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# **Do's and Don'ts of Managing the New Food Price Environment in Countries with Food Insecure Populations**

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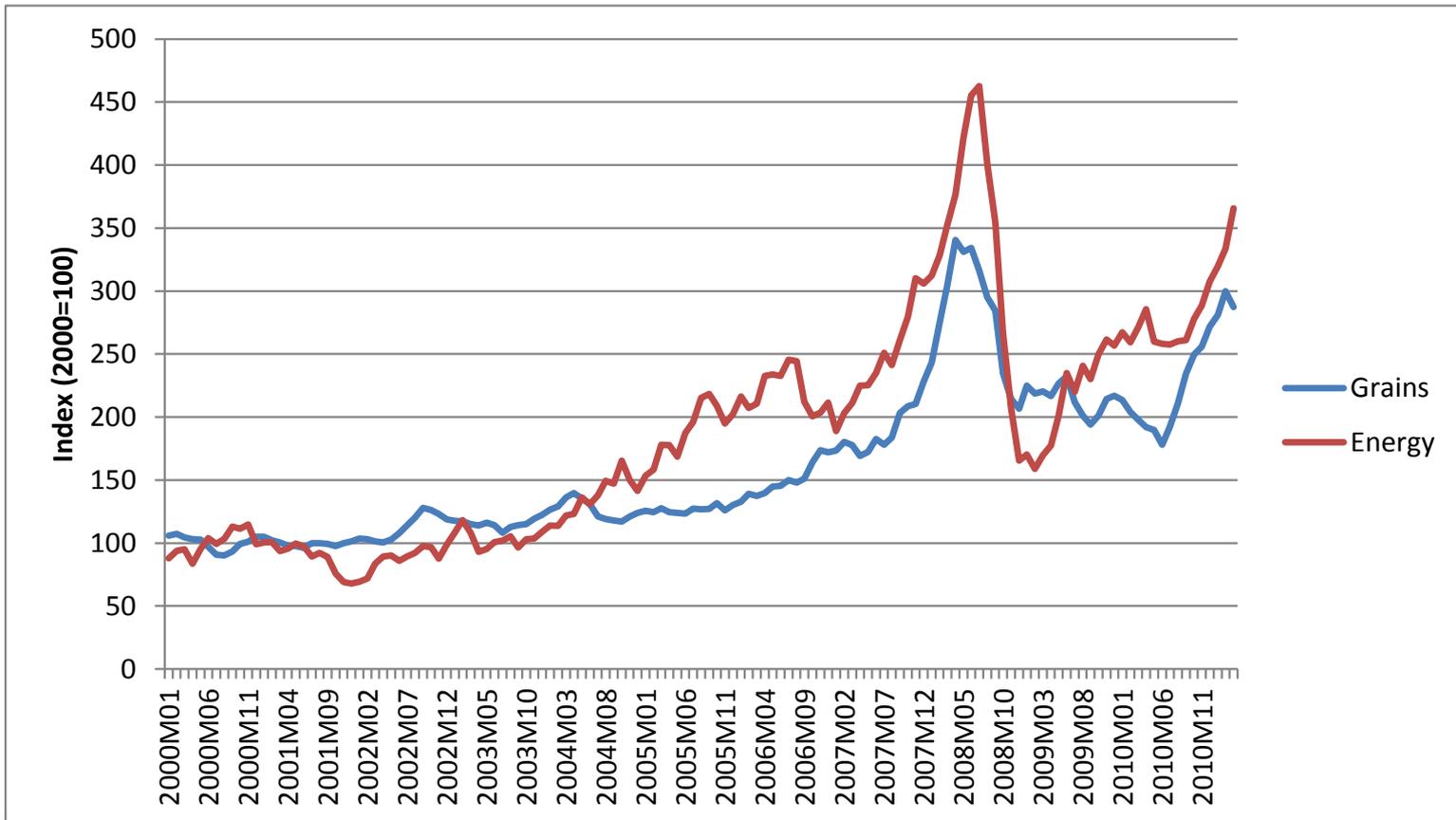
Presented at “Special Seminar on Poverty Reduction and Food Security Despite High Food Price Volatility”, sponsored by USAID Bureau for Food Security. May 20, 2011. Washington, D.C.

# Outline

- Background on events since 2007
- Key observations on recent worldwide and domestic commodity price behavior
  - Short-term price transmission
  - Internal vs. external drivers of volatility
  - The issue is not just volatility, but the likelihood of higher price levels in the long-term
    - Concept of regime shifts
- Implications
- What to do and not do

# Background – world prices

World Bank World Price Indices for Grains and Energy (Pink Sheet)  
2000-2011



# Background - causes

- Very broad phenomenon
  - Food, energy, metals/minerals
- Causes: still much debate
  - Increased demand from
    - Economic growth in Asia ... and SSA!
    - Biofuels, especially in US
  - Poor harvests in Australia, Russia
  - Speculation
    - The financialization of agricultural commodity markets

# Background - responses

- Reflexive closing of borders in many countries
- Broad assertion of need for greater role for the state in cereals markets
- Upsurge in civil unrest in developing countries
- Renewed focus on agriculture among development agencies following 2007/08 crisis
- ... but limited follow-through due to worldwide financial crisis
- Are we in a fundamentally new environment? What does that environment look like? What to do?

# Key Observation # 1

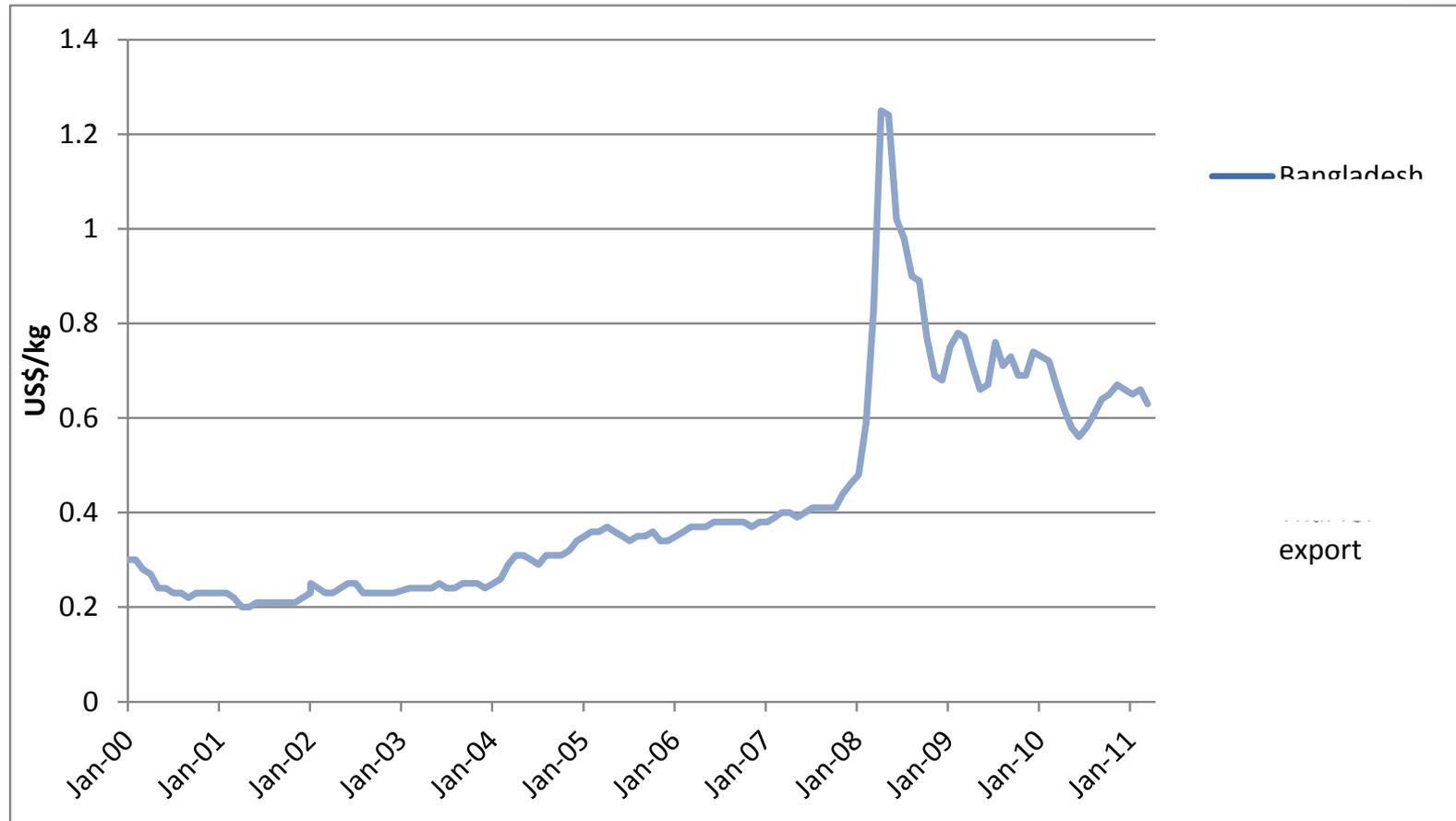
*Short-term price transmission to local markets (2-3 months) has been:*

*(a) low on average and*

*(b) highly variable across countries*

*Demonstrate with rice in Asia ...*

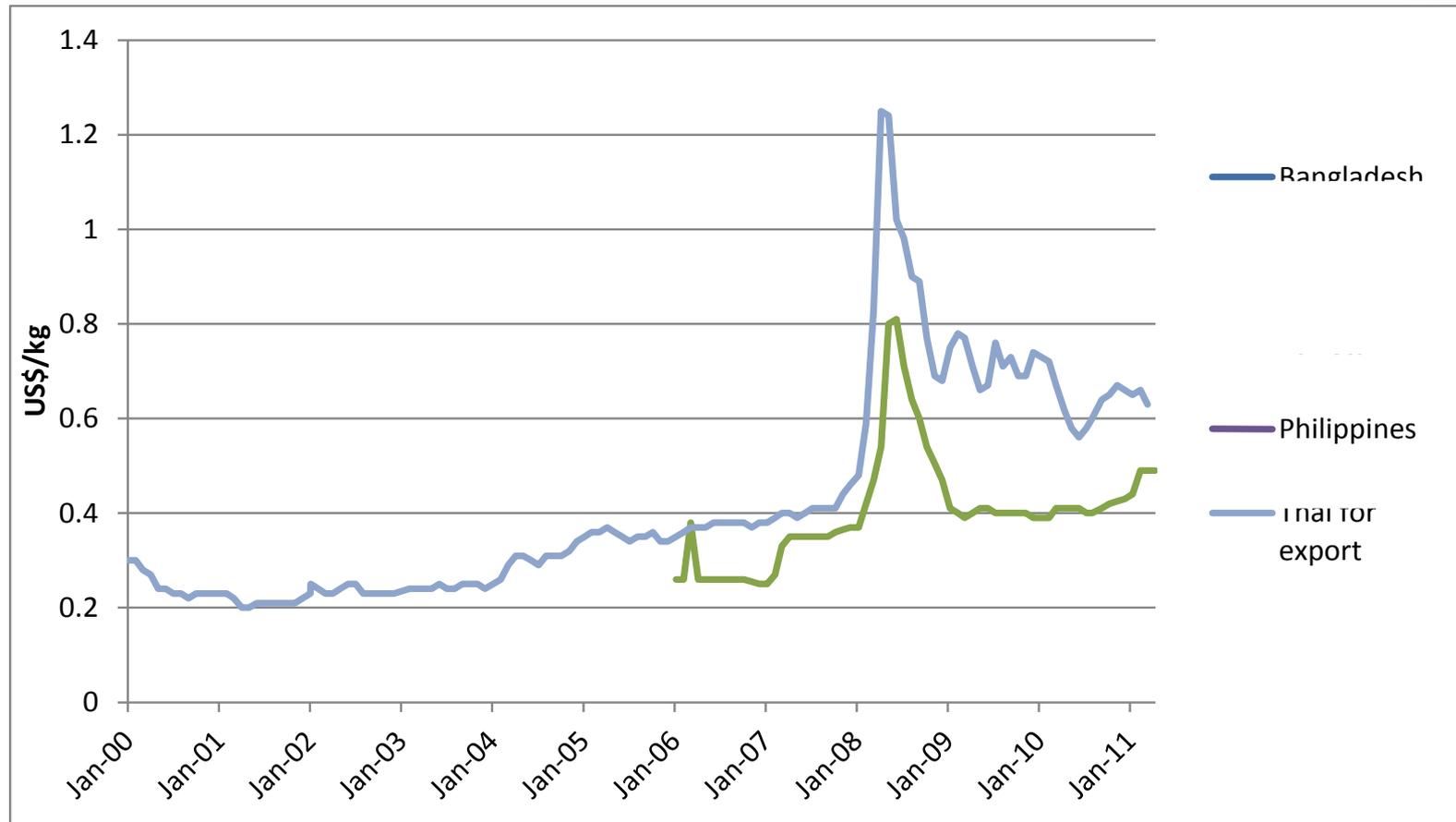
# Rice price behavior



Source: FAO-GIEWS

*> 3x from late 2007 to early 2008, + regime shift*

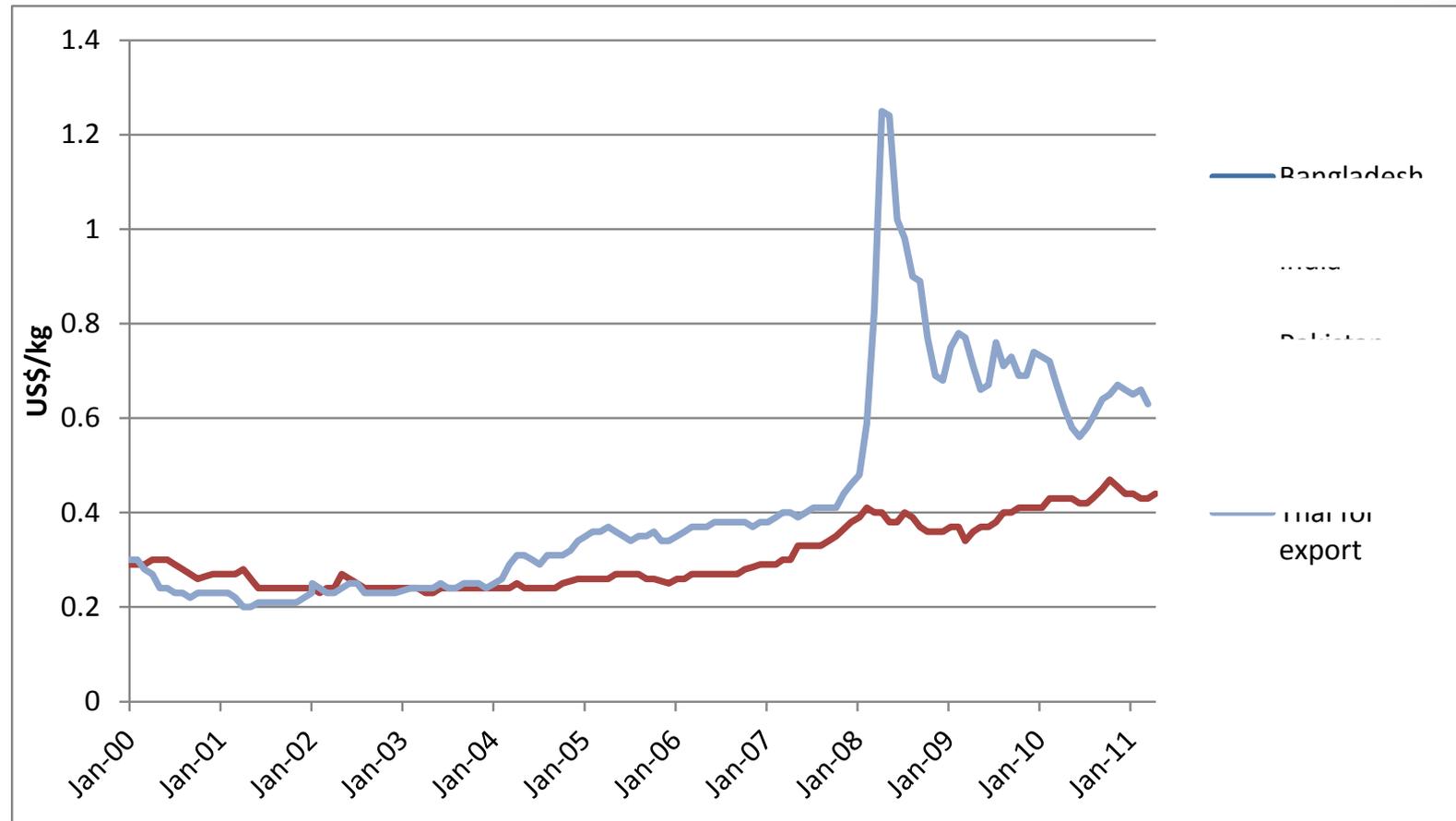
# Rice price behavior (2)



