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**Article (Accepted version)
(Refereed)**

Original citation:

Jaravel, Xavier (2018) *What is the impact of food stamps on prices and products variety? The importance of the supply response*. [American Economic Review Papers and Proceedings](#). ISSN 0002-8282 (In Press)

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Available in LSE Research Online: May 2018

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What is the Impact of Food Stamps on Prices and Products Variety? The Importance of the Supply Response

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Do supply dynamics alter the cost-benefit analysis of government transfer programs? Conceptually, government transfers can affect the relative size of different product markets by redistributing purchasing power across income groups with different preferences or by encouraging the purchase of specific products. Theoretically, transfers increasing demand in a market could lead to either higher or lower prices in this market in general equilibrium. In a standard perfect competition environment with increasing marginal cost of production, increased demand should lead to higher prices because the supply curve slopes upward. But with monopolistic or oligopolistic competition, higher demand can lead to lower prices because a larger market size induces innovations, entry of more productive suppliers, and lower markups via increased competition.¹

This paper examines this question empirically in the context of a transfer program in the United States providing benefits to low-income households to help pay for the cost of food. The Supplemental Nutrition Assistance Program, popularly known as the food stamp program, cost over 70 billion in fiscal year 2016 and provided over 40 million Americans (14% of the population) with an average of \$125 per person per month. Hastings and Washington (2010) document that stores increase prices on the specific days when food stamp recipients receive their benefits, which characterizes the effect of food stamps on prices in the very short run. In contrast, I examine the impact of changes in food stamp enrollment on prices and product variety over several years, thus taking into account the

potential response of supply over the long run.

To obtain variation in food stamp transfers plausibly orthogonal to other factors that may affect prices and product variety, I use variation in state policies that were implemented between 2001 and 2007 and made it easier to apply and continue receiving food stamps. As shown by Ganong and Liebman (2017), these policies had a large impact on the take-up rate for food stamps and their implementation across states was not correlated with economic fundamentals such as unemployment.

This research design delivers three results. First, I find that food stamp eligible households experienced relatively lower inflation in states with a larger increase in the take-up rate for food stamps, compared with ineligible households. To assuage potential identification concerns, I show that (i) the negative relationship between inflation and changes in take-up is entirely driven by food product groups with strong local brands, which is consistent with the notion that the pattern results from changes in local demand induced by food stamps; (ii) there is no effect when comparing households in other ranges of the income distribution, such as the middle class relative to high-income households, who are all ineligible; (iii) the results are robust to introducing controls such as unemployment, employment growth and population. The second finding of the paper is that food stamp eligible households experienced a higher increase in product variety in states with a larger increase in take-up. These states are also characterized by a faster decline in retailer margins, which is the third result of the analysis.

I. Sample and Variable Definitions

The analysis is based on three data sources: data on changes in the take-up rate for food stamps between 2001 and 2007 from Ganong and Liebman (2017); scanner data from The Nielsen Corporation; and data on retailer mar-

* I thank Peter Ganong for extensive help with the food stamp data, Mark Duggan for inspiration, as well as Jessie Handbury and seminar participants at Harvard and Stanford for insightful comments. Some of the results in this paper are based on data from The Nielsen Corporation provided by the Kilts Marketing Data Center at The University of Chicago Booth School of Business.

¹See Jaravel (2017) and the references therein for a complete discussion of these mechanisms.

gins for a subset of products in the scanner data.

The number of people on food stamps depends on enrollment procedures which are partly set by states, although food stamps are a federal program. Ganong and Liebman (2017) show that significant variation in the take-up rate for food stamps between 2001 and 2007 came from the introduction of various state-level policies, which made it easier to enroll and continue receiving benefits, for instance with the introduction of simplified reporting, shorter recertification lengths, and interview waivers. Different states adopted different policies, generating variation in take-up. From 2001 to 2007, the average increase in take-up was 10.62 percentage points, with a standard deviation of 6.33 percentage points across states.

To measure the response of prices and product variety, I use the Homescan Consumer Panel dataset from The Nielsen Corporation from 2004 to 2008, which provides barcode-level price data for 125 product groups covering food, alcohol, health and beauty, household supplies and general merchandise in 49 states.² I build a proxy for food stamp eligibility based on household annual income and household size; using this proxy,³ the average share of eligible households in overall spending in the scanner data is 18.64%, with a standard deviation of 4.93% across states.

I measure inflation on continued goods (available across consecutive years) using a CES exact price index, repeating the procedure separately for eligible and ineligible household groups in each state. While inflation for non-eligible households was on average 2.57% per year, it was 62 basis points higher for eligible households (Online Appendix Figure A1 reports the distribution of inflation rates across states and groups).

