

March 11, 2021

## Ranking Retail Performance Across Proteins in 2021 and Beyond

It was about a year ago when some of the initial panic buying began at retail. It was undeniable to expect a massive shift from foodservice to retail, but no one could predict its magnitude or how long it would last.

Price volatility was yet another evident and anticipated outcome of the pandemic's initial disruption. However, many did not expect protein prices at the wholesale level to remain strong throughout the year. An initial industry assumption suggested that the high price levels reached by production disruptions and strong retail demand would have been offset by the lows caused by the abrupt contraction in the foodservice, entertainment, and hospitality industries. Of course, this assumption varies based on each product and its relative exposure to retail versus foodservice. Therefore, we will remain as general as possible throughout this assessment.

Historically, price variations in the wholesale market are generally passed on to consumers at the retail level. For example, a quick analysis on egg prices found that, on average, every 10% change in wholesale prices results in nearly a 4% move in retail prices within 4 to 6 weeks.

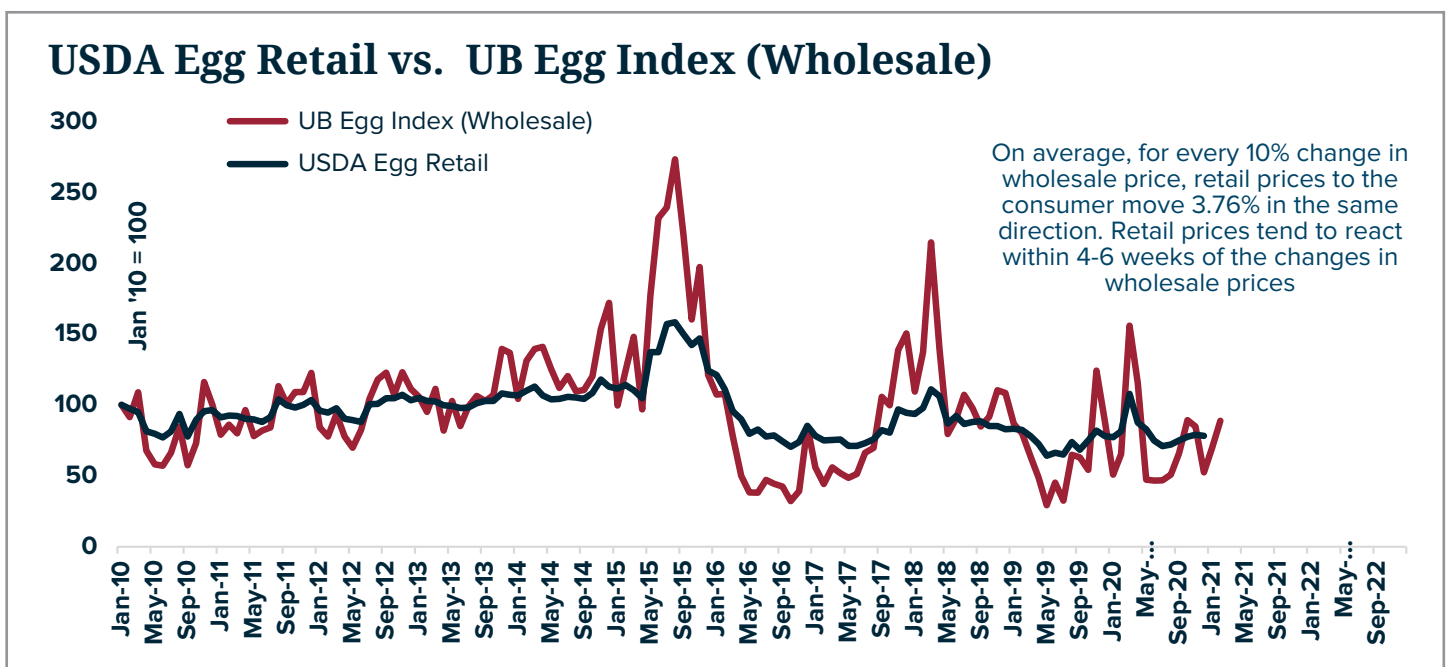


Figure 1. Wholesale and retail prices indexed at 100. Source: USDA, Urner Barry, UB Consulting.

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Again, the magnitude of these variations diverges widely not only by protein but also by specific parts or cuts and different time lags. Last year, prices at the retail level rose for all main land-based animal proteins, while wholesale prices rose for all except chicken and the two main seafood items, shrimp and salmon.

It is essential to remind ourselves that the wholesale and retail markets are co-dependent on each other. Sustained undesirable events, like wholesale price volatility or low margins, can have adverse long-term effects as these are usually passed on to the consumer through relatively higher prices. For example, taking simple retail ratios to wholesale prices, we noticed how retailers enjoyed record-high levels for pork and chicken but remained somewhat steady for eggs and beef. Despite the potential to interpret this in many ways, the bottom line is that consumers had the income to absorb price increases, regardless of what happened to prices at the wholesale level. Still, historical data suggests that large and sustained price gaps between wholesale and retail are not sustainable in the long run.

