

Why food prices are high

When global food prices shot up in 2008, panic broke out all over the world. Some countries decided to restrict exports so as to be able to feed their own populations. Now, once again, the prices of agricultural produce are high on global markets. Why is this? And is it a bad thing? TEXT KORNE VERSLUIS ILLUSTRATION JENNY VAN DRIEL, WAGENINGEN UR

Food prices are a matter of supply and demand: is there enough food for a growing world population?

Over much of the past 50 years, world food production grew consistently faster than the world population, causing the price of food to plummet. That was until the year 2000 when the trend reversed and prices started to rise – slowly at first and more recently in sudden spurts. Can agriculture no longer keep up with rising demand? On the contrary, believe world food organization FAO and the Organization for Economic Cooperation and Development (OECD). This year they jointly published a forecast until 2021, and they think food production will continue to outstrip the growth in the world population in the decade to come. Growth in food production is set to level off, however – from 2.3 percent in recent decades to 1.7 percent in the coming years – but it will still be sufficient to produce 0.7 percent more food every year per world citizen.



What is the current level of world food prices?

There are several different indicators for world food prices. The FAO and the World Bank both regularly publish statistics, including a food price index based on export prices of a number of commonly traded food crops. Both institutions report that food prices are about as high as they were in 2008. That is twice as high as the average between 2002 and 2004. The World Bank reported record prices for maize and soya this summer.

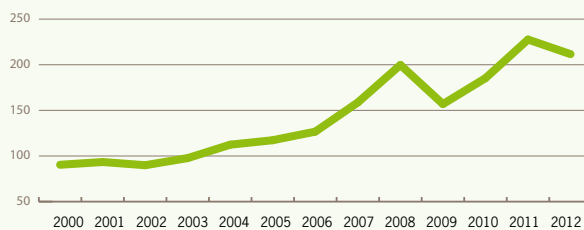


What drives prices up?

According to the World Bank, one of the main reasons for the high prices is an exceptionally hot dry summer in the 'corn belt' in the United States. It has not been as dry in America as it was this summer since the nineteen fifties. And it was not just in the US that the weather was bad, but also in Russia, the Ukraine and Kazakhstan, where the summer was dry and 10 percent less grain than expected was harvested. In anticipation of a short-fall, traders are charging higher prices.

FAO Food Price Index: an indication of relative international world food prices.
2002-2004 = 100.

Source: FAO



Where do you pay 'world food prices'?

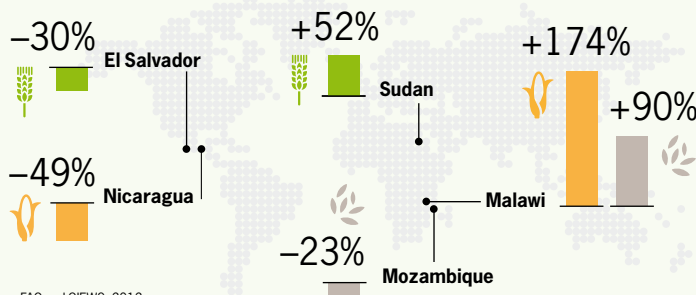
On many local markets there is no sign of the prices set in offices in Rome or Washington. An overwhelming proportion of the food produced worldwide does not come onto the global market but is traded and processed regionally. The price of rice on the world market went up by 7 percent between July 2011 and July 2012, for example; the price of maize rose by 11 percent, and that of wheat by 14 percent. Yet in the same period in Malawi, the price of rice went up, not by 7 but by 90 percent, while in Mozambique it went down by 23 percent. In Malawi you paid not just 11 percent more for maize, but 174 percent more, but in Nicaragua you paid 49 percent less. The price of wheat in Sudan rose during that period by 52 percent, while in El Salvador it dropped by 30 percent.

The local harvest has a much bigger impact on prices than the world market

Changes in the price of food crops

at various locations around the world between July 2011 and July 2012.

