

# International Food Price Volatility: Regulating the (Super)-Market

Global prices for wheat have surged nearly 40% since June. This has led to rampant speculation that the world is on the cusp of a global food-price crisis similar to the one in 2007-2008 that sparked food shortages and political unrest in numerous developing countries. Resultant turmoil – 13 Mozambicans were killed in September during riots over bread prices – has further demonstrated that social stability in food-insecure nations can be dramatically shaken by volatility in international food markets.

The former director-general of the International Food Policy Research Institute (IFPRI), Joachim von Braun, blames current price volatility on the lack of effective regulation by global bodies, like the G8. His call for the establishment of “a global architecture for policies on

agriculture and food” has been echoed by senior Food and Agriculture Organization (FAO) officials, who say the G20 must address this issue through “improved regulation of markets...market transparency, and (by) establishing an appropriate level of emergency stocks.” Others specifically blame speculative trading and some simply point to increased global demand for food.

Ergo worked with five experts on international food issues to study the current price volatility, the relationship between the events of recent months and the 2007-2008 food crisis, and the likelihood of major changes to the regulation and administration of international food markets.

## 2007-2008 redux?

While recent events resemble those that presaged the 2007-2008 crisis, experts caution against drawing too many parallels. At that time, surging petroleum prices drove up agricultural production costs and increased demand for biofuel feed stocks, like corn, while unfavorable weather conditions led to production shortfalls in major agriculture-exporting countries. These factors, combined with low agricultural commodity reserve stocks and export bans from major producers, drove prices for numerous staple foods to historic highs. The predictable result was food shortages, and political unrest, in much of the developing world.

**The recent surge in commodity prices, on the other hand, has not been nearly as uniform as the spikes of two years ago.** Experts argue that the most recent volatility has been largely restricted to agricultural commodities where specific events, especially drought in Russia and panic buying (people buying unusually large amounts in anticipation of a disaster), have driven price spikes. Robert Paarlberg, a political scientist specializing in international agricultural issues, says the main difference is that grain stocks are much higher today than they were in 2008. “What we are actually seeing is a response conditioned by the most recent food crises,” he explains. “Panicked buying pushed up domestic prices in Russia in the wake of weather-related events. This is what led to the export restrictions on wheat.”

## Changing Market Fundamentals or Psychology?

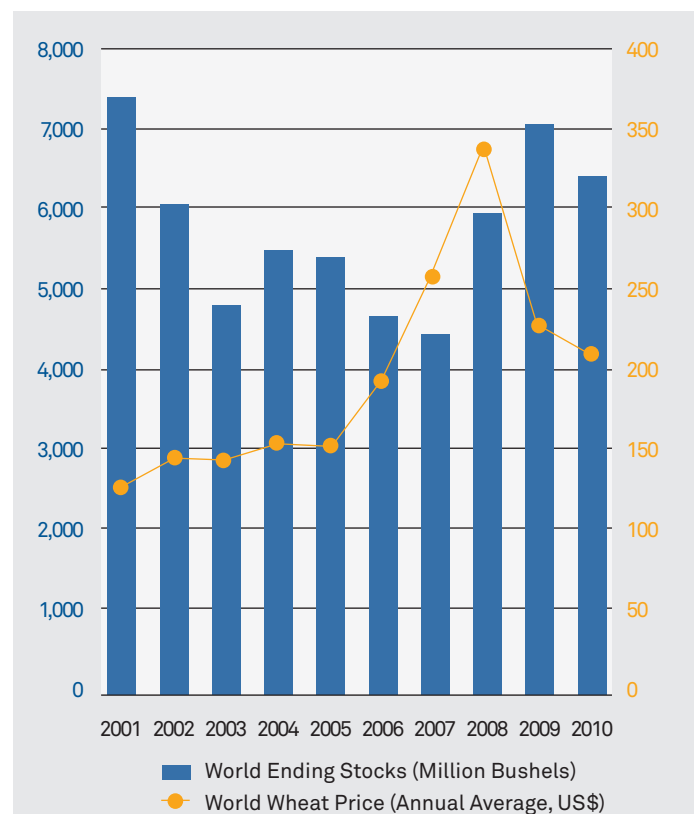
A parallel debate is underway over whether current wheat price spikes reflect a new reality of market fundamentals for agricultural commodities or a ripple effect from 2007-2008. Paarlberg places the blame for the current price volatility squarely on the psychology of market participants; he is optimistic that volatility will ebb as we move further from the shock of two years ago. “What we are seeing now is fear of resumed export restrictions, and as such, **current price spikes don’t truly reflect market fundamentals,**” he explains.