Source: FAO-GIEWS

*Exporter that continued to export*

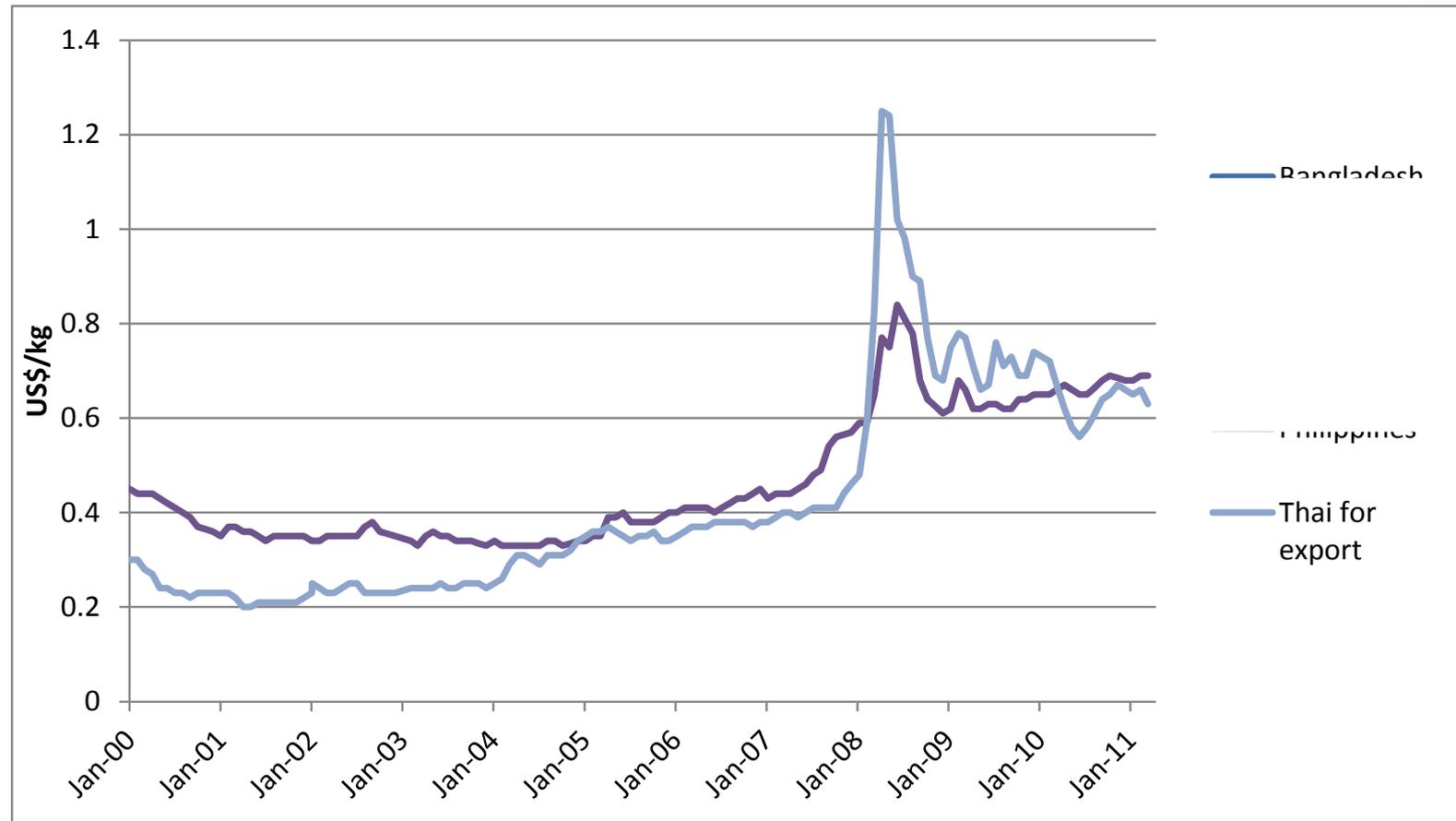
# Rice price behavior (2)



Source: FAO-GIEWS

*Exporter that closed its borders*

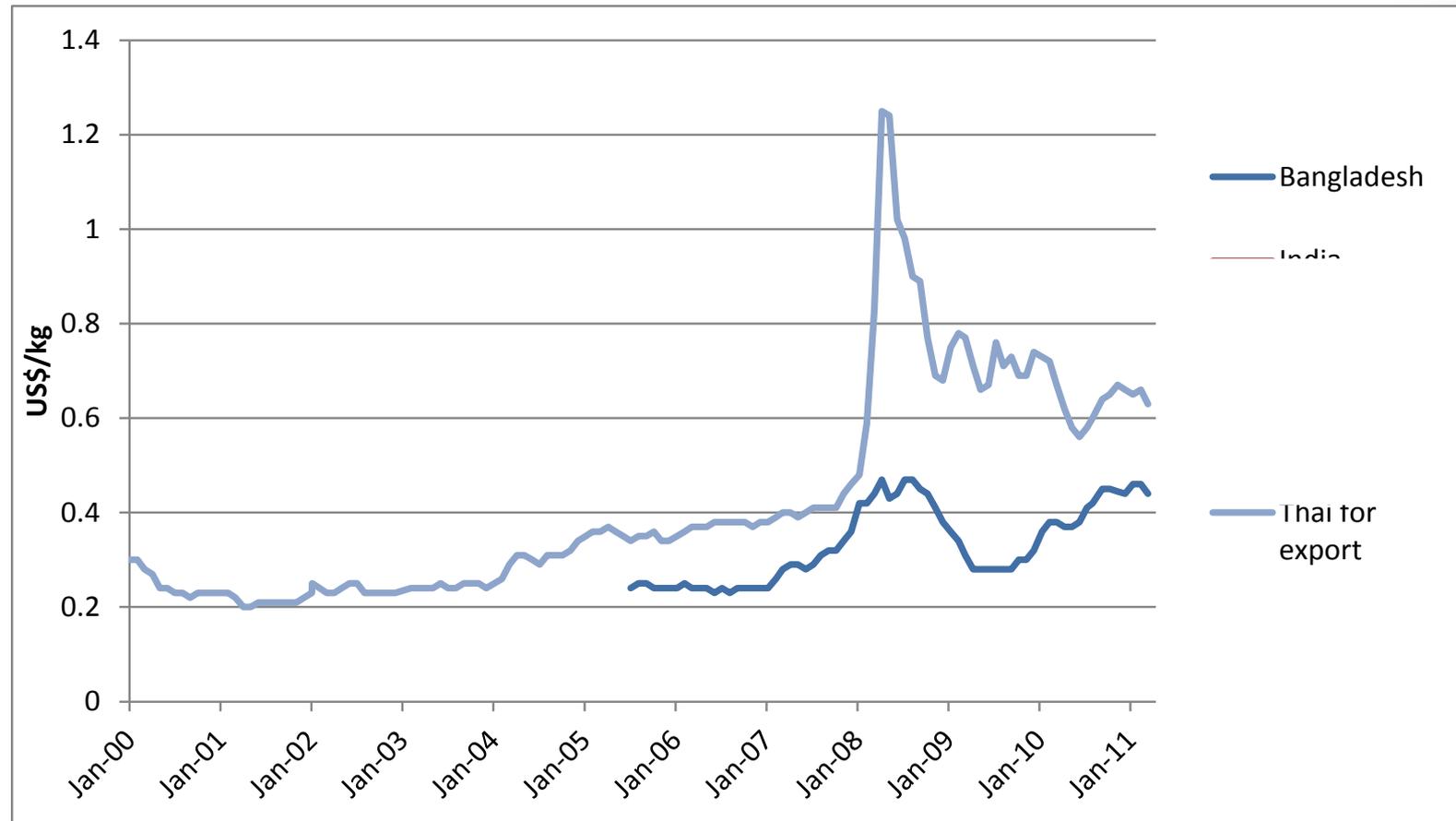
# Rice price behavior (3)



Source: FAO-GIEWS

*Major importer that partially controlled imports and sales prices*

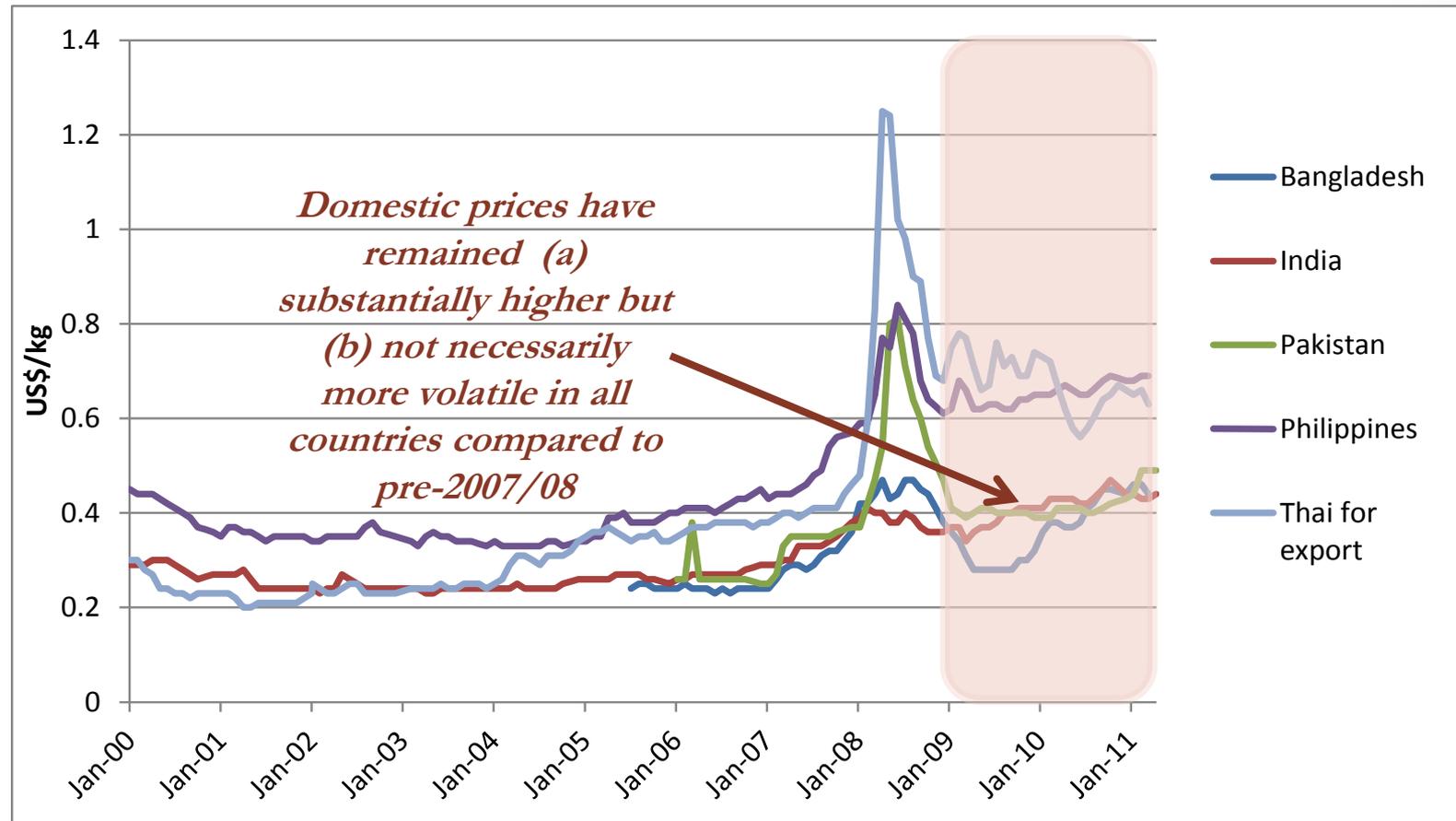
# Rice price behavior (4)



Source: FAO-GIEWS

*Importer (5% of consumption) that (presumably) subsidized sales prices*

# Rice price behavior (6)



Source: FAO-GIEWS

# Key observation # 2

*Historically, drivers of domestic volatility have been more internal than external*

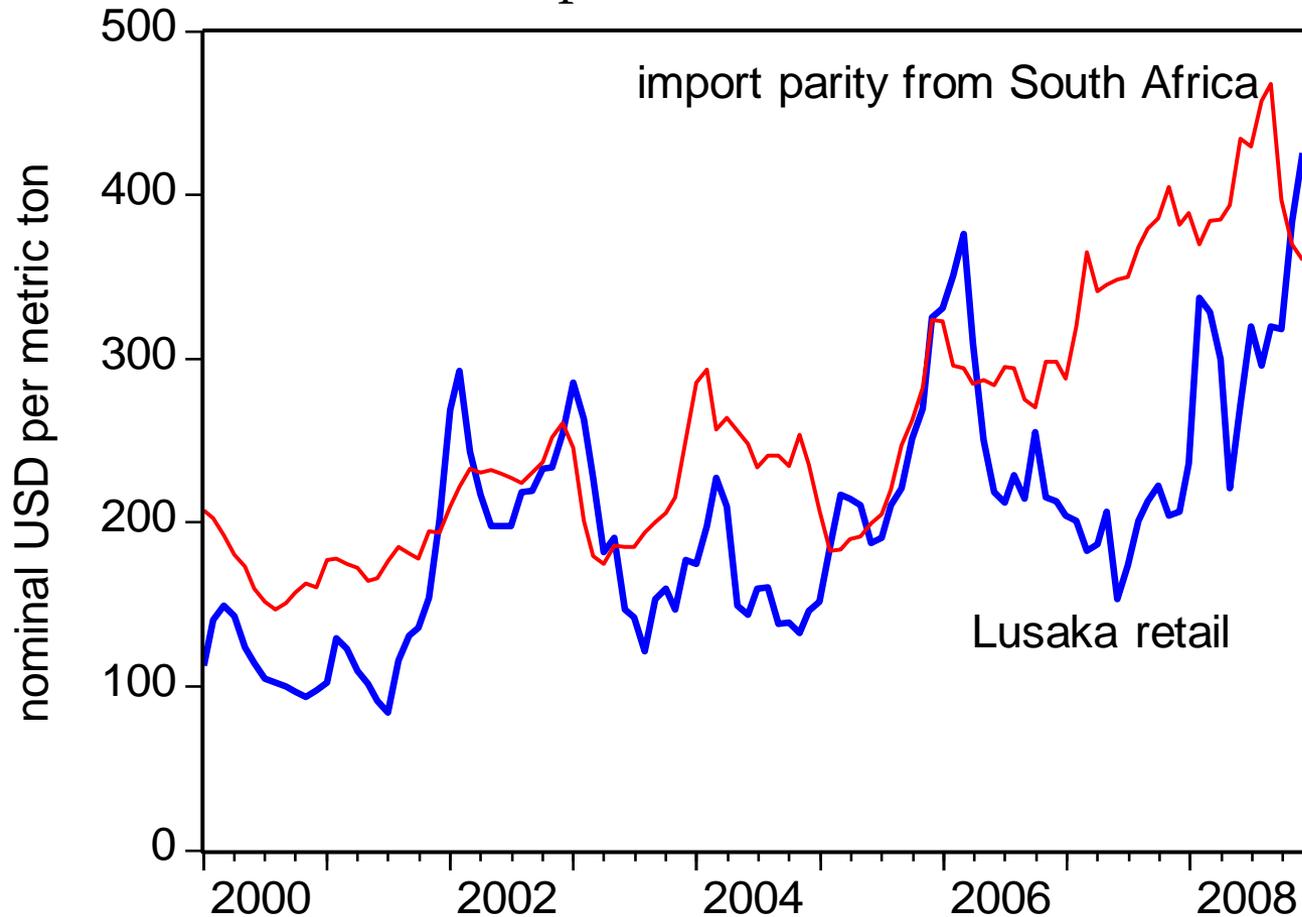
# Internal drivers

- High costs of storage and trade
  - A wider range within which prices can fluctuate, even if trade were fully liberalized
- Rainfed production
  - Greater year-to-year variability in production
- Unpredictable policy
  - Sidelines the private sector, leads to greater price spikes
- Poor management of public stocks

*Demonstrate with maize in southern Africa ...*

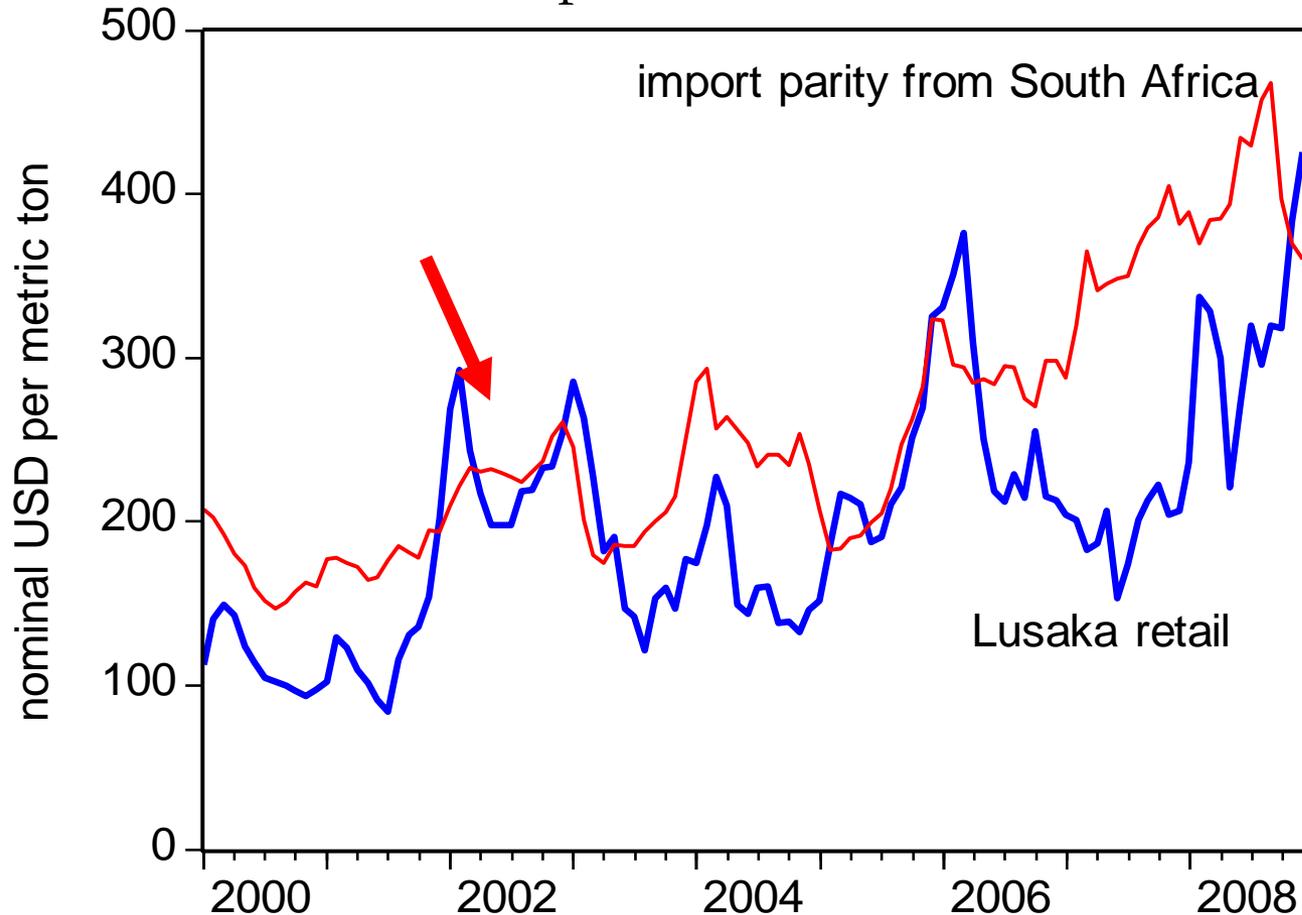
# Internal drivers (1)

