

Box 5

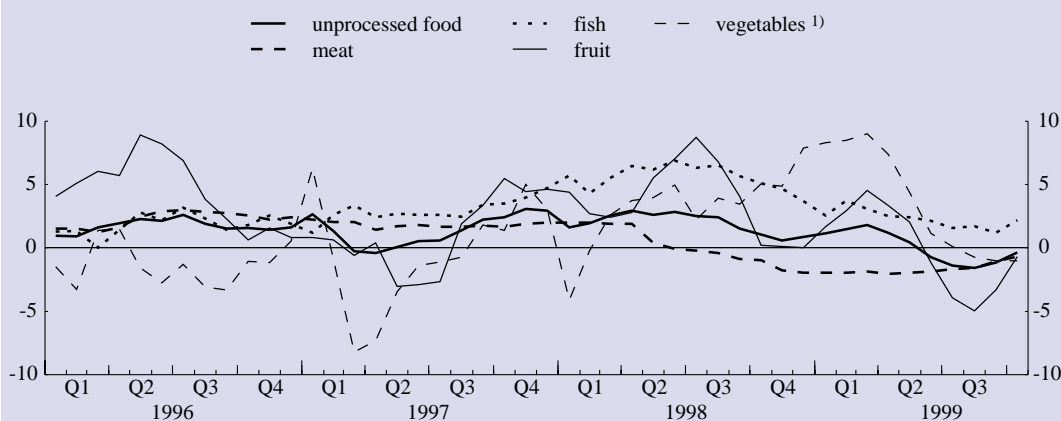
Recent developments in unprocessed food prices

In the recent past the development in the Harmonised Index of Consumer Prices (HICP) has often been strongly influenced by its two most volatile components, unprocessed food and energy prices (see Chart 10 in the main text). Since the beginning of this year the annual rate of increase in energy prices has risen continuously as a result of the ongoing increases in the world market price of oil. However, the upward effect of the energy price increases on the HICP has partly been counteracted by the slowdown in the rate of increase in services and non-energy industrial goods prices; however, unprocessed food prices have also played an important role. The development in energy prices and their relation to the substantial swings in the world market price of oil in recent years have been commented upon extensively in previous issues of the ECB Monthly Bulletin (see, in particular, Box 2 entitled "The effect of oil prices on the Harmonised Index of Consumer Prices (HICP)" in the September issue). In turn, this box provides more information on developments in unprocessed food prices and their underlying determinants.

Unprocessed food prices account for 9% of the euro area HICP, i.e. a figure broadly similar to the weight of energy prices. Unprocessed food consists of four sub-components, of which meat prices are the most significant (4.6% of the area-wide HICP). The remaining three, known collectively as seasonal food, are vegetable prices, which have a weight of 1.8%, and fish and fruit prices, which both have a weight of 1.3%. Seasonal food prices are far more volatile than meat prices (see the chart below). For analytical purposes, it can be useful to examine a measure of consumer price developments which is not distorted by the erratic movements in seasonal food.

The unprocessed food price index and its components

(annual percentage changes; monthly data)



Source: Eurostat.

1) Including potatoes and other tubers.

The year-on-year decline in unprocessed food prices slowed from 1.6% year-on-year in August to 0.4% in October 1999 due to developments in fruit and meat prices. While no upward movement has yet been recorded, the steep decline in the annual rate of change in vegetable prices since March 1999 appears to have come to an end.

Factors underlying the recent development in unprocessed food prices

Vegetable and fruit prices are generally strongly influenced by weather conditions and the strong decline in the rate of increase in these prices in mid-1999 reflects favourable weather conditions in the euro area as a whole. The level of the vegetable price index generally falls between April/May and August with the arrival of

a new harvest, while the level of the fruit price index tends to fall between June/July and October/November. This year, however, the seasonal decline in the price level of both indices was stronger than on average during the previous four summers. Meat prices, on the other hand, are to a larger extent determined by developments in world demand, and the sustained year-on-year decline since early 1998 relates, in particular, to a series of public health scares which have shaken consumer confidence in meat products in a number of countries in the euro area. In addition, a downturn in the external demand for meat products may also have contributed to the decline in meat prices. However, supply factors (increased competition resulting from the efforts of some producers to regain market shares for pork which were lost as a result of earlier cases of disease) could also have played a role. Finally, enhanced competition at the retail level has been cited as a factor behind the recent weakness in unprocessed food prices. The general downward trend in the rate of increase in processed food prices during 1999 provides some support for this view.

The outlook for unprocessed food prices depends on factors such as consumer demand, weather conditions and other seasonal factors and developments in market structure, which are difficult to quantify, e.g. the intensity of retail competition. However, in the months ahead, as meat prices appear to be recovering and the unusually strong seasonal decline in fruit and vegetable prices is not likely to persist, the negative contribution from unprocessed food is expected to decline gradually and may even become positive.