A former executive at the Arab National Bank in Riyadh, Elie Elhadj, disagrees. He believes that **fundamentals are driving the current surge in wheat prices and that volatility is an intrinsic part of commodities markets.** He explains, “The bottom line is that the world population is growing, which is of course pushing demand up. Combine this with climate change and specific weather events and you understand that volatility is built in to these markets.”

## Toward International Food Market Regulation?

The debate over market fundamentals continues, but most experts agree on an important related question: can global bodies effect meaningful changes in international food markets? The consensus: they cannot. Paarlberg says **all we are likely to see from G8 and G20 summits is “aspirational language and little else.”**

GLOBAL WHEAT PRICES AND ENDING STOCKS (2001-2010)



Source: FAO, International Commodity Prices & USDA, Foreign Agricultural Service

The demand to establish mechanisms for insulating consumer nations from price volatility is not new. IFPRI has attempted “to revive the old dream” of an international food reserve that would allay fears of supply security, says Eckart Woertz, Economics Program Manager at the Gulf Research Center in Dubai. “Such an approach has the potential of reducing market overreaction,” Woertz explains, “but it comes with the complementary problem of trying to coordinate market intervention internationally.”

This international coordination is complicated by a yet unanswered question: who will foot the bill? Frederick Crook, a former U.S. agricultural attaché in Hong Kong, says the FAO will continue to advocate for a reserve because “their main constituent countries are importers that want cheap grain.” But he says it is “unrealistic” to think that producer nations will maintain stocks at higher levels solely in order to pass on benefits to consumer nations. These competing priorities mean that international solutions are much less likely to gain traction than national ones. **Elhadj believes the simplest solution is for importer nations “to take it upon themselves to invest in storage” and maintain stocks of staple agricultural commodities.** “They can’t hope for others to help them out of a sense of duty.”

But nationally-focused initiatives come with their own set of challenges, and will not fully insulate consumer nations from price volatility on the international market. Mozambique’s Food Production Promotion Plan, for example, which was intended to build domestic food stocks and decrease reliance on imports, has produced mixed results since its implementation in 2008. Agricultural economist Cynthia Donovan, currently in Mozambique conducting policy research and training at the Ministry of Agriculture, says part of the problem has been the inevitable lag between conception and implementation of the program. This has been exacerbated by what she describes as “a lack of engagement with the private sector and limited human resources capacity.” Donovan predicts, however, that key elements of the plan, such as irrigation improvements and increased food storage capacity, will generate results in future growing seasons and help reduce price volatility.

## ERGO’S VIEW

Despite the promise of Mozambique’s plan, the country will remain highly import-dependent for many years and will continue to struggle with the challenges faced by importer nations around the world. These countries are vulnerable to price fluctuations from all sources, and significant changes to how commodities are priced, stored, and delivered are unlikely in the near future. With concerted international action unlikely, national level solutions are the only workable ones, but they take time to implement. Importer nations remain in need of tools to help protect themselves from the extant volatility in these markets. This need will translate into major opportunities for the establishment of food storage facilities in exporting countries across the supply chain. The clear connection between steady staple food prices and political stability will make these national level solutions far more important, and far more common, for years to come.

*Ergo has conducted numerous studies on the geopolitical implications of recent food security policies and laws as well as the opportunities for investment in agricultural sectors around the world.*