- Nominal USD maize prices in **Zambia**



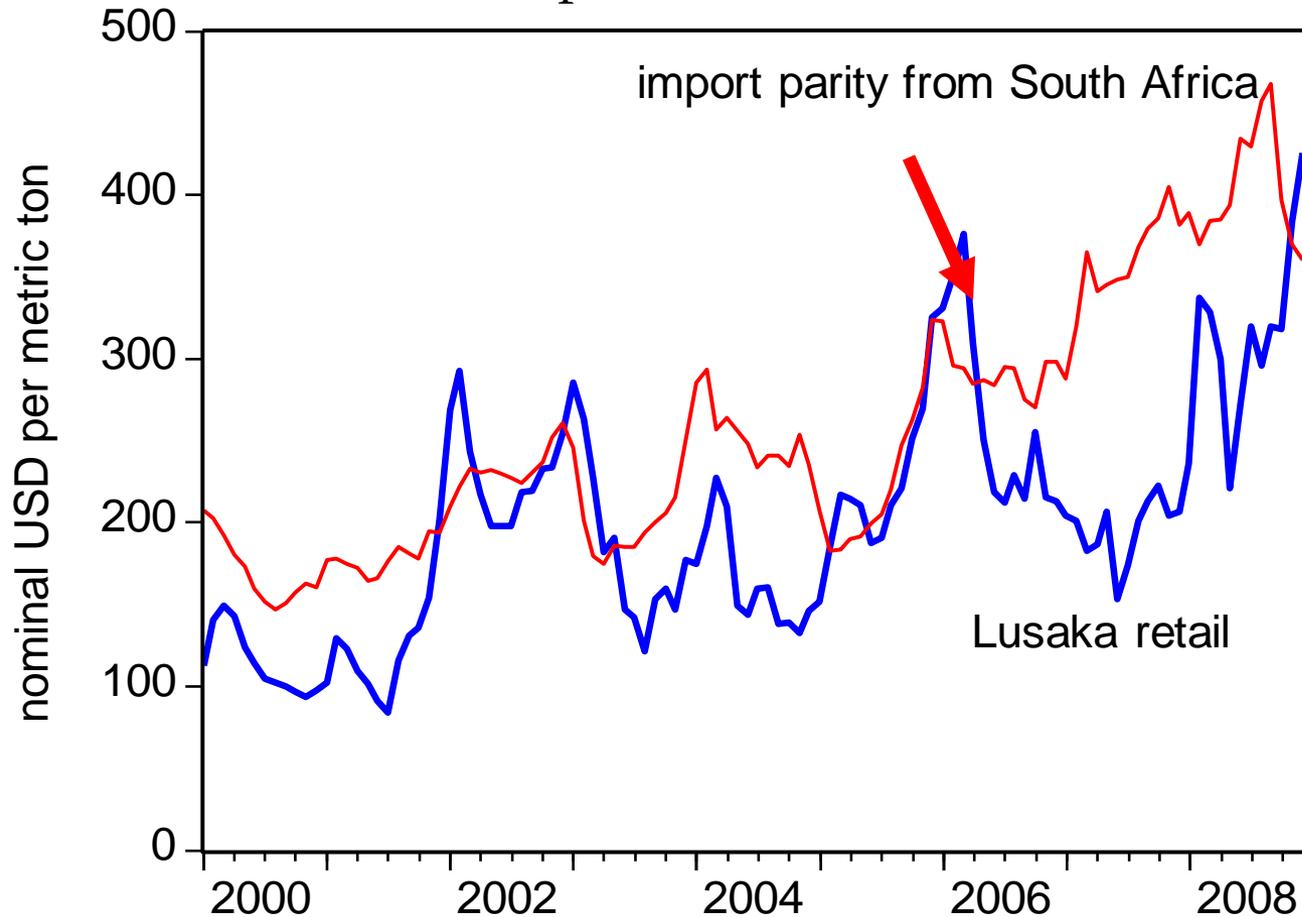
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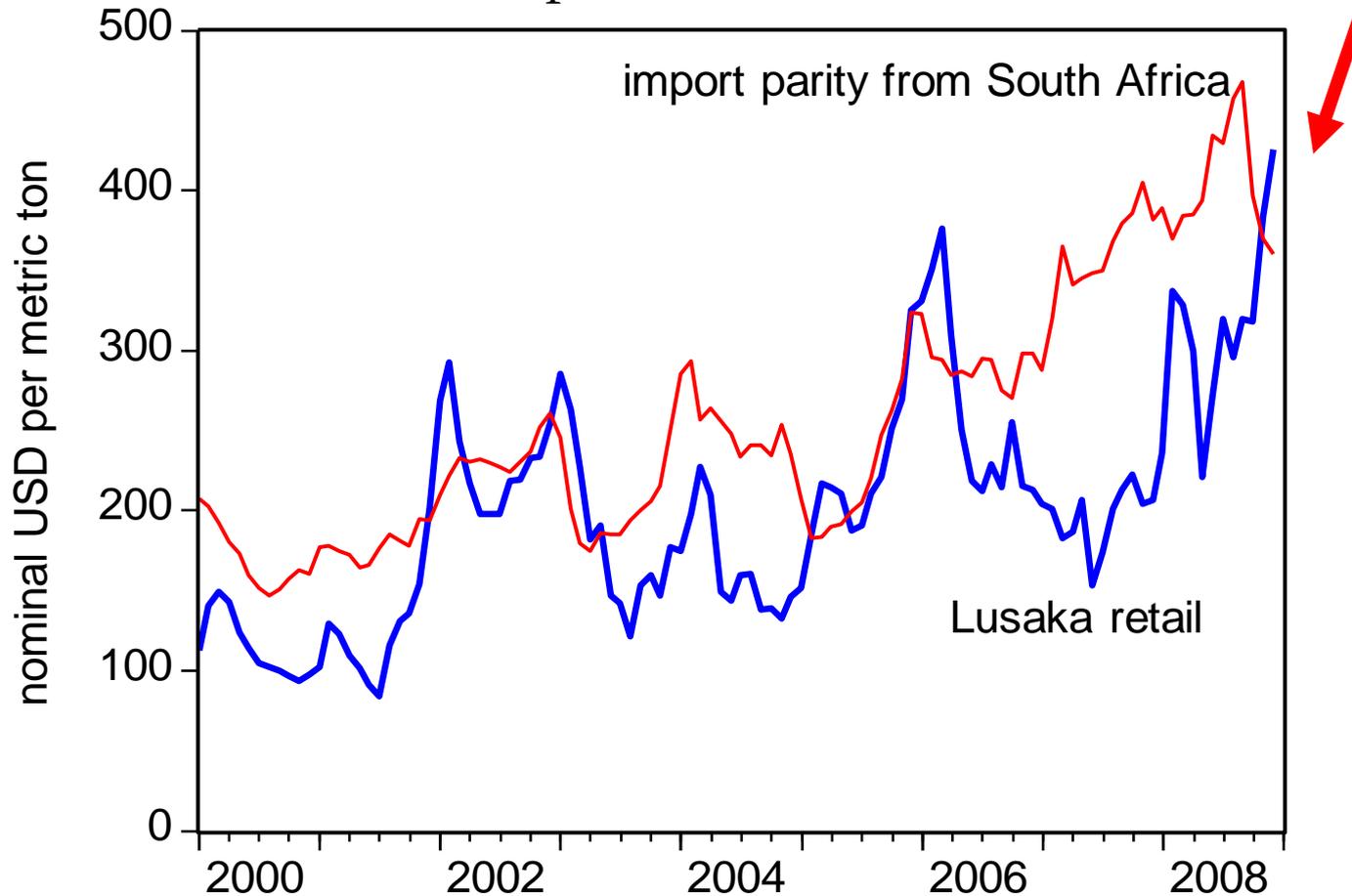
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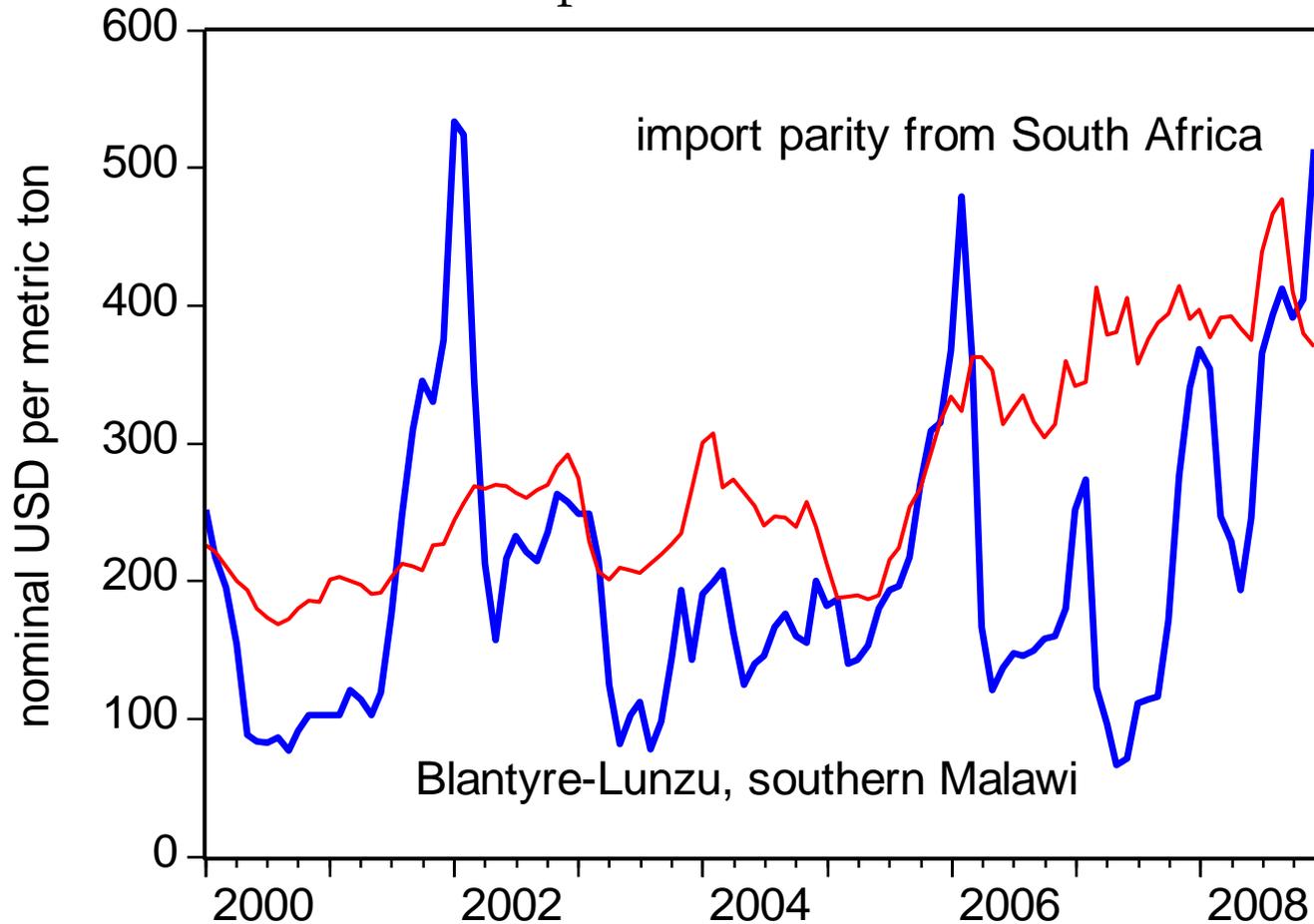
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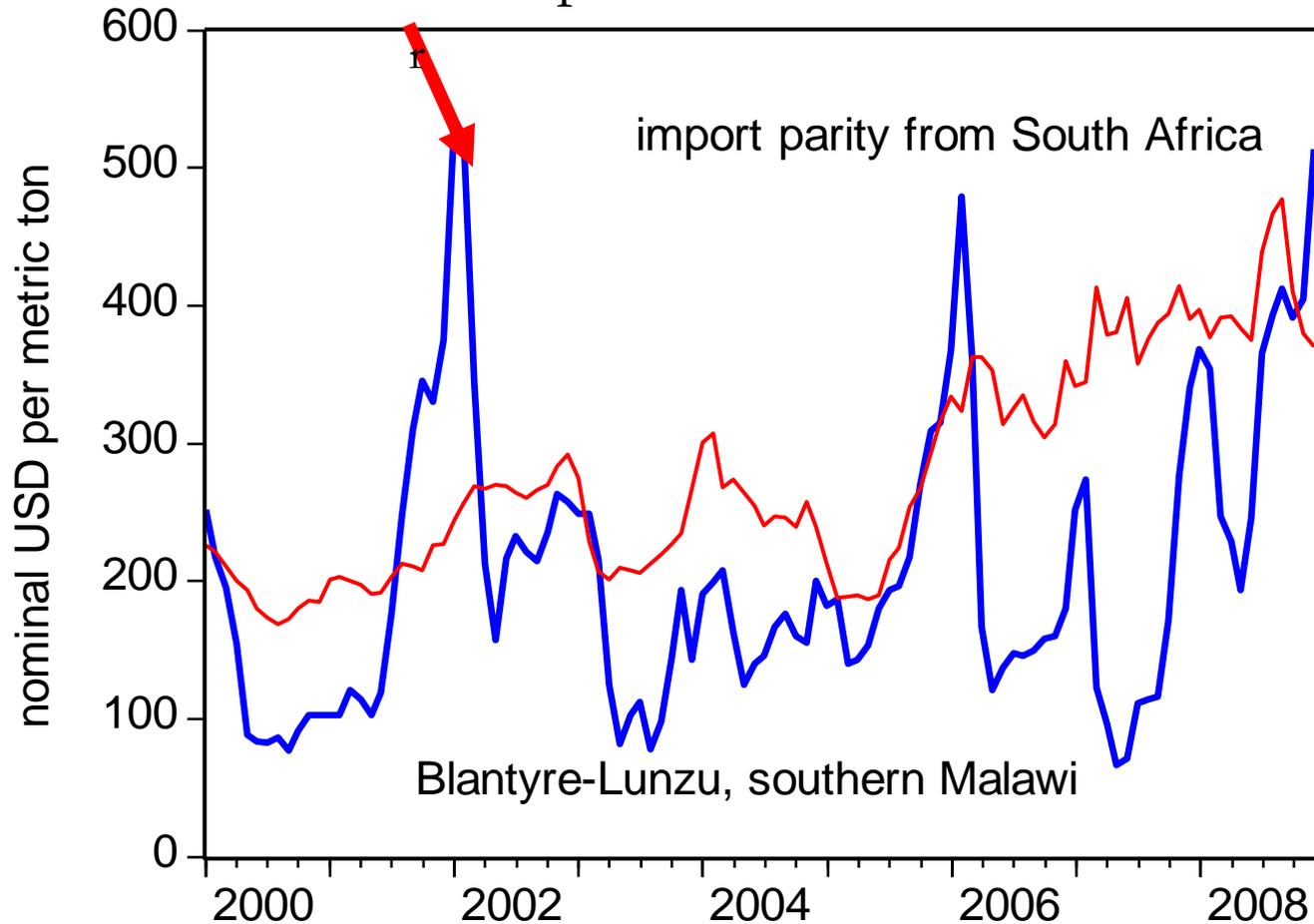
# Internal drivers (5)

