Rising Energy and Food Prices: Effects on Families

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Issue Statement

The cost of living – measured by the Consumer Price Index – rose during the past 12 months at the fastest pace since 1991. The July 2008 price increases reflected, in part, rising food prices and the surge in energy costs that pushed crude oil and gasoline prices to record highs. Although crude oil prices have dropped recently, this steady rise in energy prices continues to ripple through the economy. Many agree that while consumer prices may rise quickly, they tend to come back down more slowly. Since most families' incomes are not keeping pace with rising costs for everything from food to gasoline, many are facing hard choices – especially those at the bottom of the income ladder. The purpose of this paper is to review recent trends in consumer prices and the effects on families' abilities to make ends meet.

Situation: Rising Prices and Stagnant Wages

Rising Prices

The Consumer Price Index was 5.6 percent higher in July 2008 than in July 2007 (Table 1). This average change masks higher price increases in two important expenditure categories: food (5.8 percent) and transportation (13.4 percent). The special energy index includes items that cut across expenditure categories. For example, natural gas which is a component of housing and gasoline, a transportation expenditure are included in this index. The food index excludes

Table 1. Consumer Price Index for All Urban Consumers (CPI-U)

Expenditure Category	Relative importance, December 2007	% change 12-mos. ended July 2008 (unadjusted)
All items	100.0	5.6
Food and beverages	14.9	5.8
Housing	42.4	3.9
Apparel	3.7	.8
Transportation	17.7	13.4
Medical care	6.2	3.5
Recreation	5.6	1.7
Education and communication	6.1	3.7
Other goods and services	3.3	4.0
Special indexes:		
Energy	9.7	29.3
Food	13.8	6.0
All items less food and energy	76.5	2.5

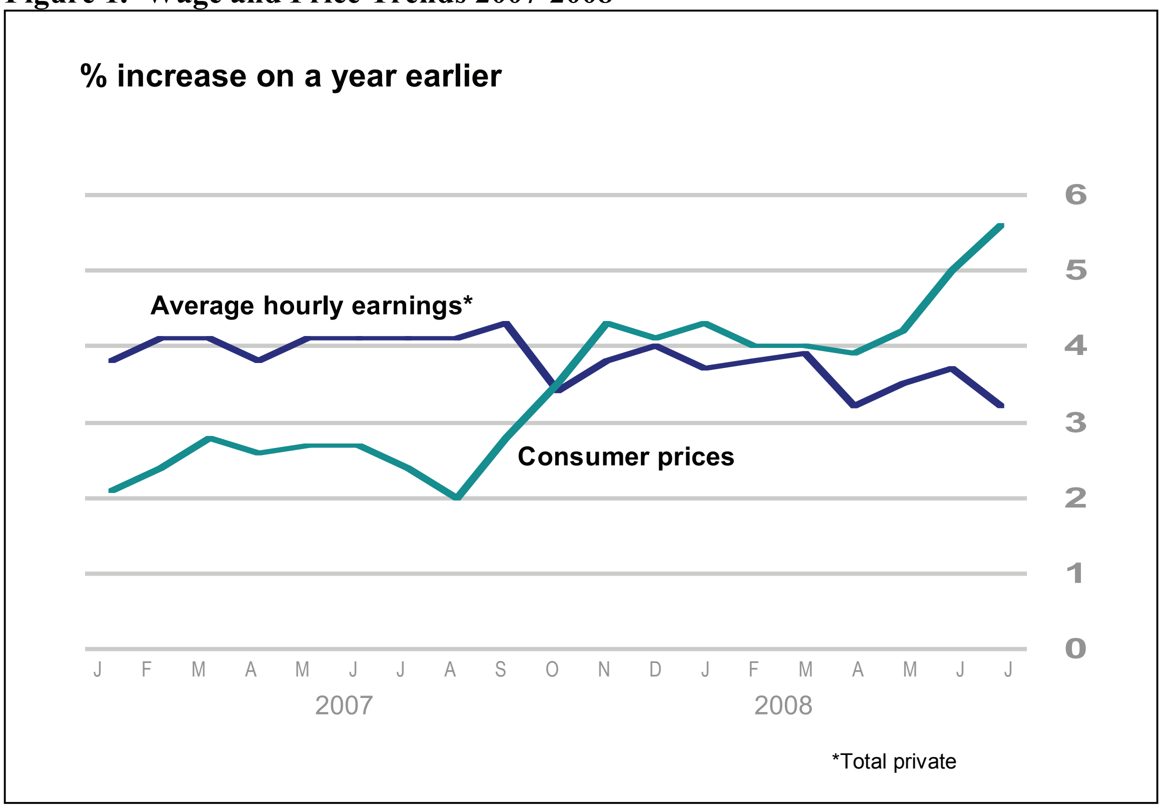
Source: Bureau of Labor Statistics

alcoholic beverages which are a component of the food and beverages expenditure category. The energy index rose nearly 30 percent and the food index jumped 6 percent in the 12 months ending in July 2008. The "relative importance" of each expenditure category can be interpreted roughly as the average share of total consumer expenditures. Because energy and food represent significant shares of consumer spending – about 10 percent and 14 percent, respectively, these price increases over the past year have had a noticeable impact on consumers' purchasing power.