Average price change Wheat +14% Maize +11% Rice +7%



Source: FAO and GIEWS, 2012



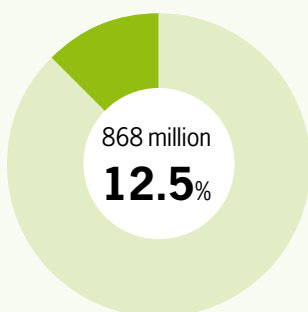


What were the consequences of the price peak of 2008 in the end?

The high prices came in for extra attention in 2009 because the UN reported that the number of people going hungry in the world had risen above one billion, partly due to high food prices. At the beginning of October this year, the FAO adjusted that figure downwards. Further analysis had shown that the price peak had in fact had very little effect on the number of people going hungry. To some extent, this good news could be attributed to the FAO's chosen method of calculation. Hunger levels were overestimated because the model could not handle fast price fluctuations, the organization claimed. But at least as important was the fact that in many countries, such as China, India and Indonesia, the prices during the peak had hardly gone up.

Hunger

Number of people going hungry in the world, 2010-2012. In numbers and in percentage of world population.



Source: FAO, WFP, IFAD. 2012.

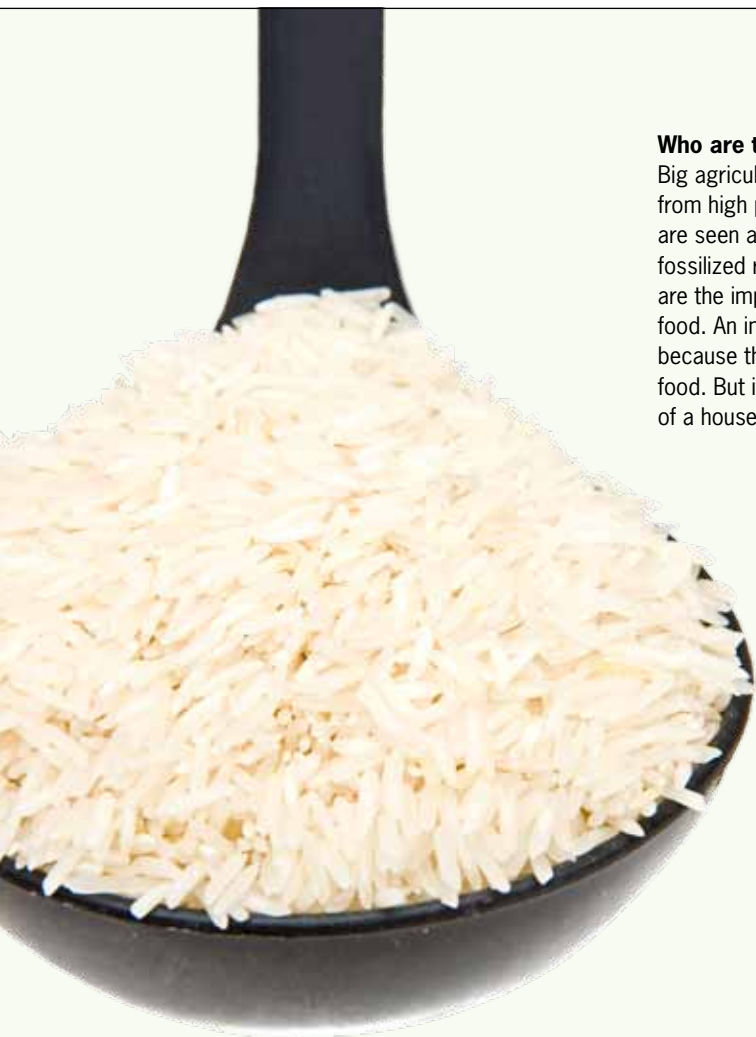
Does speculation play a role?