- Nominal USD maize prices in **Malawi**



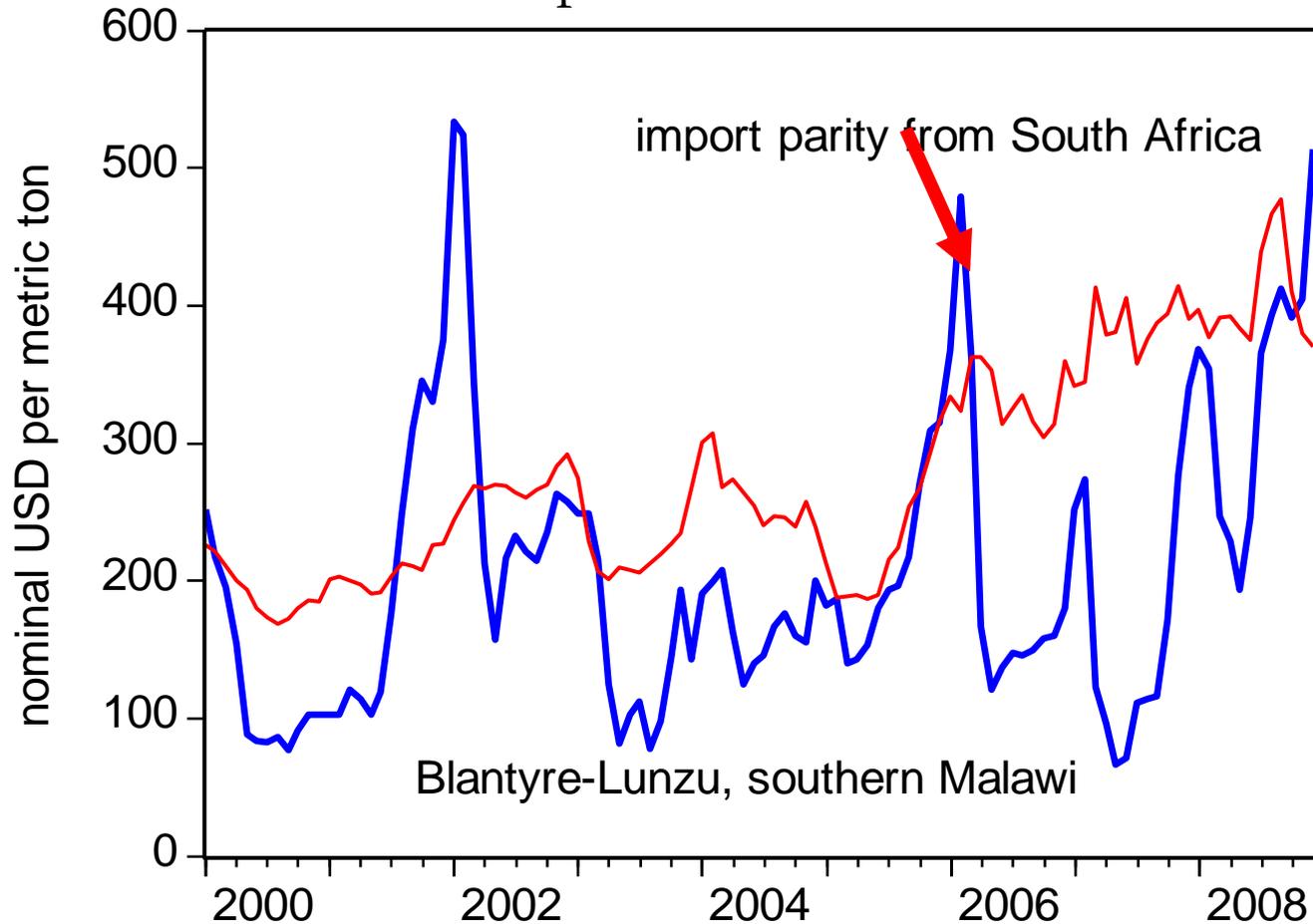
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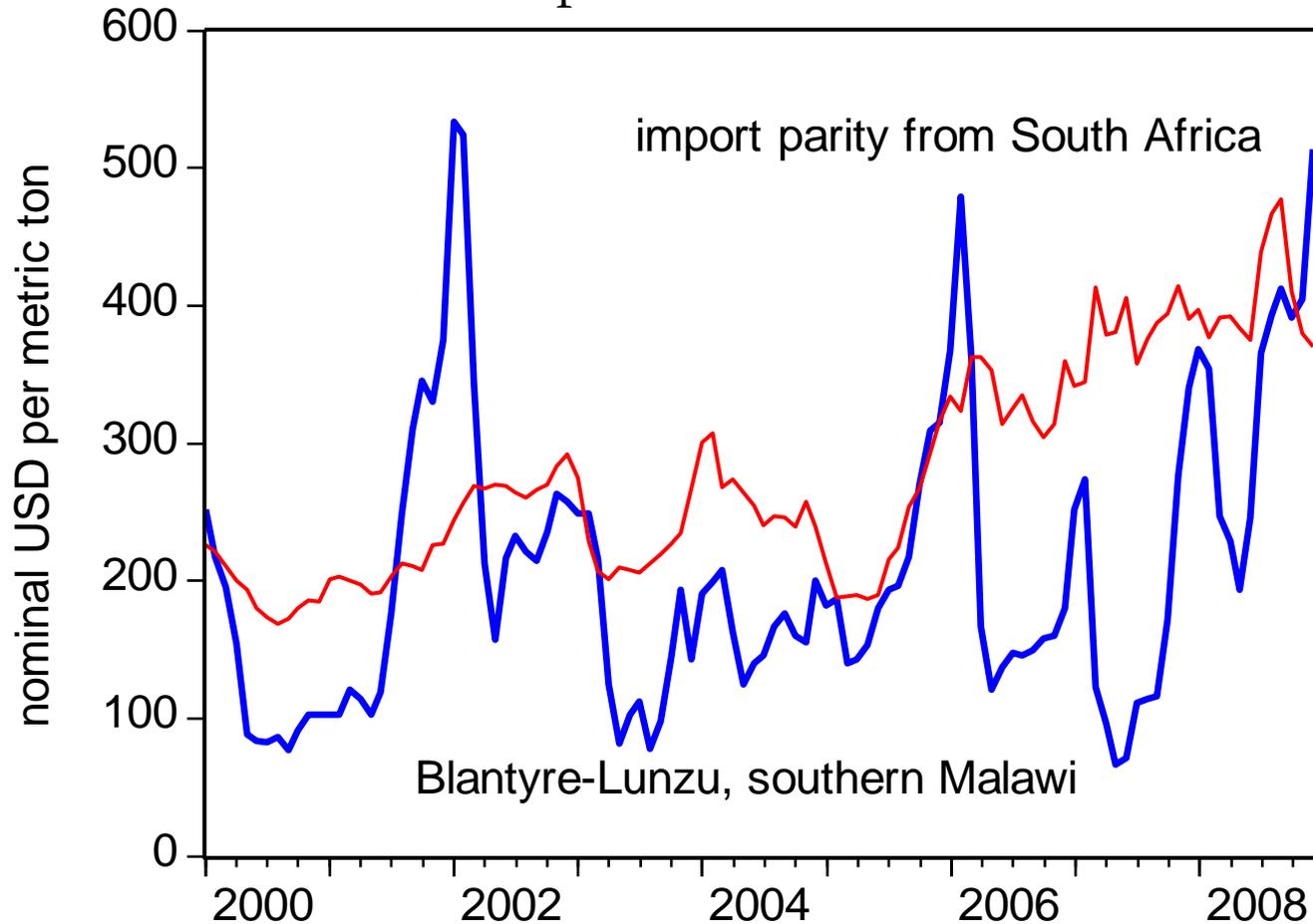
# Internal drivers (7)

- Nominal USD maize prices in **Malawi**



# Internal drivers (8)

- Nominal USD maize prices in **Malawi**



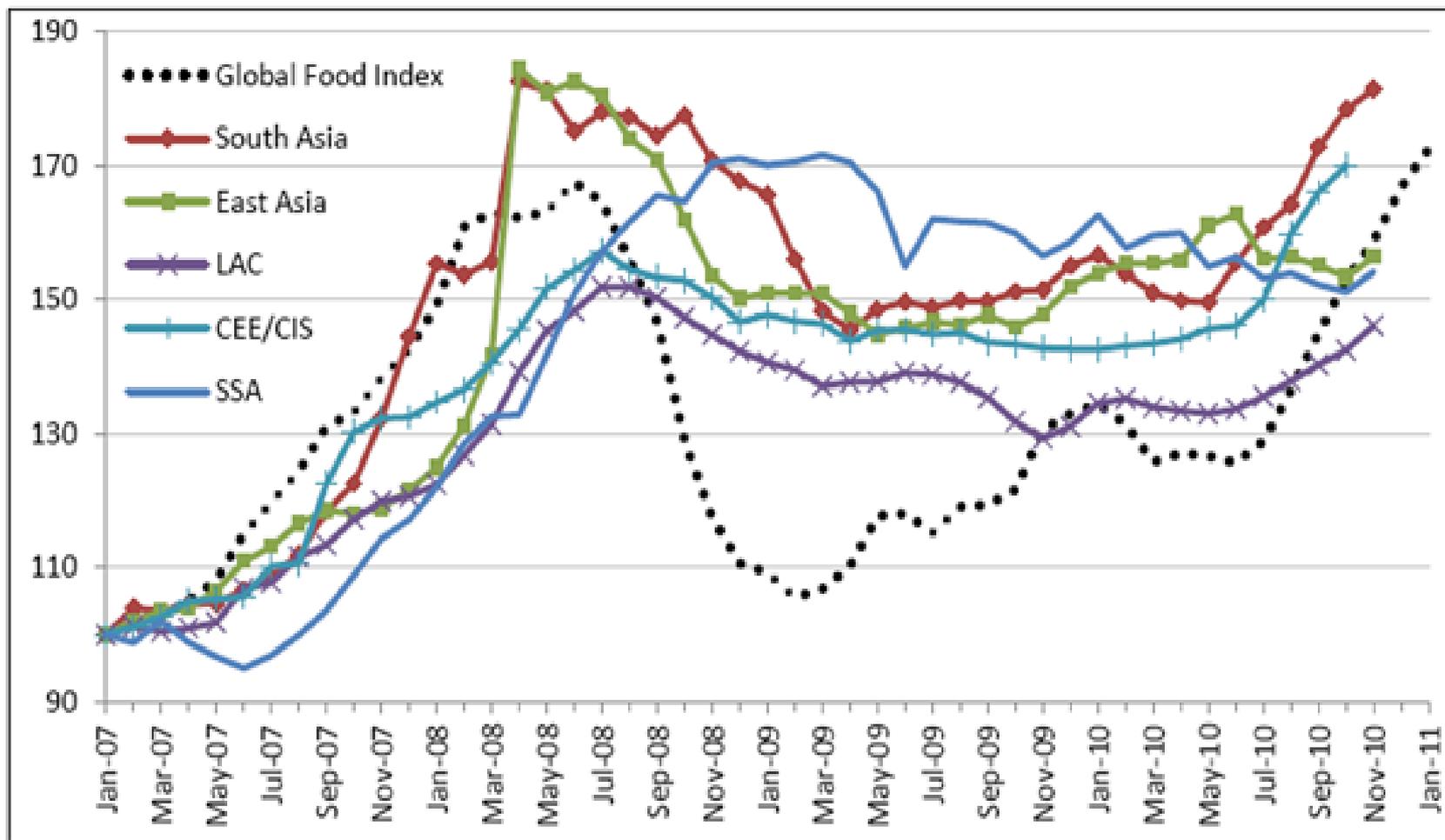
# Key observation # 3

*But the issue in developing countries is not just price volatility ...*

*price levels have shifted*

*(and are not necessarily more volatile)*

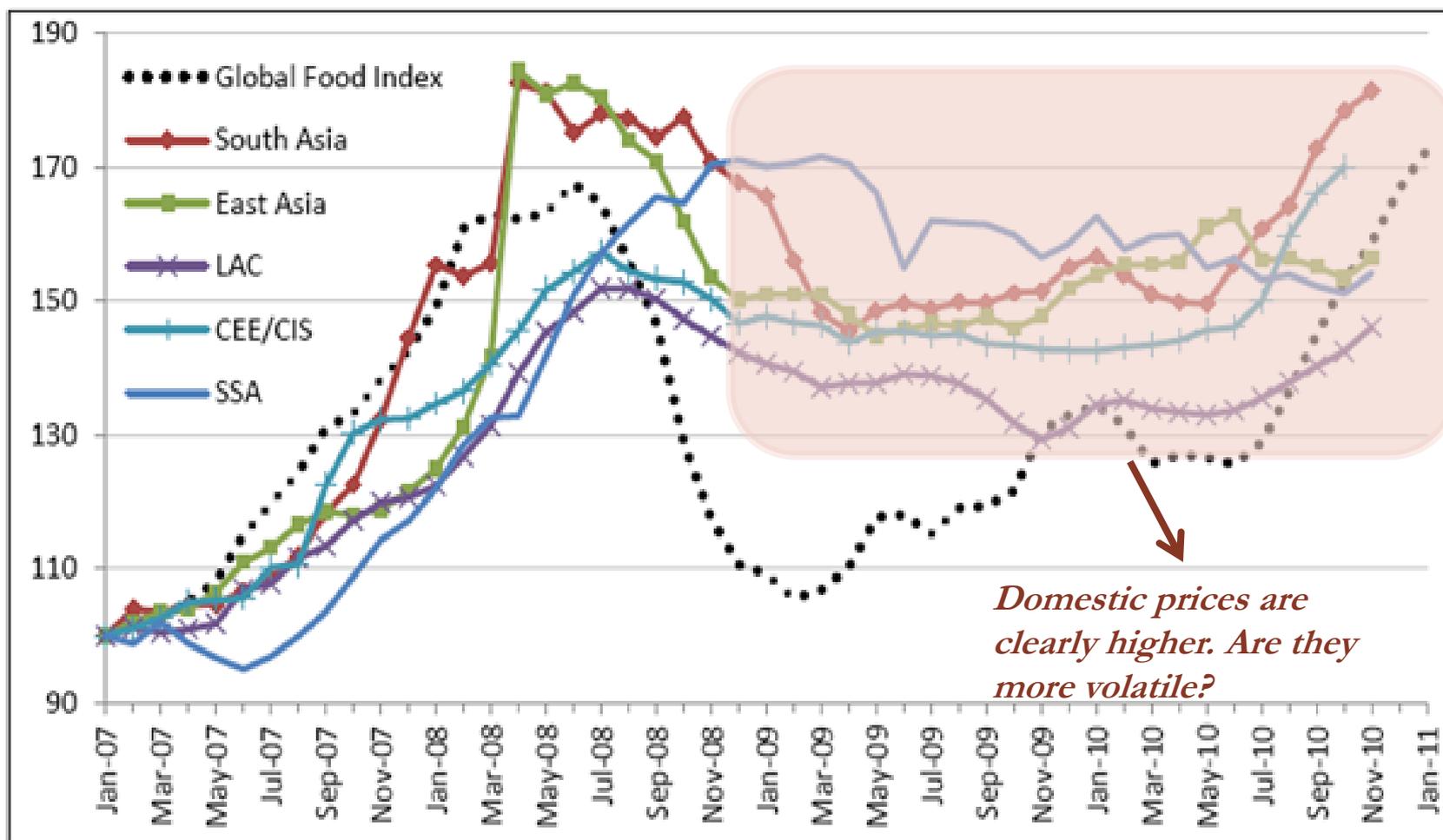
# Food price indices, world and regions



**Source:** Figure extracted from Ortiz and al., (2011) in Escalating Food Prices, UNICEF, Page 8.

FAO (2010f) and authors' calculations. Note: Sample includes 5 countries from South Asia, 5 from East Asia, 16 from LAC, 7 from CEE/CIS and 24 from SSA

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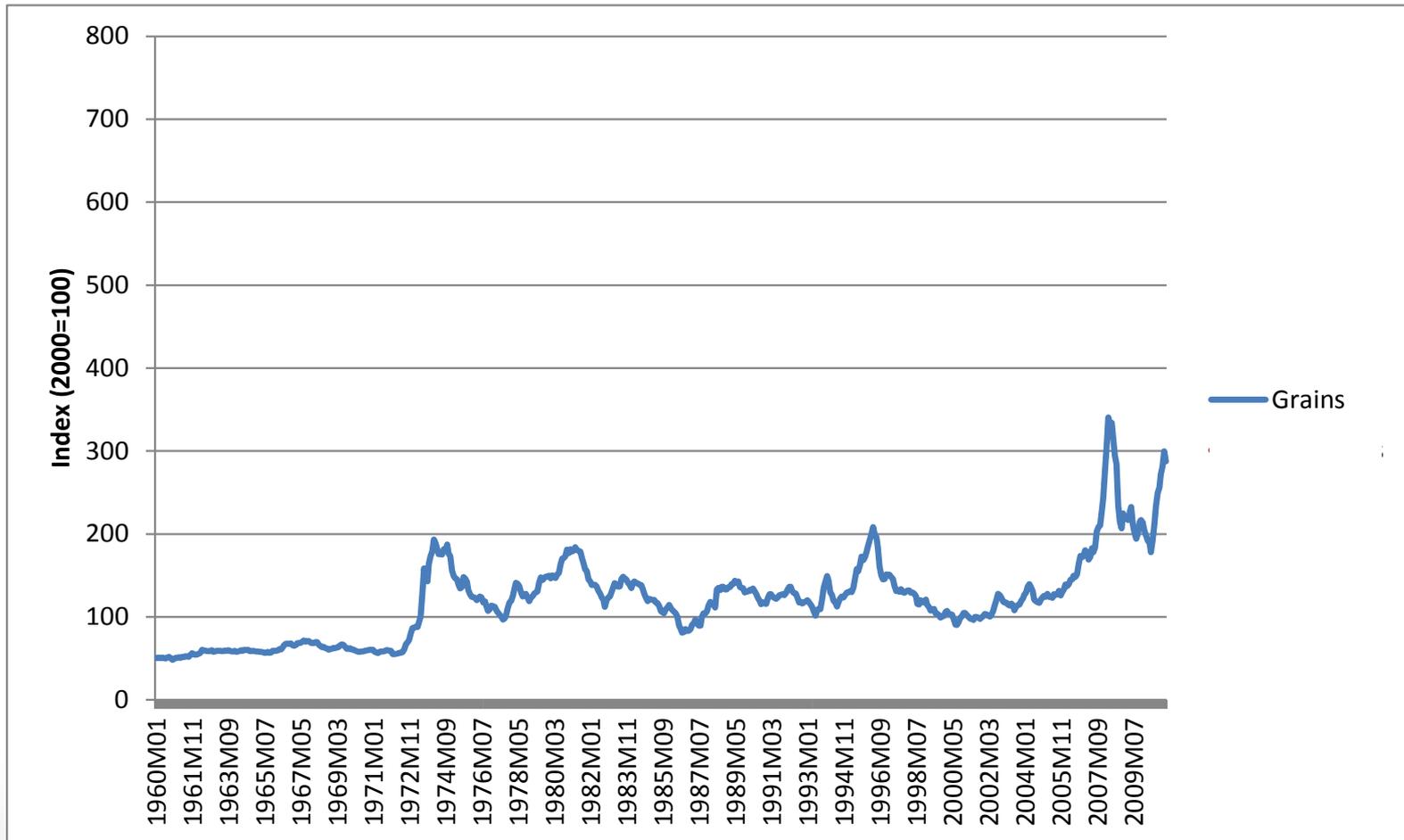