Next, I measure changes in product variety following Feenstra (1994). For each eligibility group, I compute the share of spending in year

t on goods that are new relative to $t - 1$ (s_t^N) and the share of spending in year $t - 1$ on goods that were discontinued in year t (s_{t-1}^D).⁴ The change in product variety between $t - 1$ and t is given by $s_t^N - s_{t-1}^D$. Repeating the procedure for each eligibility group in each state, I find that the average yearly increase in product variety was 1.03 percentage points larger for ineligible households.

Finally, I measure retailer gross margins for a subsample of barcodes for which data is available on both consumer prices p and wholesale costs c_w in 20 states. The gross margin is defined as $\frac{p - c_w}{p}$ and the average margin is 44.19%.

II. The Price Effects of Food Stamps

This section presents the main result of the paper, the impact of changes in take-up for food stamps across states on inflation for eligible households.

As previously mentioned, the change in food stamp take-up rates varied substantially across states, as different states adopted different enrollment policies (Ganong and Liebman (2017)). These policies generated variation in purchasing power for food products at the bottom of the income distribution, in a way that may be orthogonal to price dynamics across the product space and across states. To test this identification assumption, I implement three falsification tests. First, although in principle recipients could treat food stamps as fungible income, Hastings and Shapiro (2017) show that in practice the marginal propensity to spend food stamp benefits on food products is much higher than on other products; therefore, if there is an effect it should exist primarily for food products. Second, many products are partly non-tradable because of the strength of local brand preferences. The strength of local brand preferences varies across product groups and inflation should respond to changes in local market size induced by food stamps primarily in product groups for

²2004 is the earliest year for which the data is available. Conceptually, starting to measure prices and product variety later than the first year of introduction of the policies (2001) may be desirable because these policies are implemented gradually across states and it may take a few years for suppliers to start responding.

³In fact, food stamp eligibility is primarily determined by a household's *monthly* income and its size; eligibility also depends on additional factors which are not measured in the Nielsen data, such as assets.

⁴A given barcode in a given state is defined as "new" in year t if nobody in that state purchased it in year $t - 1$ (likewise for discontinued products). An alternative is to define a product as "new" for a given eligibility group if nobody *in this group* purchased in year t , but this would introduce measurement error because of the uneven sizes of eligibility groups across states, as pointed out in a different context by Handbury and Weinstein (2014).

which brand preferences are more local.⁵ Third, a similar analysis can be conducted for ineligible households of different income levels to check that the inflation patterns are specific to the recipient population and not a broader feature of inflation across the income distribution. Conceptually, these three tests use subsamples or outcomes for which I expect to find no effect if the identification assumption is valid.

I compare the difference inflation rates of eligible and ineligible households by estimating

$$(1) \quad \pi_{si}^E - \pi_{si}^I = \beta \Delta \tau_s + \alpha_i + \varepsilon_s,$$

where s indexes states, i product groups, $\pi_{si}^{E/I}$ is the average CES inflation rate for eligible/ineligible households in product group i between 2004 and 2008, $\Delta \tau_s$ is the change in take-up between 2001 and 2007, and α_i is a product group fixed effect. Standard errors are clustered by states.

The results are reported in Table 1. Panel A shows that inflation is lower for eligible households in states with a higher increase in take-up (column 1); as expected, the share of eligible households in total spending is larger in those states (column 2). Panel B shows that the effect is entirely driven by food product groups with stronger local preferences. The regression coefficients are precisely estimated zeros for non-food products or food product groups with stronger national preferences. In contrast, the effect is large for food products with local preferences: a 10 percentage point increase in take-up (the average change across states in this period) leads to a 19.8 basis points fall in inflation for eligible households, which is about a third of the overall inflation gap between eligible and ineligible households.

The Online Appendix shows the robustness of these results. Online Appendix Figure A2 depicts the main result graphically. Online Appendix Table A1 shows robustness to the introduction of controls such as unemployment and employment growth (Panel A) and reports that the inflation difference between other income groups is a precisely estimated zero in all parts of the product space (Panel B). Therefore, if

omitted variables drive the results in Table 1, they would have to be specific to food products with strong local brands, not strongly correlated with employment dynamics, and specific to households that are eligible for food stamps.

III. Mechanisms

This section investigates two channels that may explain the fall in prices in response to increasing demand from food stamp recipients: increasing product variety and a fall in retailer margins. Both of these mechanisms were emphasized in Jaravel (2017) when studying the response of supply to changes in the income distribution over time.