Stagnant Wages

Incomes have failed to keep up with consumer price increases, resulting in a defacto pay cut for the average family. Figure 1 charts the percentage change from the previous year in consumer prices (measured by the CPI) against change in wages from January 2007 to July 2008. Hourly private-sector wages were up only 3.4 percent in the 12 months ending in July, resulting in a real wage decline of more than 2 percent. Families are finding it increasingly difficult to balance their budgets. Credit card debt has grown, banks are now more selective in granting loans, and those on Social Security will receive the highest cost-of-living increase since 1982. Given the weak economy, most workers are likely to find any pay raises in the near future consumed by rising living costs.

Figure 1. Wage and Price Trends 2007-2008



Source: Bureau of Labor Statistics

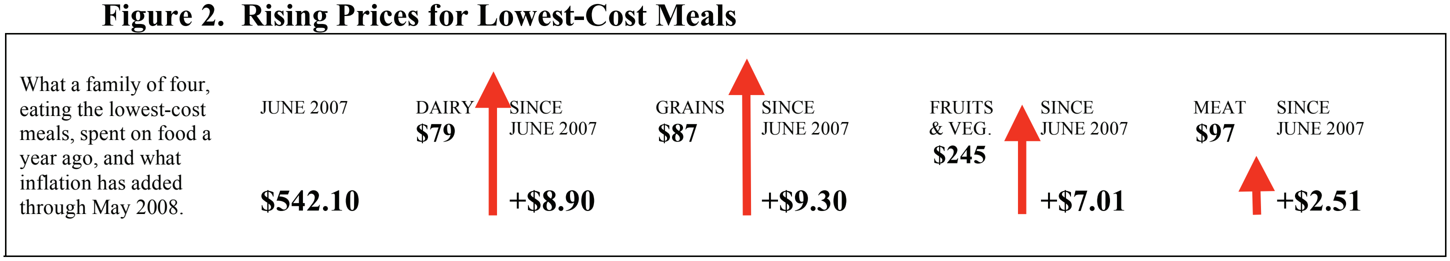
These recent wage data reflect a long-term trend that began during the previous oil crisis. From the end of World War II to about 1973, real hourly pay (adjusted for inflation) for nongovernmental workers rose by about 40 percent. Since then, real wages for these workers, on average, have fallen about 5 percent. The average private worker now earns about $600 per week, not counting benefits; these workers have very little leeway on spending and directly feel the pinch when prices of basic needs rise.

Differential Impacts on Families

Although it is instructive to look at averages, a better understanding of how recent price increases are affecting families comes from a look across the income range. The budget shares consumed by food and fuel vary widely by income. In reality, recent price increases have little impact on those with upper or upper-middle incomes. Using 2006 Consumer Expenditure Survey data to illustrate, families with incomes in the upper 20 percent of the income distribution spend roughly 7 percent of after-tax income on food and about 2.5 percent on gasoline and motor oil. Their food bill would have increased during the past year from about $10,300 to $11,000 and their gasoline expenses would have jumped from $3,500 to $4,900. These families have many options to adjust to price increases – substituting lower-cost foods, reducing the number of restaurant meals, and purchasing more fuel-efficient vehicles.

In contrast, families in the lowest 20 percent of the income ladder spend nearly one-third of their after-tax income on food and about 10 percent on gasoline and motor oil. Their average food expenditures would have grown from about $3,200 to $3,400 and their gasoline bill from about $1,000 to nearly $1,400. Increases in food prices are felt acutely by poor families on food stamps, the federal food assistance program. In the 12 months ending in May 2008, the cost of food for USDA's minimum nutritional diet had risen 7.2 percent, but food stamp allocations have not changed since last fall and will not rise again until October 2008. Figure 2 shows what a family of four, eating the lowest-cost meals, spent on food in June 2007 and the added costs associated with food price increases through May 2008. Given the growing challenge of stretching the food dollar, it is not surprising that local food pantries are experiencing increasing numbers of requests for supplemental food.

Figure 2. Rising Prices for Lowest-Cost Meals



Source: Statistics from the United States Department of Agriculture and the Bureau of Labor Statistics, New York Times, June 22, 2008.

Rising gas prices place similar strains on the poor. Low-income families tend to drive older, less fuel-efficient cars; they don't trade them in as often as higher-income households and can't afford new models that are more efficient. Rural low-wage workers often face long commutes as they find affordable housing in rural communities, but drive long distances to jobs in urban centers. Finding ways to cut fuel bills can be particularly difficult for rural low-income families. Rising food and fuel costs are placing pressures on senior nutrition programs that serve the elderly and frail. Nationwide, nearly 60 percent of the Meals on Wheels programs have lost volunteers who can't afford gas to deliver meals and nearly half of the programs have eliminated routes or consolidated meal services to control costs.

Discussion and Summary

Making ends meet became an increasingly difficult task, especially for low-income families, as prices for food and fuel rose faster than wages in 2007 and 2008. Some upper income families have directly benefited from profits in these sectors of the economy; they also have sufficient discretionary income to absorb costs or implement changes to control spending. In contrast, low-income families are more likely to have real wages or means-tested assistance that fail to keep up with inflation. Attention in the near term should address the unmet needs of those who are bearing the brunt of the rising cost of living. A long-term view suggests that there is an opportunity to explore ways to develop more sustainable lifestyles—adopting healthy food choices, opting for environmentally friendly forms of transportation, and encouraging innovations and public policies that support efficient use of resources. Current discussions of the impacts of rising food and fuel costs can also provide a setting for exploration of the underlying causes of the widening gap between "haves" and "have nots" and a search for solutions at individual, community, national and global levels.