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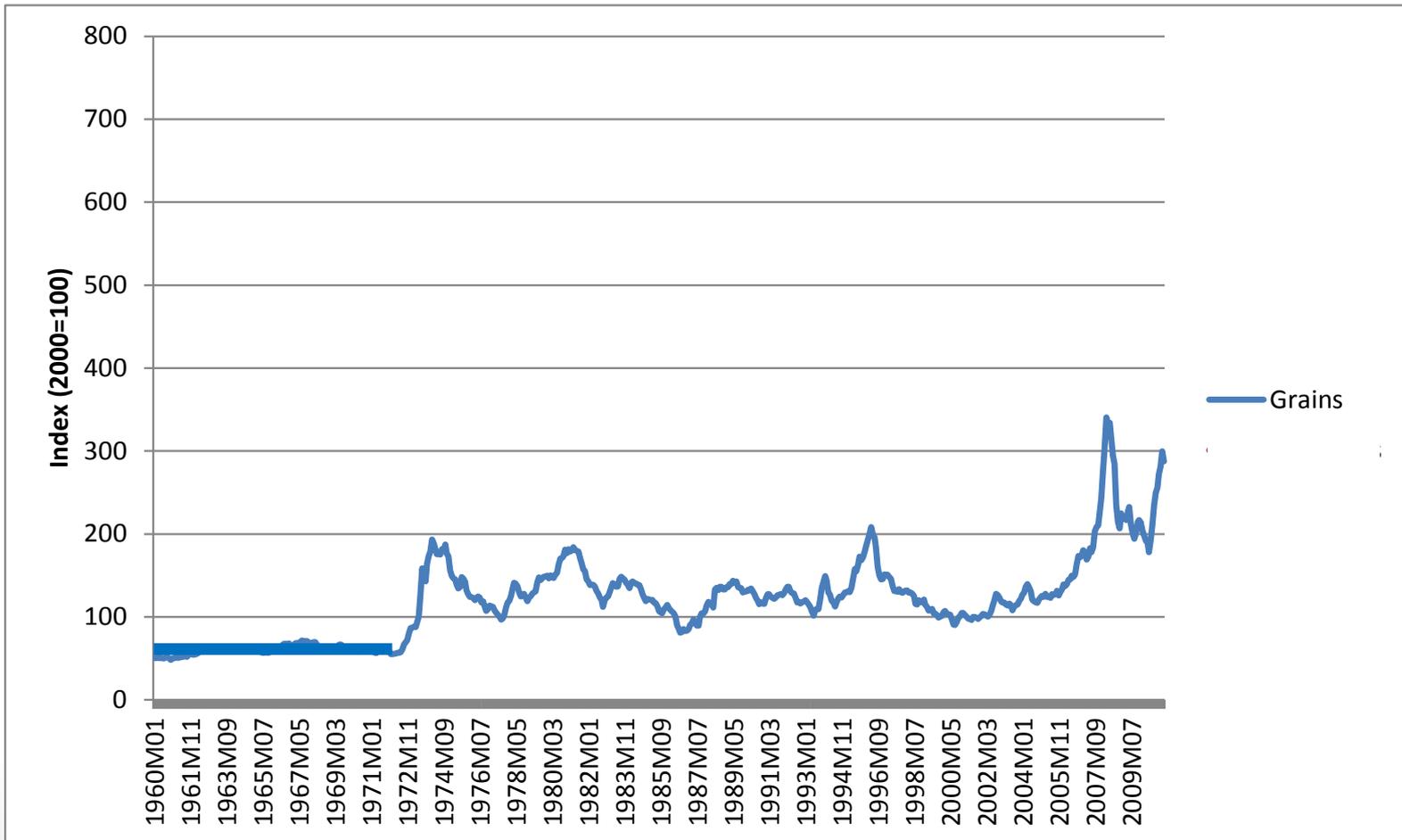
# Higher price levels – the long view

World Bank World Price Indices for Grains and Fertilizer (Pink Sheet)  
1960-2011



