there is no pick-up in global demand, some of the downward pressure on food price inflation may fade only gradually.

Overall, rising food prices contributed to the rebound in inflation in early 2015 supported by significant base effects. Food price inflation, however, remains rather low by historical standards. Special factors, such as the Russian ban on EU food imports, the oversupply of dairy products stemming from the abolition of milk quotas and lower than expected global demand, are presently limiting increases in food prices.