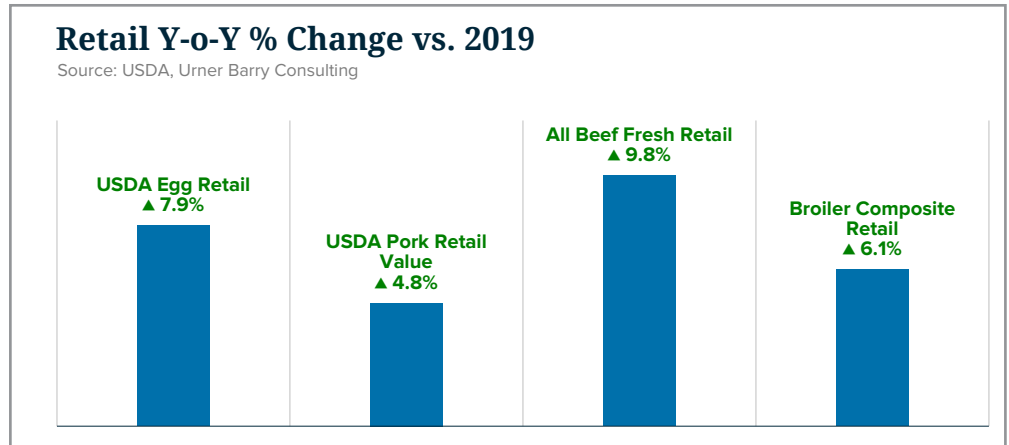


Figure 2. USDA's retail prices. Percent change of yearly average prices from a year ago.

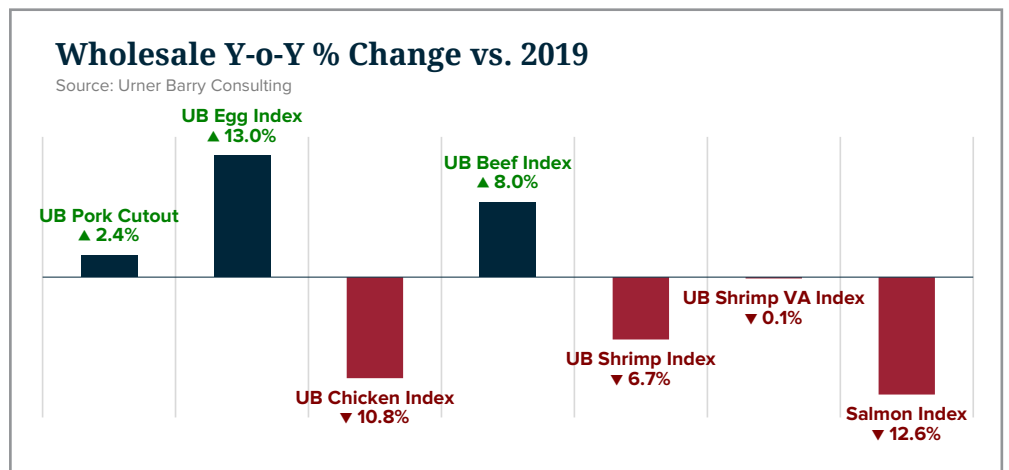


Figure 3. Wholesale prices illustrated using Urner Barry's Wholesale Price indices.

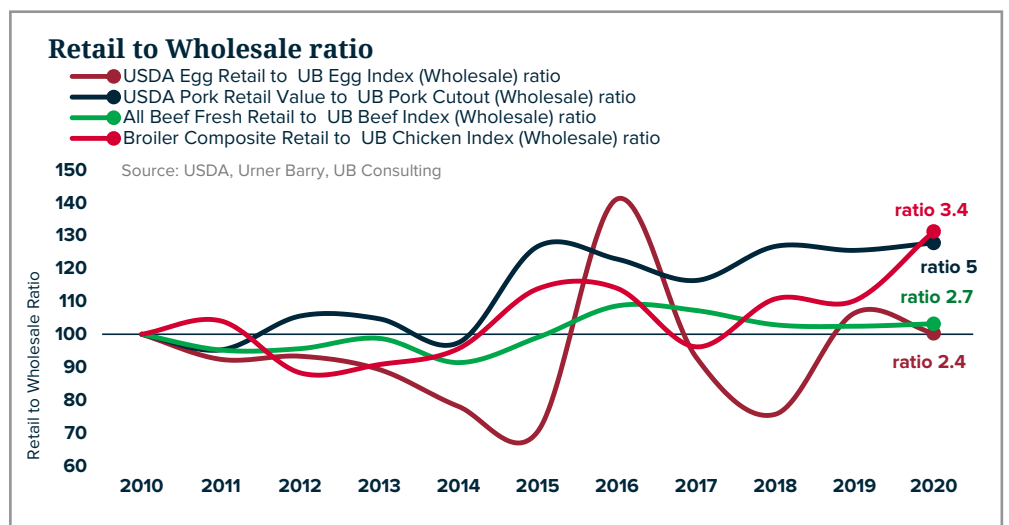


Figure 4. Retail to wholesale price ratio, indexed 2010 = 100. Source, USDA, Urner Barry, UB Consulting.