After the price peak in 2008, several economists said the soaring prices were partly due to speculation and investments. Various financial products in that period offered the opportunity to speculate on rising food prices, and the big influx of money into those funds was said to have driven food prices up. This claim is still controversial among economists. According to the sceptics, investors only confirm existing trends; their money is at stake so they are not eager to speculate on uncertain price rises. The prices, goes this argument, only rise because investors make sure they are well informed about the current situation and base their decisions on that. What is more, say the critics, the proponents of the theory do not differentiate between various different sources of finance. Speculators always go for options and the trade in those has very little influence on prices in the here and now, they argue. It is not yet possible to declare a clear winner of this debate.

And is there such a thing as desirable world food prices?

The experts put out mixed messages about this, said Belgian economist Johan Swinnen in an article published in *Science* at the beginning of this year. After 2005, the FAO sounded the alarm because food prices were too low, he explains. That depressed farmers' incomes, leading to severe poverty. In 2008, the same organization held a summit about the price hikes which, it said, also led to severe poverty. The truth is more complicated, Swinnen explained. High prices are a blessing for farmers but a curse on city dwellers. But, says Swinnen, development organizations only stand to gain from bad news, so that is what they tell. And this trend, he believes, is reinforced by the media, which have a preference for bad news. High prices do create winners too, and they are found in the countryside.

High prices do create winners too, and they are found in the countryside



Who are the victims of higher food prices?

Big agricultural exporters such as Australia, Argentina and the US benefit from high prices. The victims are the importers. For this reason, high prices are seen as one of the causes of the Arab Spring. Latent dissatisfaction with fossilized regimes was ignited by anger at the high price of food. Hardest hit are the importing countries in which people spend most of their income on food. An importer such as Norway is not seriously affected by a price rise, because the Norwegians only spend about ten percent of their income on food. But it is a different story in the Congo or Liberia, where more than half of a household's income goes on food.

Percentage of income spent on food

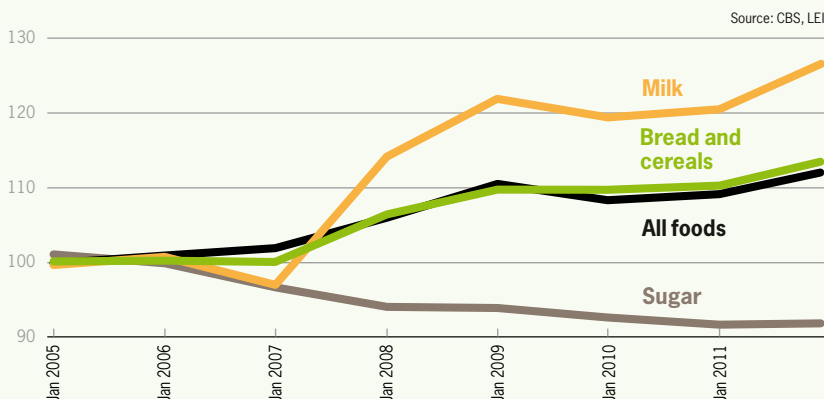


Source: USDA, 2011

Are Dutch consumers paying more for their food?

The world price plays a very modest role in the Dutch supermarket, the LEI shows. The Netherlands is an importer of food such as cereals and soya. However, the prices of most foods rose very little more than the rate of inflation between 2005 and 2011. Sugar even went down in price. And milk, which is produced in the Netherlands, went up in price.

Relative price of foodstuffs in the Netherlands
2005=100



Source: CBS, LEI

What is the influence of biofuels?

LEI Wageningen UR states in a dossier on the high food prices that biofuels are not the main cause of the high prices, but that they do play a role in them. The targets for the use of biofuels in the European Union, the US and Brazil create an increased demand for food crops. The EU obliges oil companies to mix biofuel into their petrol, while in the US one third of the maize harvest is processed into bio-ethanol. In spite of that extra demand, American maize exports were kept up at the same level until last year. So biofuels do not play more than a minor role, according to the LEI. ■

Info: Internet dossier on food security and FAQ on world food prices:
www.wageningenUR.nl/lei/foodsecurity