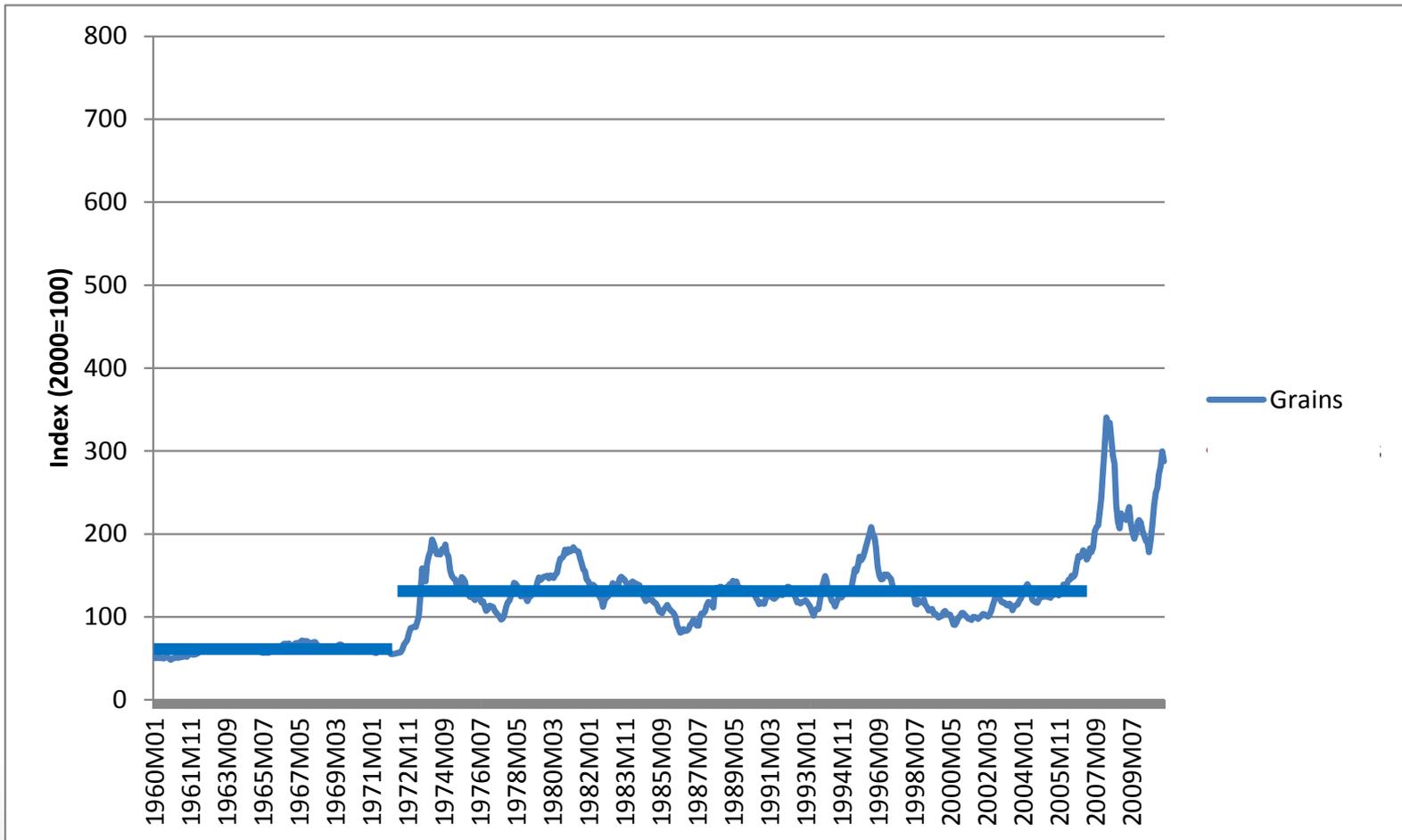
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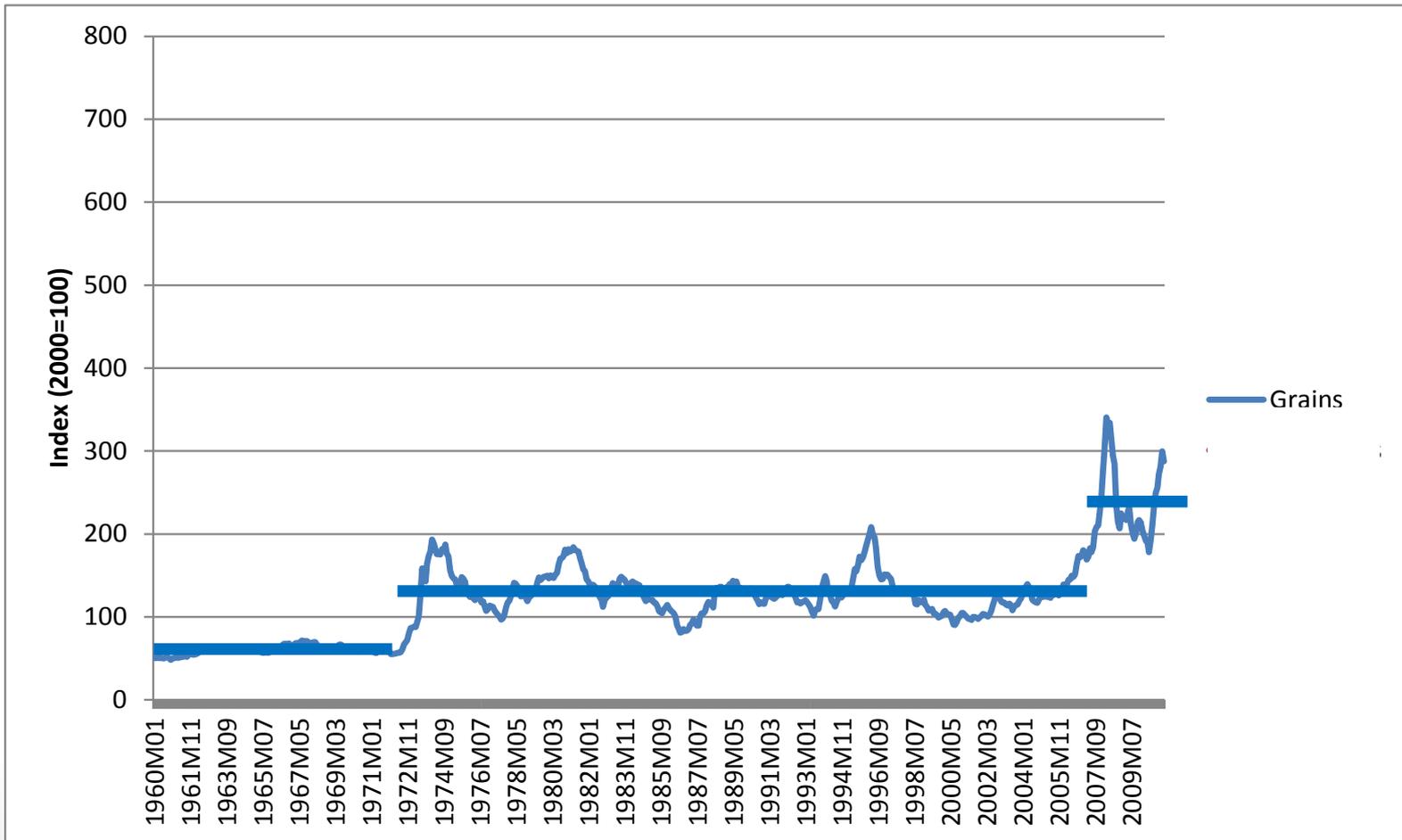
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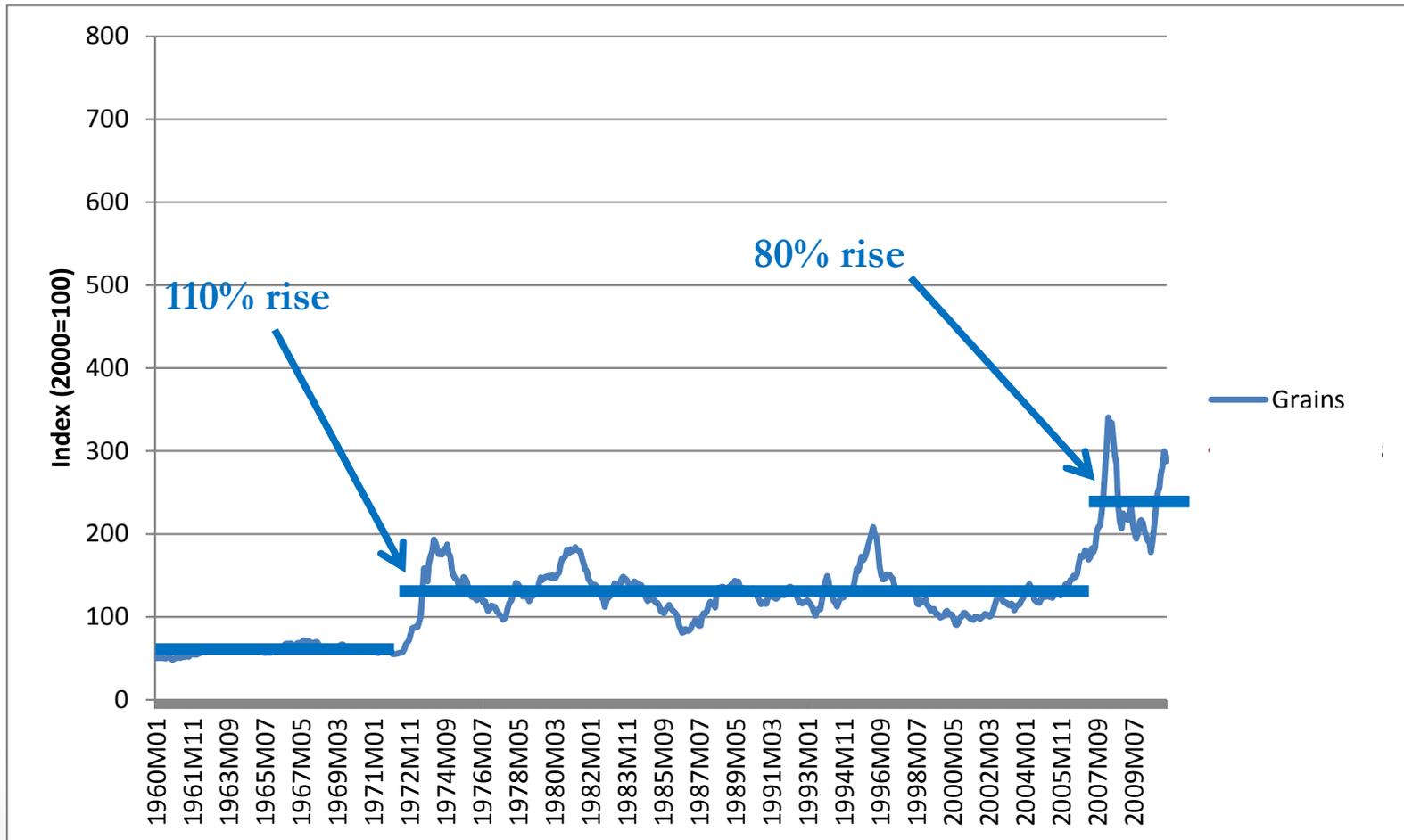
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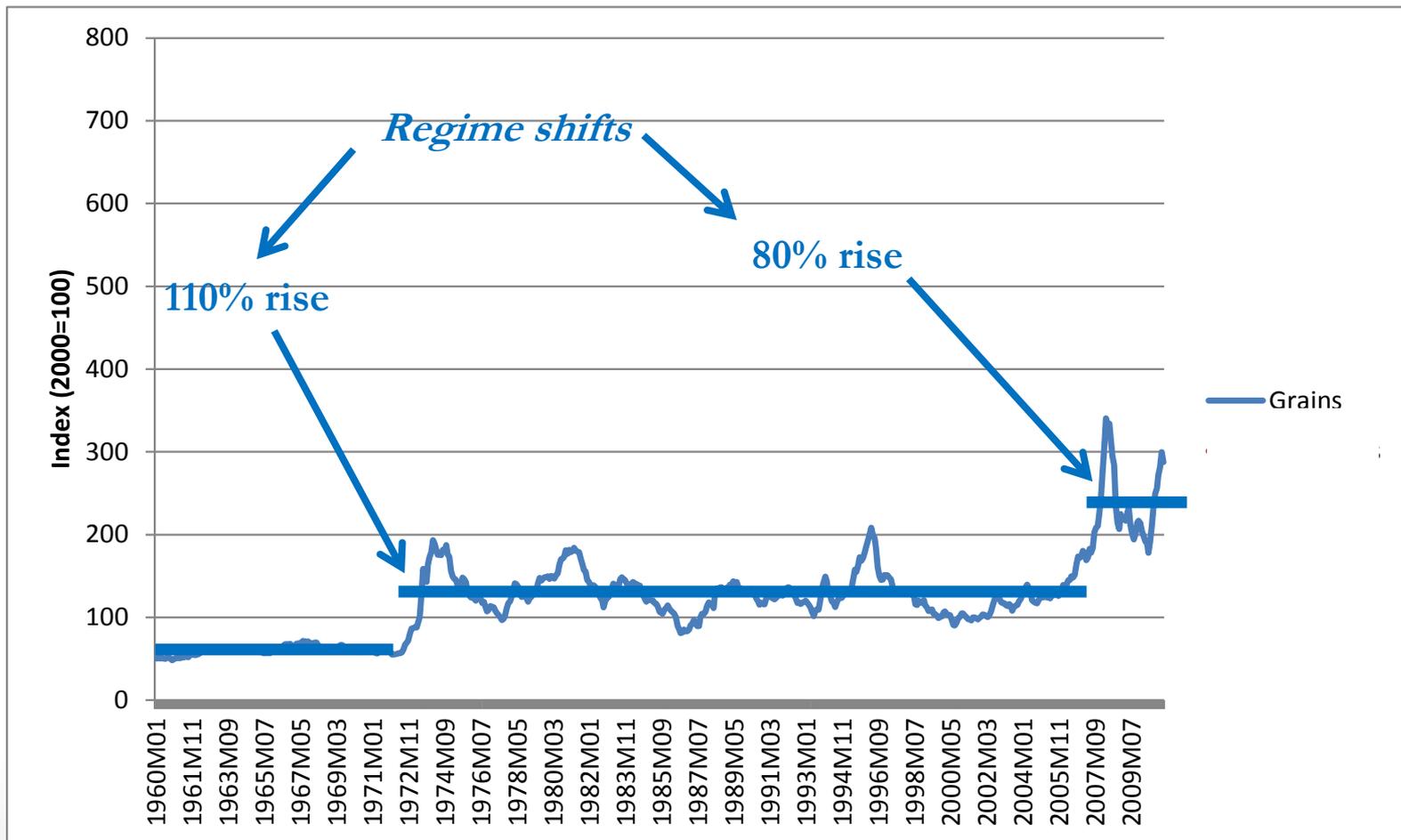
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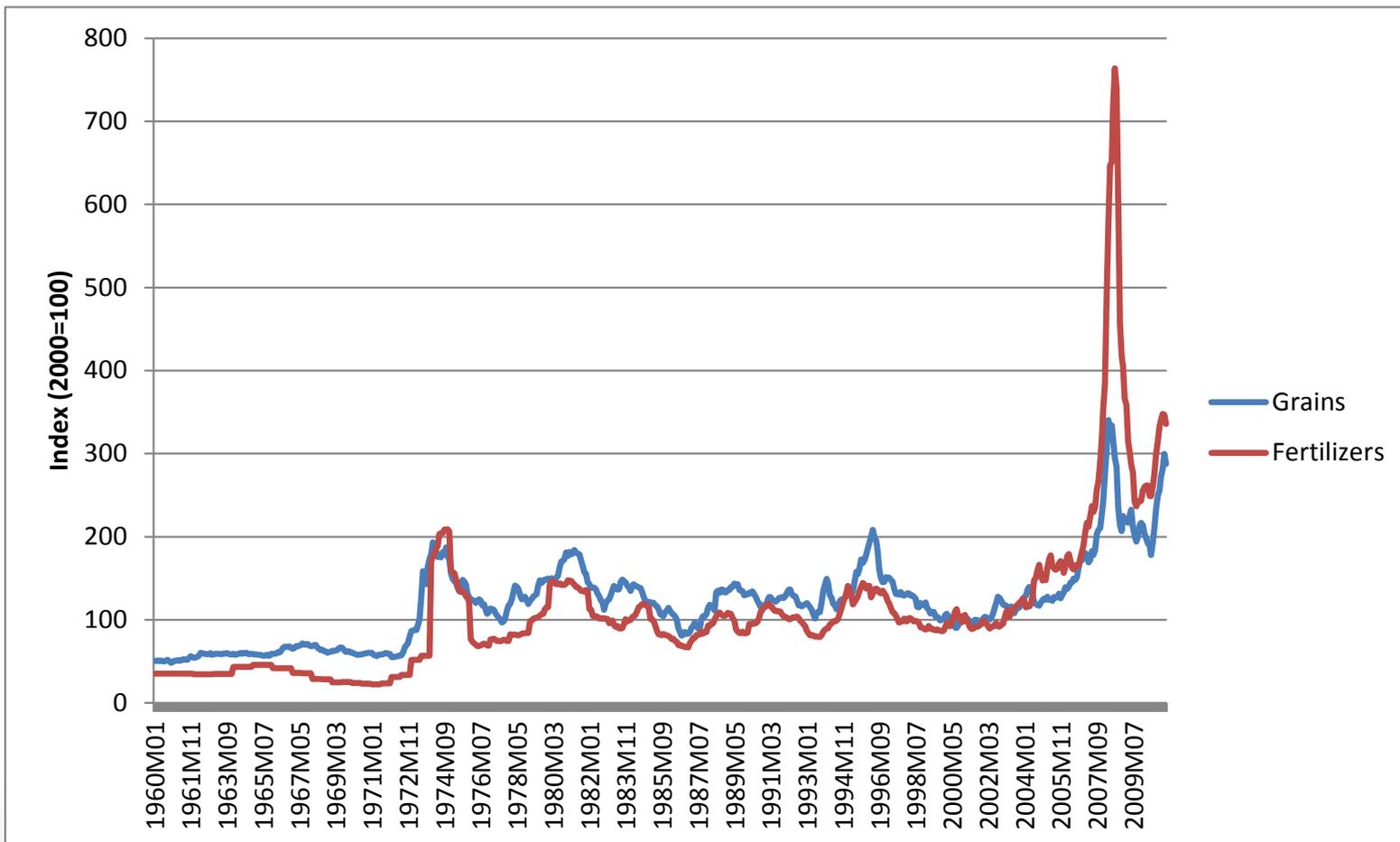
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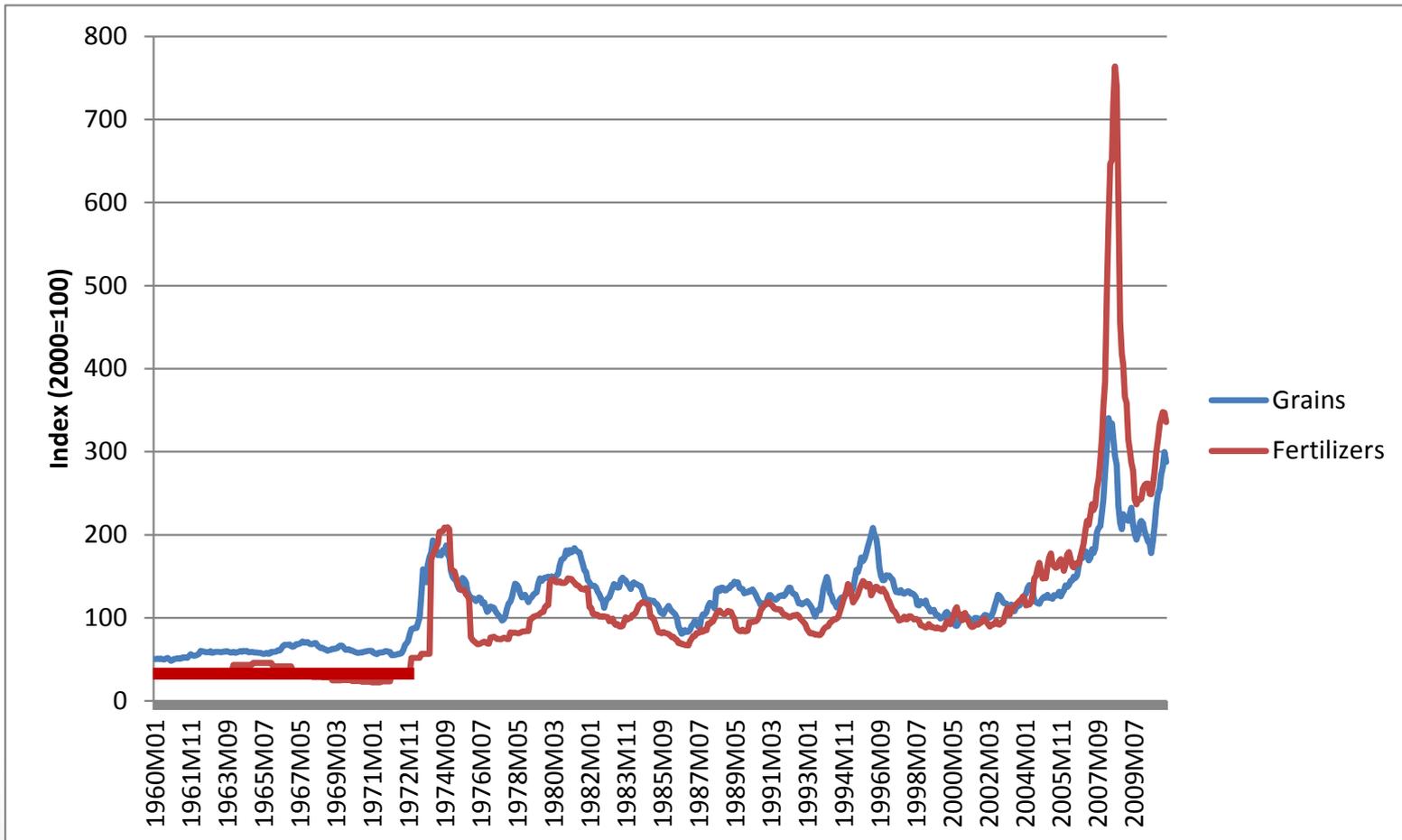
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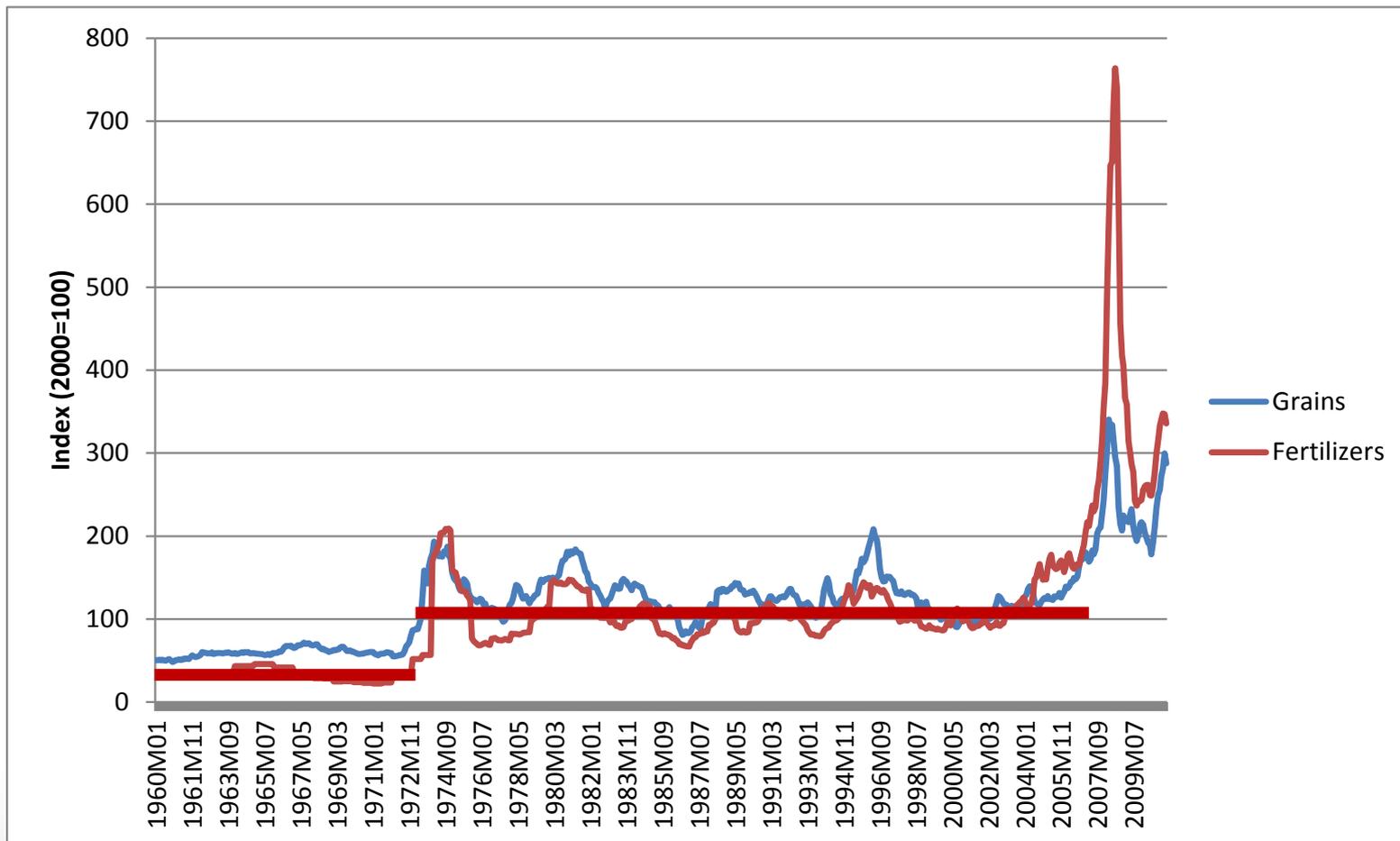