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Our initial hypothesis suggested that as consumers' income shrank, protein consumption would trade down towards the lower-priced proteins. We saw this first-hand at the pandemic's initial stages when wholesale egg prices shot up to record highs primarily due to strong retail demand. Yet, we believe that despite persistently high long-term unemployment figures—particularly in the foodservice, entertainment, and hospitality industries, which accounts for about 10% of the labor workforce—the injection of money into the system through emergency unemployment benefits helped protein consumption remain relatively intact. For instance, shrimp sales at the retail level remain at significantly higher figures than a year ago, while both wholesale and retail ribeye prices managed to reach a seasonal record high in Q4 of 2020. We can see this through a clear bump in the consumer price index for food at home, and more specifically, meat, poultry, fish, and eggs. Also, food prices away from home, which includes the foodservice prices to the consumer, rose.

Disposable income moved up and remains relatively high, mainly due to the government's cash injection to the system and the fact that air-travel expenditures, sporting events, and other similar activities remain contracted.

As vaccine rollouts continue, some reports suggest the U.S. could reach herd immunity by around September 2021. Also, another injection of government relief money in the system should help the economy buffer the pandemic's persistent adverse effects, particularly for the estimated 10 million-plus workers who remain unemployed.

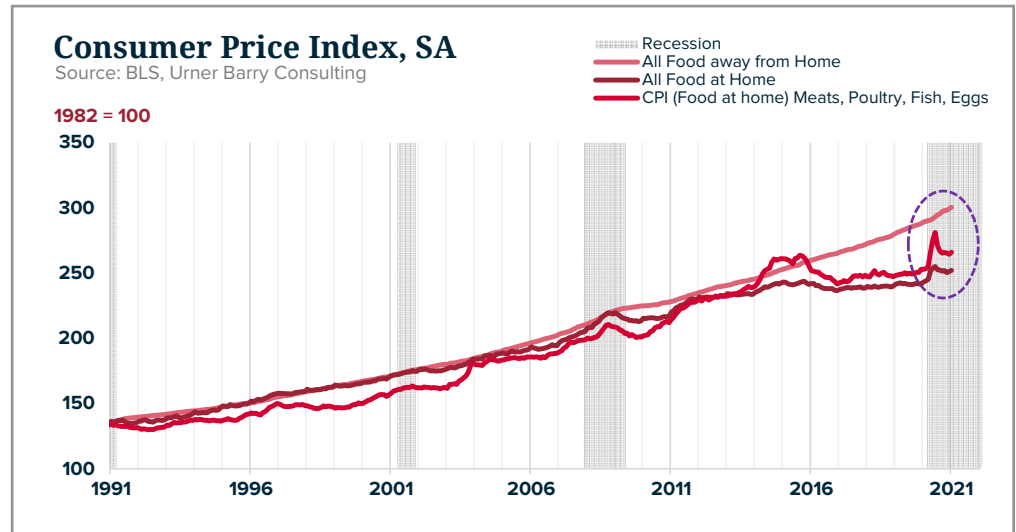


Figure 5. Consumer price index for food away from home and food at home for meats, poultry, fish and eggs. Seasonally Adjusted. Source: BLS, UB Consulting.