Table 2 reports the results for changes product variety. I run a specification analogous to (1) with the difference in the rate of increase in product variety across eligible and ineligible households as the outcome (using the measure defined in Section I). Product variety increases more for eligible households relative to ineligible households in states with a larger increase in take-up. The effect is driven by food products (column 2) and product groups with stronger local preferences (column 4). A 10 percentage point increase in take-up leads to a 14.3 basis point increase in product variety for eligible households, close to 15% of the overall gap in increasing product variety between eligible and ineligible groups. A faster increase in product variety for eligible households has a direct effect on cost-of-living through love of variety, as well as a potential indirect effect through margins for continued products via increased competition.

Table 3 documents the response of retailer margins. I run a specification analogous to (1) at the barcode level, with retailer margin as the outcome. For a 10 percentage point increase in take-up, retailer margins fall by 28 basis points on average (column 1) and this effect is entirely driven by food products (columns 2 and 3). These large effects indicate that it is plausible for increased competition (induced by additional entry) to generate the fall in prices for eligible households documented in Table 1.⁶

⁵To identify product groups with stronger local brand preferences, I use a random effects model as in Jaravel (2017). See the Online Appendix for a complete discussion.

⁶The comparison of the estimates in Tables 1 and 3 is imperfect, because retailer margins are observed in a sample with only 20 states and without information on customer income; but one can see that the estimates in these tables are similar in magnitudes.

IV. Conclusion

This paper documented the effect of expanding food stamp enrollment on prices and product variety over the long-run (several years). There are substantial declines in prices and increases in product variety for eligible households when enrollment (and thus demand) increases, which strengthens the impact of food stamp expansions on the welfare of eligible households. Therefore the long-run supply response to changes in demand from food stamp recipients has a first-order impact on the cost-benefit analysis of the program. Extending the analysis to other government programs and other industries is a useful avenue for future work.

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TABLE 1—THE EFFECT OF CHANGES IN TAKE-UP FOR FOOD STAMPS ON INFLATION

Panel A: In Full Sample				
	Inflation Difference b/w		Share of Eligible HH	
	(1)		(2)	
Change in take-up rate, 2001 to 2007, pp	-0.0078026*		0.206364***	
	(0.0041204)		(0.0757597)	
Product group fixed effects	Yes		Yes	
Observations	4,856		4,856	
Panel B: In Subsamples				
	Inflation Difference b/w Eligible and Ineligible HH, pp			
	Food Product Groups		Non-Food Product Groups	
	Local	National	Local	National
	(1)	(2)	(3)	(4)
Change in take-up rate, 2001 to 2007, pp	-0.0198453***	0.0020867	-0.007024	-0.0097536
	(0.0055633)	(0.0065311)	(0.0085525)	(0.0135336)
Product group fixed effects	Yes	Yes	Yes	Yes
Observations	1,074	1,786	1,160	787

Notes: This table presents the results from specification (1). In both panels, each observation is at the level of product groups by state and all regressions use spending weights. The inflation difference is the average annual difference from 2004 to 2008 between eligibility groups. In Panel B, local and national product groups are defined based on the estimates of the random effects model presented in the Online Appendix. Standard errors are clustered by state. * $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$.

TABLE 2—THE EFFECT OF CHANGES IN TAKE-UP FOR FOOD STAMPS ON PRODUCT VARIETY

	Differential Change in Product Variety b/w Eligible and Ineligible HH, pp				
	Full Sample	Food	Non-Food	Local	National
	(1)	(2)	(3)	(4)	(5)
Change in take-up rate, 2001 to 2007, pp	0.0089079*	0.0143542***	-0.0046595	0.0105038*	0.007025
	(0.0049189)	(0.0048838)	(0.011482)	(0.0058191)	(0.0061231)
Product group fixed effects	Yes	Yes	Yes	Yes	Yes
Observations	2,997	1,979	1,018	1,228	1,731

Notes: This table presents the results from specification (1) with the average change in product variety between 2004 and 2008, differenced across eligibility groups, as the outcome. Each observation is at the level of product groups by state and all regressions use spending weights. In columns (4) and (5), local and national product groups are defined based on the estimates of the random effects model presented in the Online Appendix. Standard errors are clustered by state. * $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$.

TABLE 3—THE EFFECT OF CHANGES IN TAKE-UP FOR FOOD STAMPS ON RETAILER GROSS MARGINS

	Change in Retailer Gross Margins, pp		
	Full Sample	Food	Non-Food
	(1)	(2)	(3)
Change in take-up rate, 2001 to 2007, pp	-0.0289324***	-0.0391377***	0.0106899
	(0.0117693)	(0.0146433)	(0.0290296)
Product group fixed effects	Yes	Yes	Yes
Observations	5,734,840	4,488,368	1,246,472

Notes: This table presents the results from specification (1) with the change in retailer gross margin between 2004 and 2007 as the outcome. Each observation is a barcode by store by year and all regressions use spending weights. Standard errors are clustered by state. * $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$.