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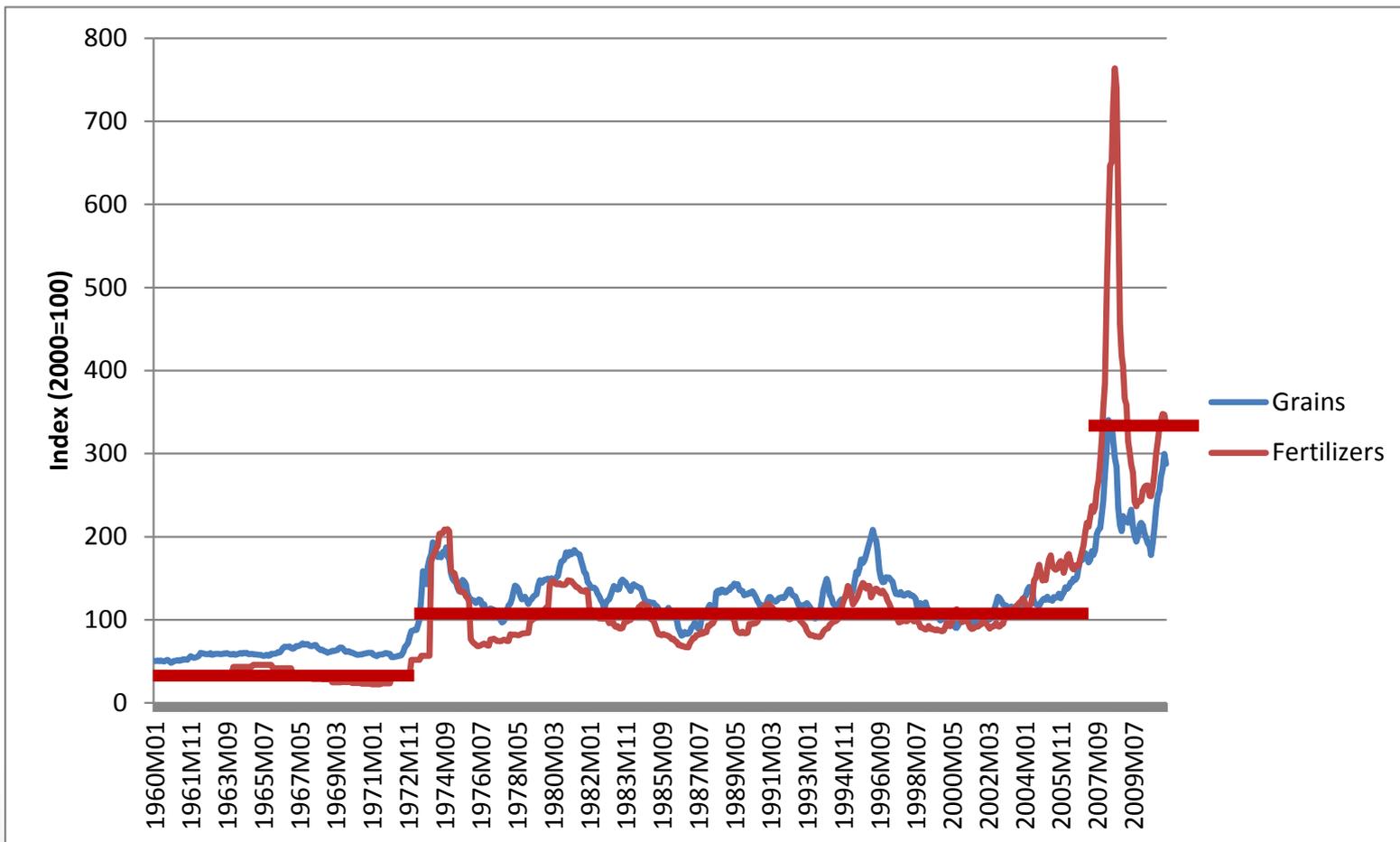
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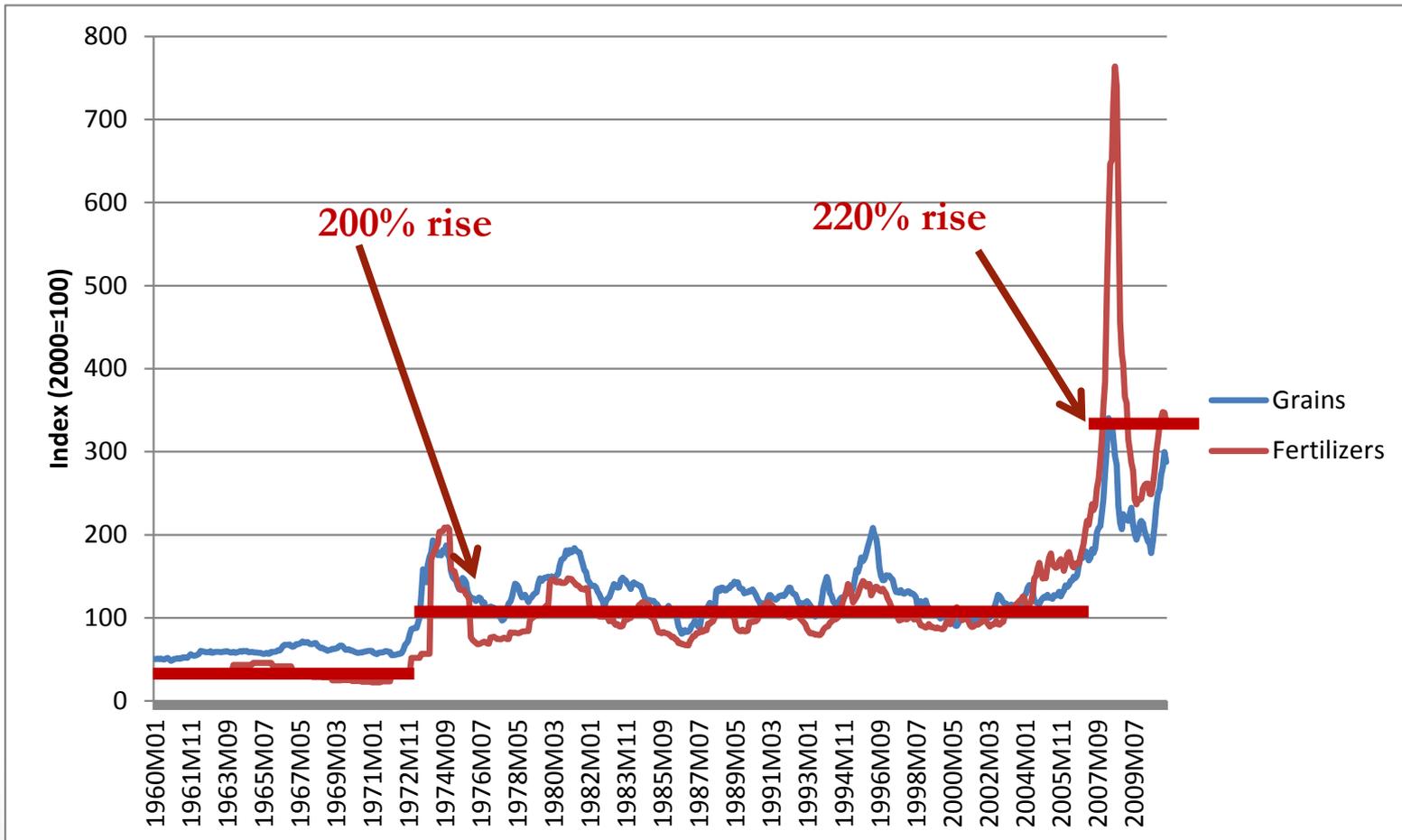
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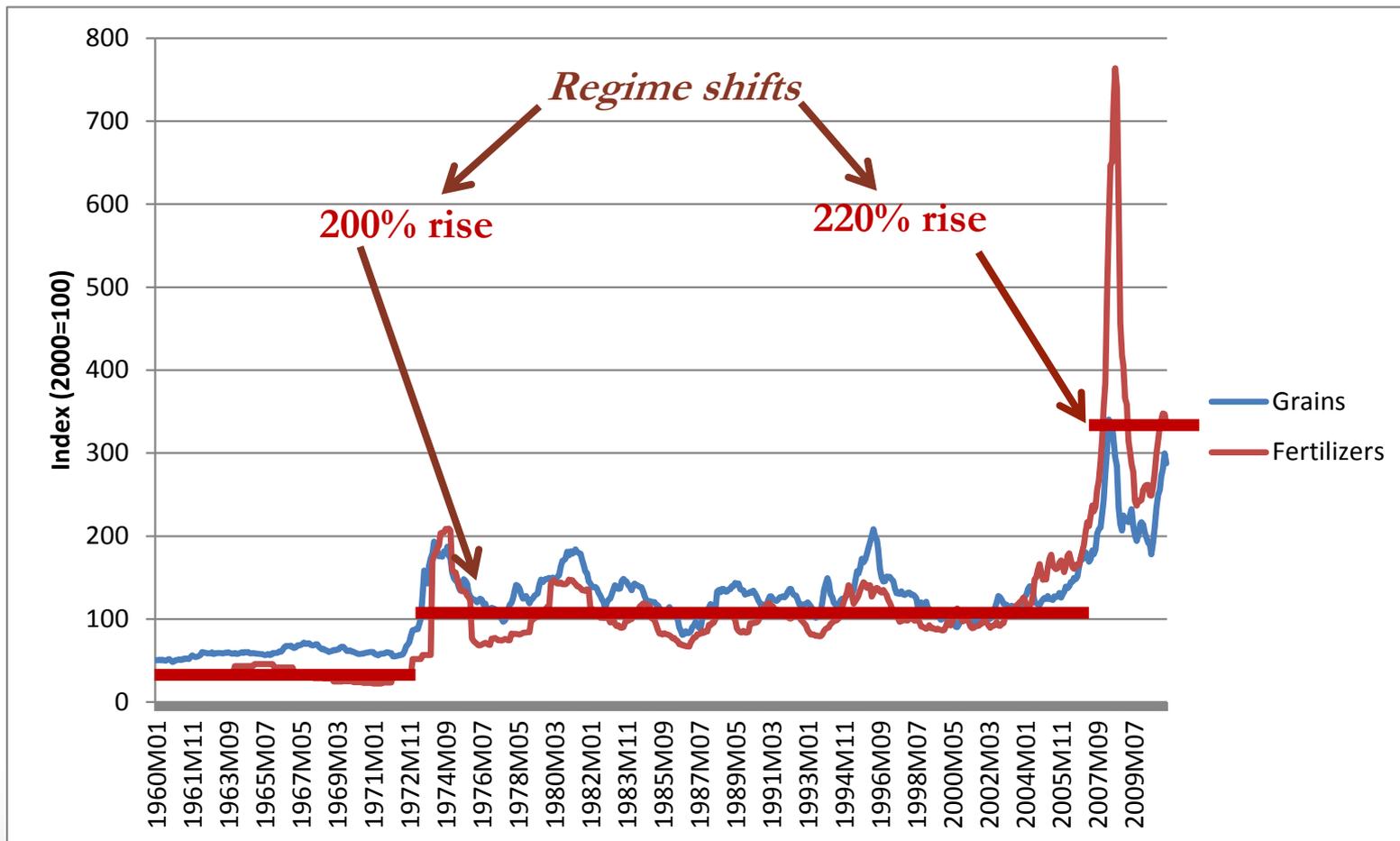
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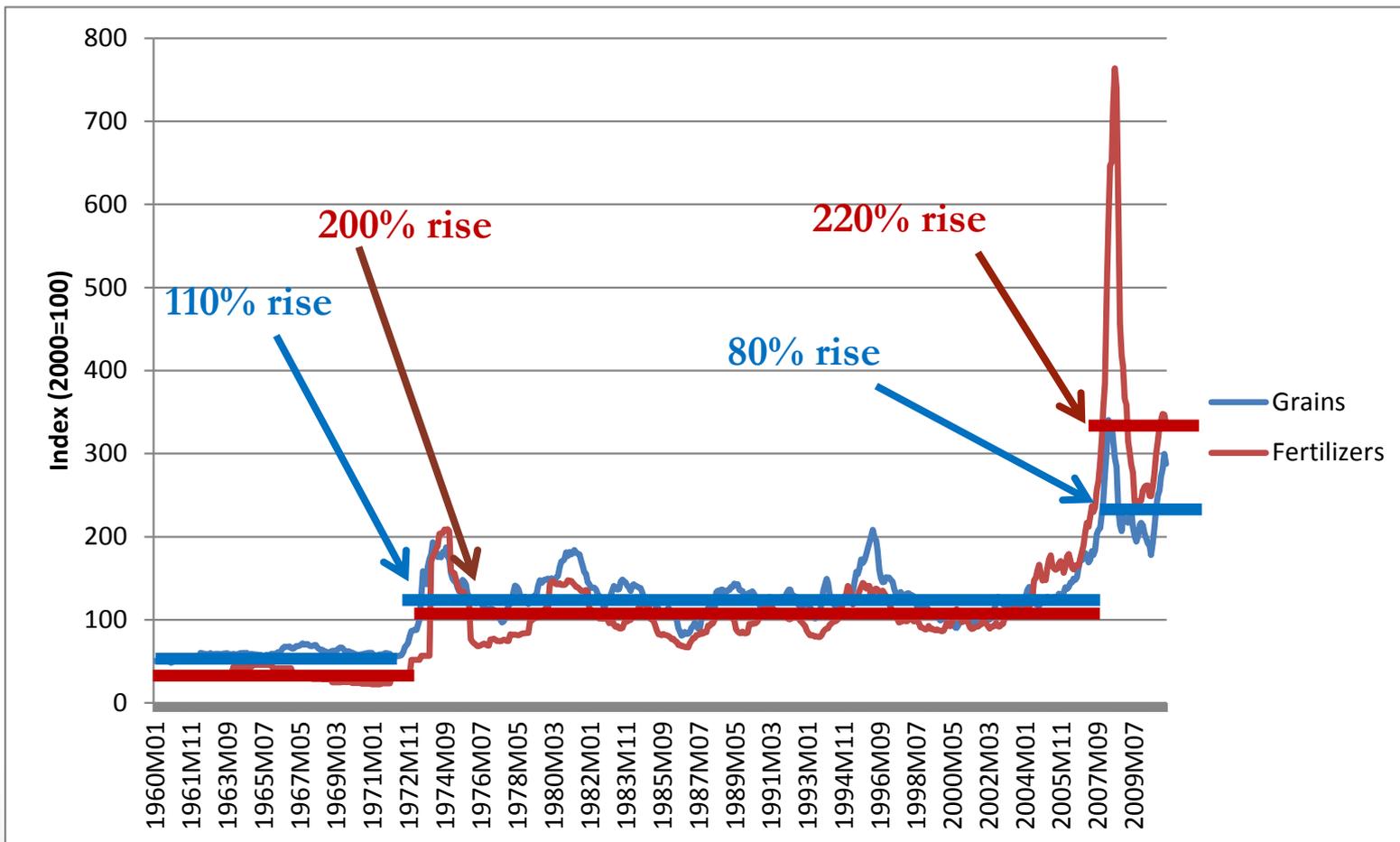
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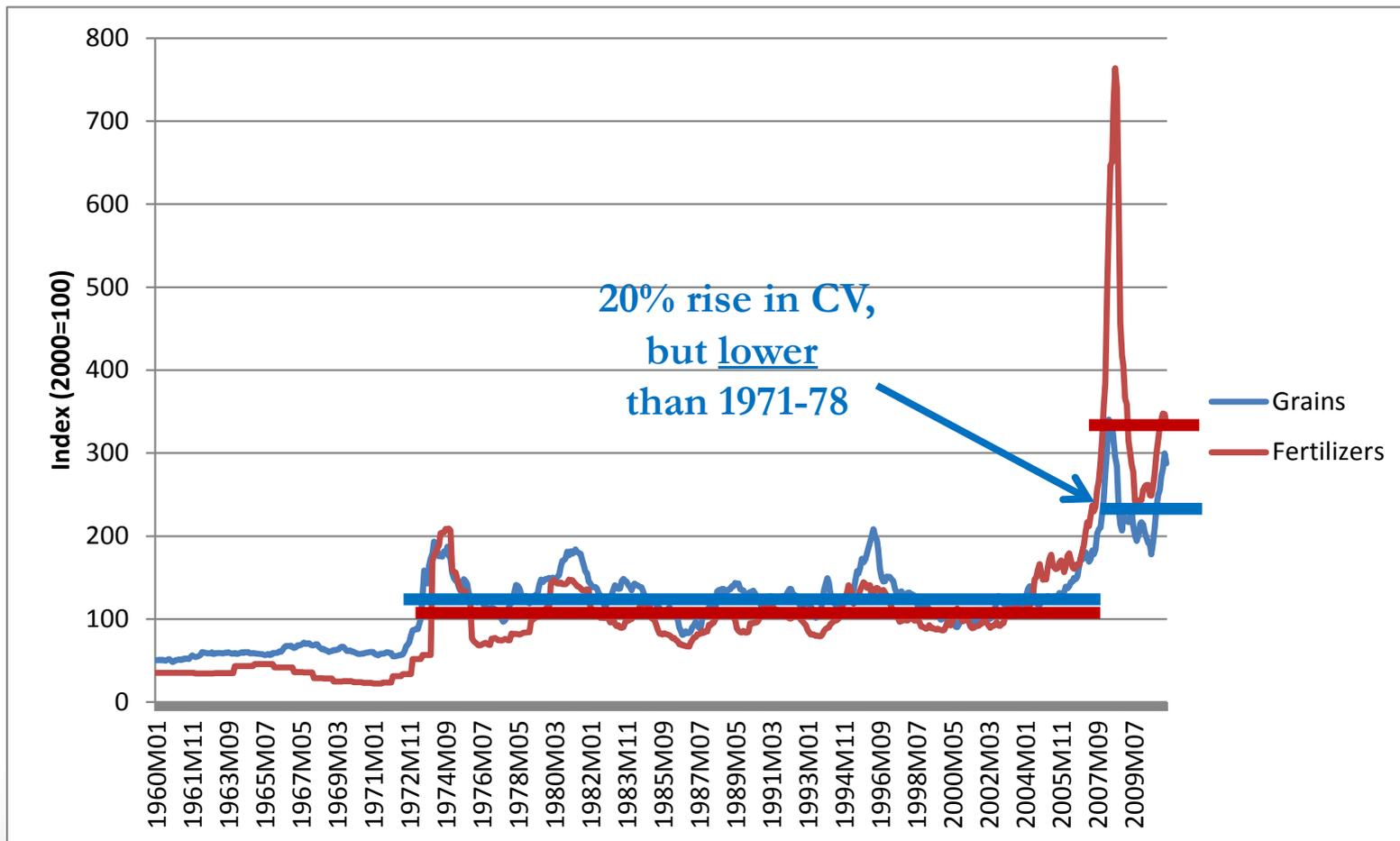
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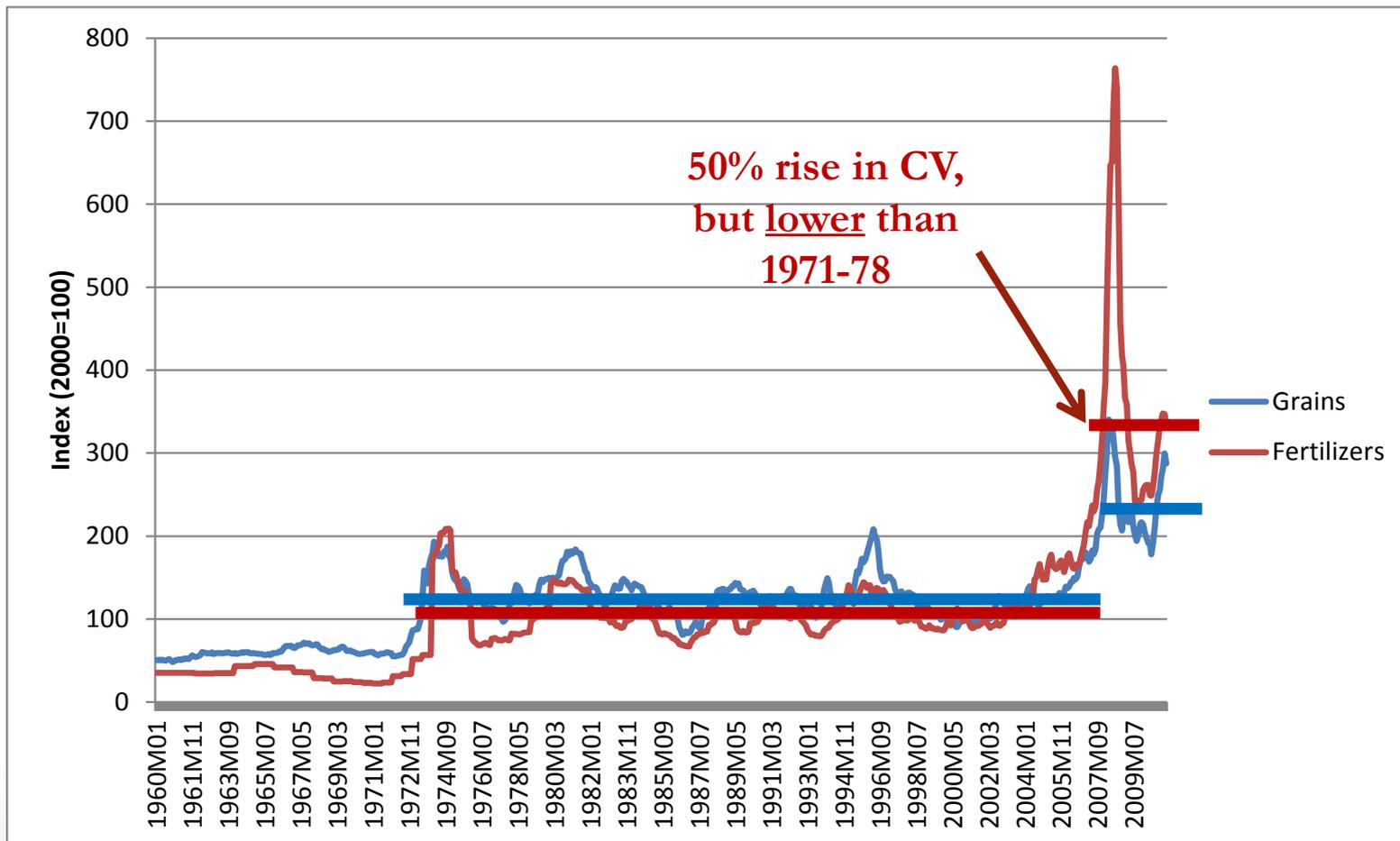
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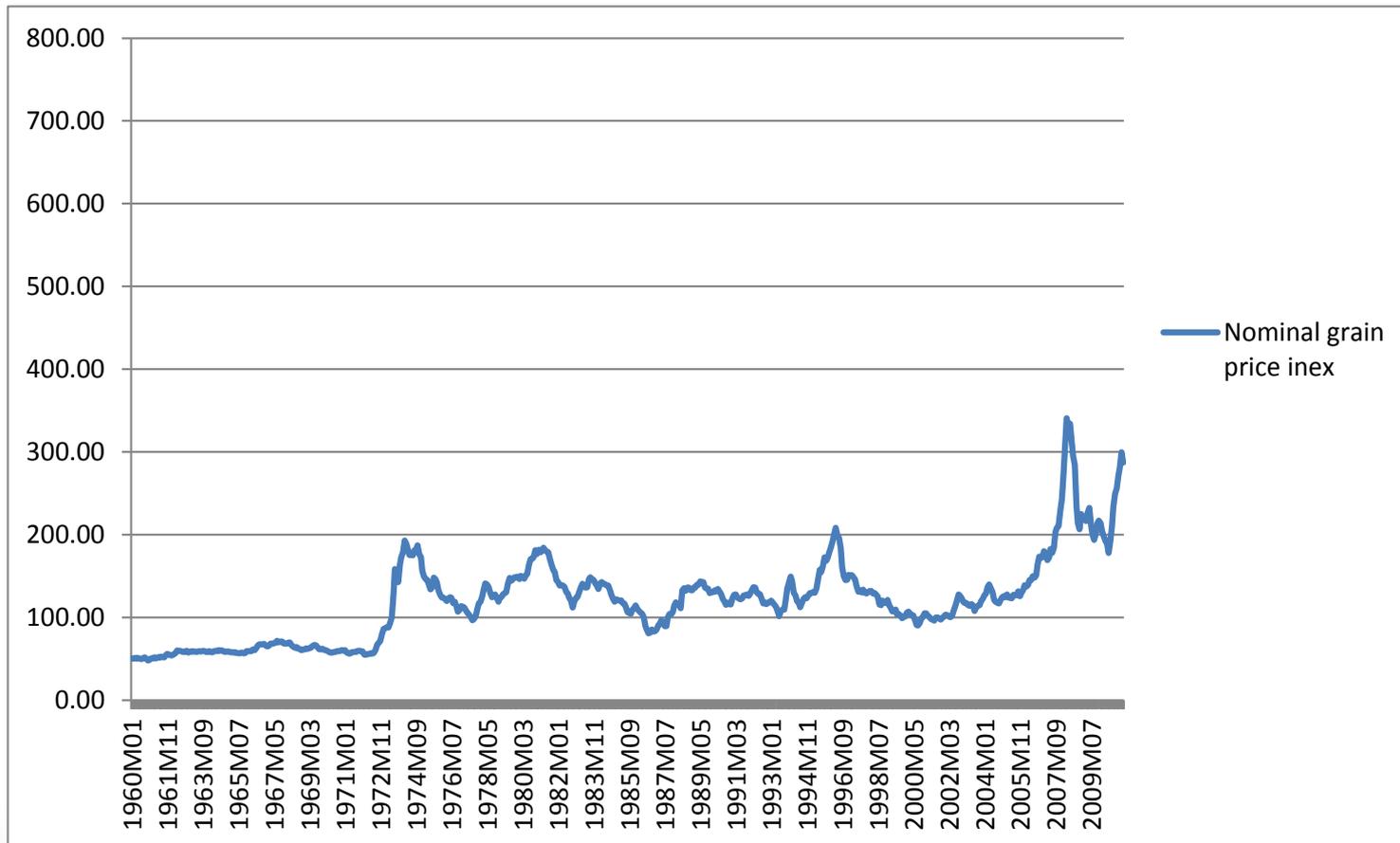