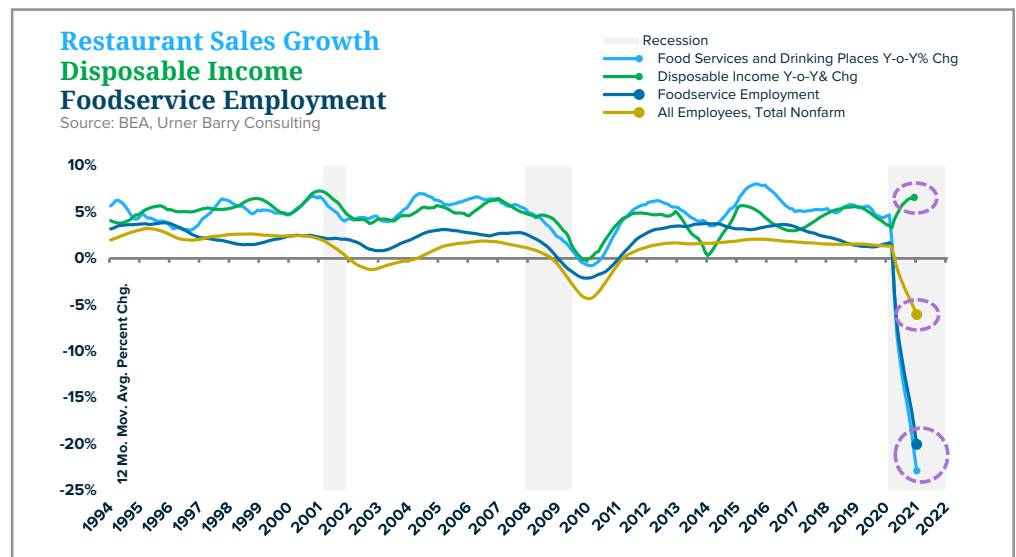


Figure 6. Restaurant sales growth and disposable income, y-o-y chg., 12 month moving average. Source: U.S. Census, BEA, BLS, UB Consulting.

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However, we must consider that inflation fears in the economy as a whole continue to mount. These fears are rooted mainly due to the potential of a shock-like effect from the economy re-opening, and naturally, by the above-mentioned large government stimulus. Inflation is quite relevant to our industry, given that when macroeconomists reference it, they usually exclude food and energy prices due to their volatile nature. And in this case, food inflation in 2021 could persist due to a pent-up consumer demand even after record high (or near-record high) prices to consumers last year.

All these indicators, in hindsight, make sense of why prices at the retail level have remained strong. Less elastic consumer demand at retail, in addition to higher wholesale prices, at least for beef, pork, and eggs, pushed prices to a record level for consumers.

UB Consulting’s revised predictions made last June were for retail sales to grow between 12% and 17% and for foodservice to contract anywhere between 14% and 24% in 2020. Actual seasonally adjusted figures came in at about 19% contraction for foodservice and an 11% growth in retail in 2020. The predictions for 2021 have a much wider range given the uncertainty surrounding vaccine rollouts. In the best-case scenario, we expect as early as late March or early April for foodservice sales to begin improving considerably and for retail sales to remain strong throughout the year.

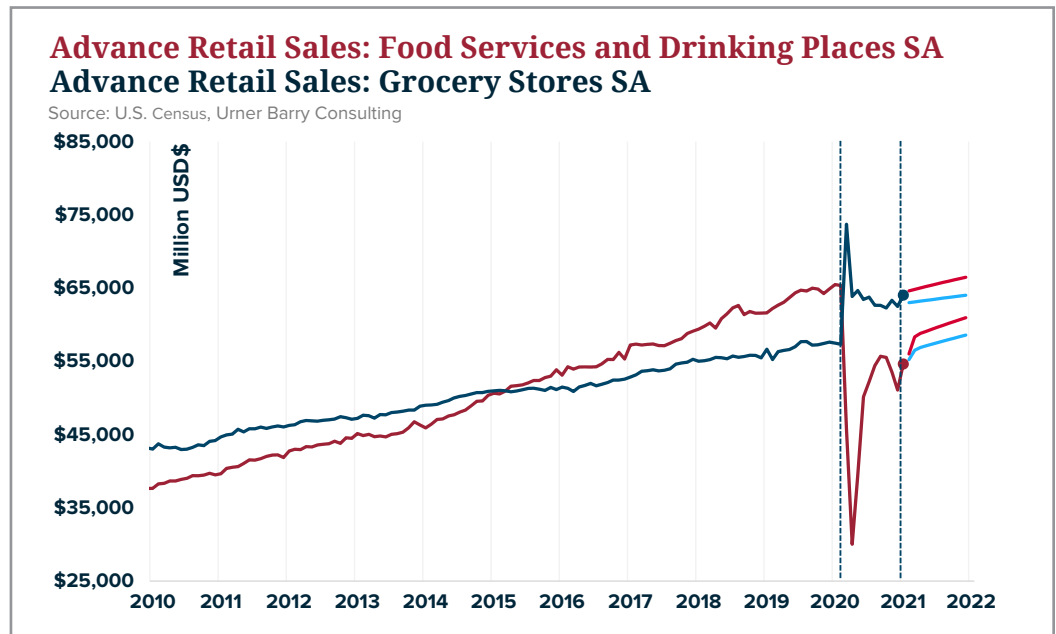


Figure 7. Retail sales for foodservice and grocery stores, seasonally adjusted. Source: U.S. Census, Urner Barry Consulting.

While retail has carried significant weight in protein industry sales throughout the pandemic, much will also depend on how these other essential sectors recover throughout 2021.

For now, we remain cautiously optimistic that the recovery trend will be positive, whether it is swift or gradual, through 2021 and into 2022. Data from 2020 will, however, prove rather useful when analyzing prolonged market shocks in the future.