# Higher price levels – the long view

- Regime shifts driven by rising energy prices
- Fertilizer prices (and energy prices even more so) rising more rapidly than grain prices
  - Rising average worldwide productivity
- Coefficients of variation *not* higher now
- Yet prices continue to *fall* relative to average purchasing power (per capita GDP)

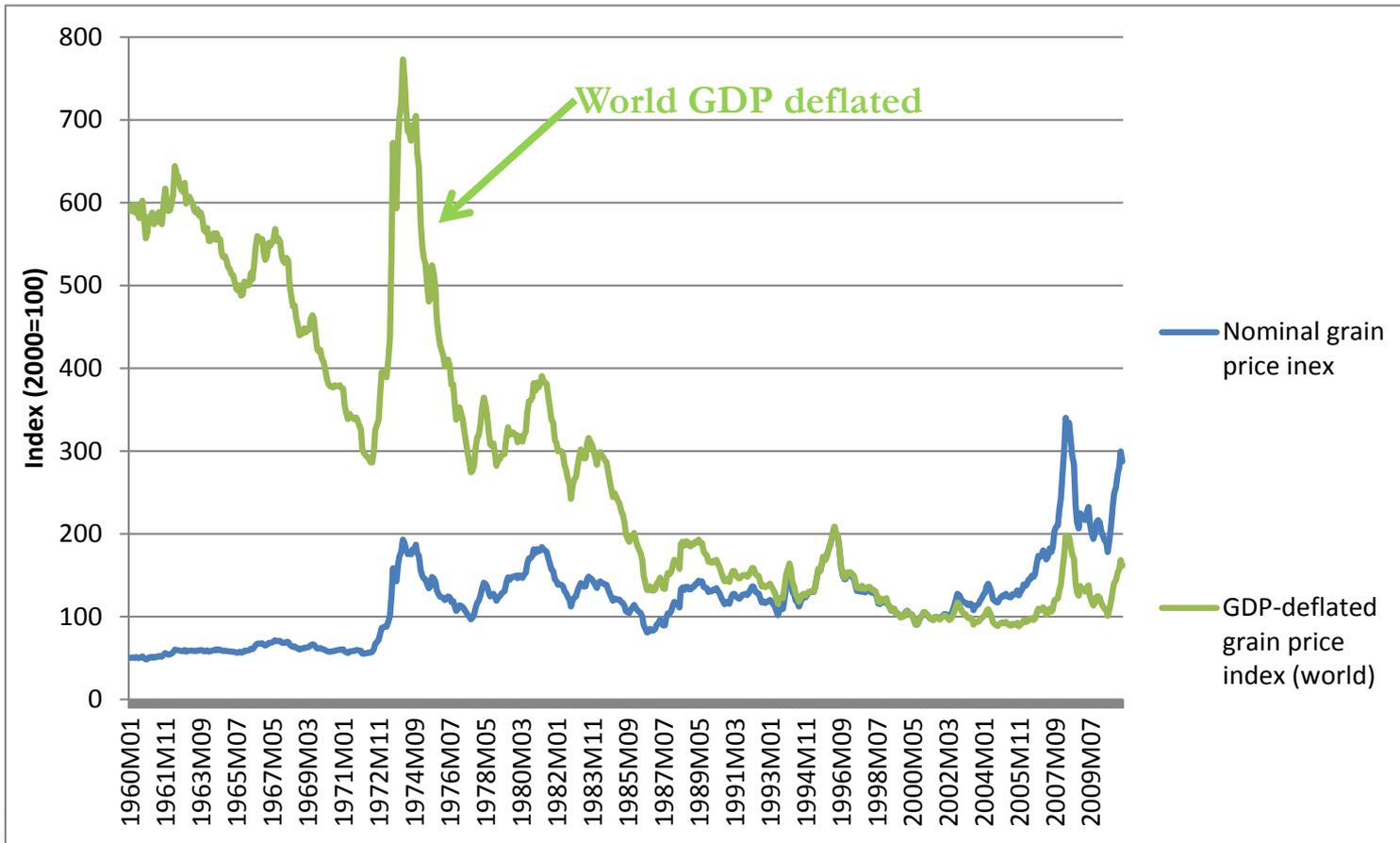
# Higher price levels?

**World Bank World Price Indices for Grains: Nominal and deflated with SSA and World per capita GDP (1960-2011)**



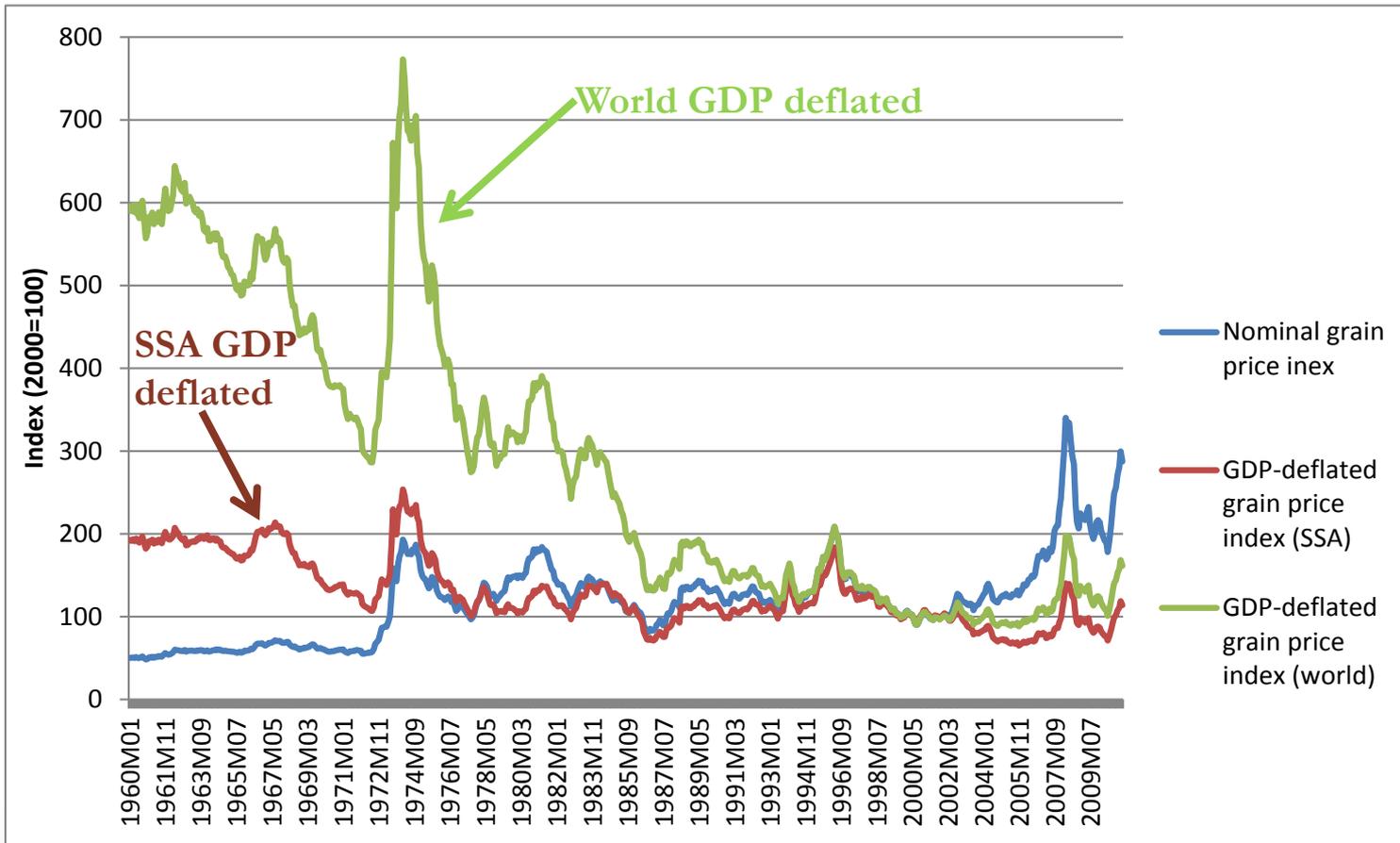
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World Bank World Price Indices for Grains: Nominal and deflated with SSA and World per capita GDP (1960-2011)



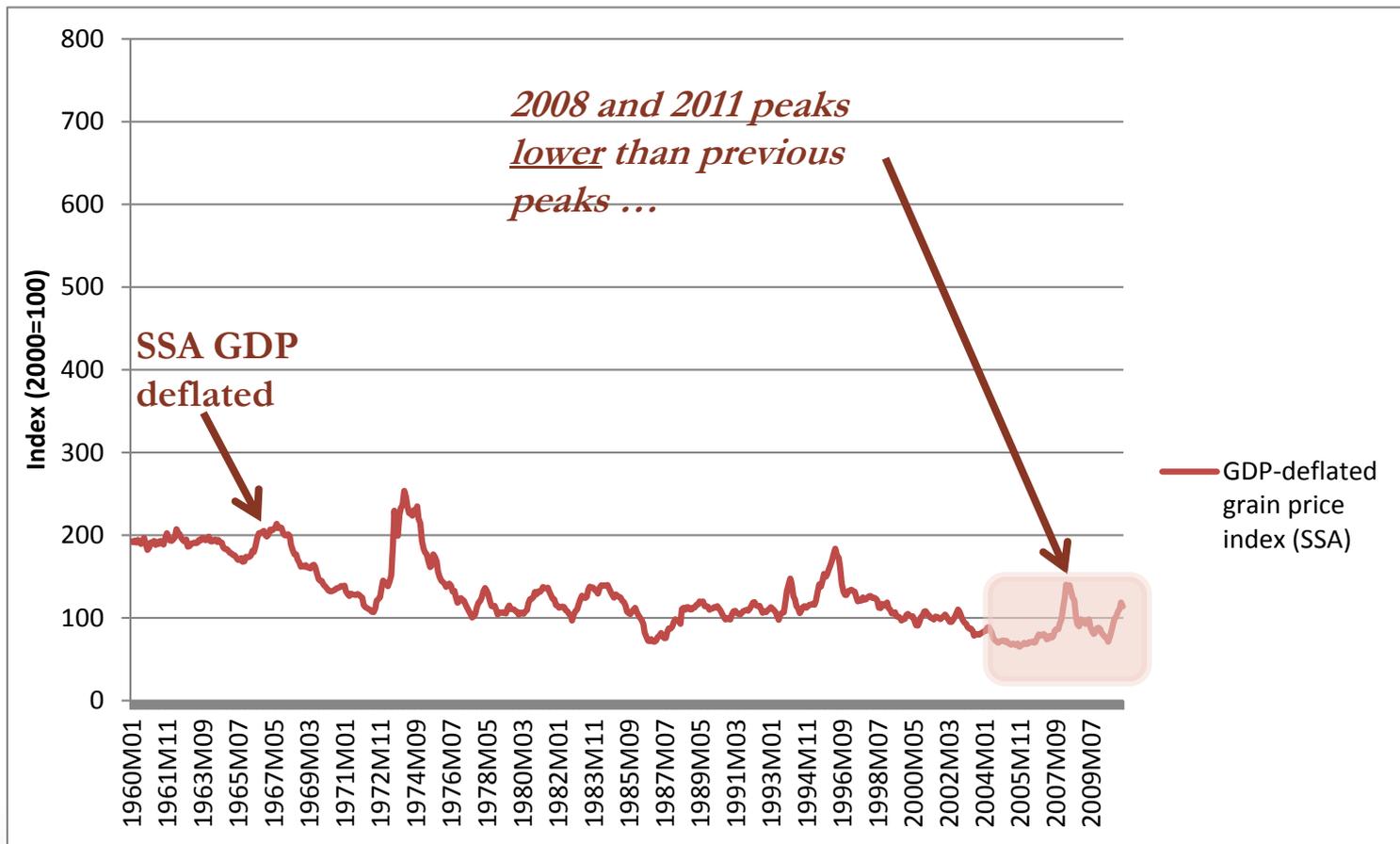
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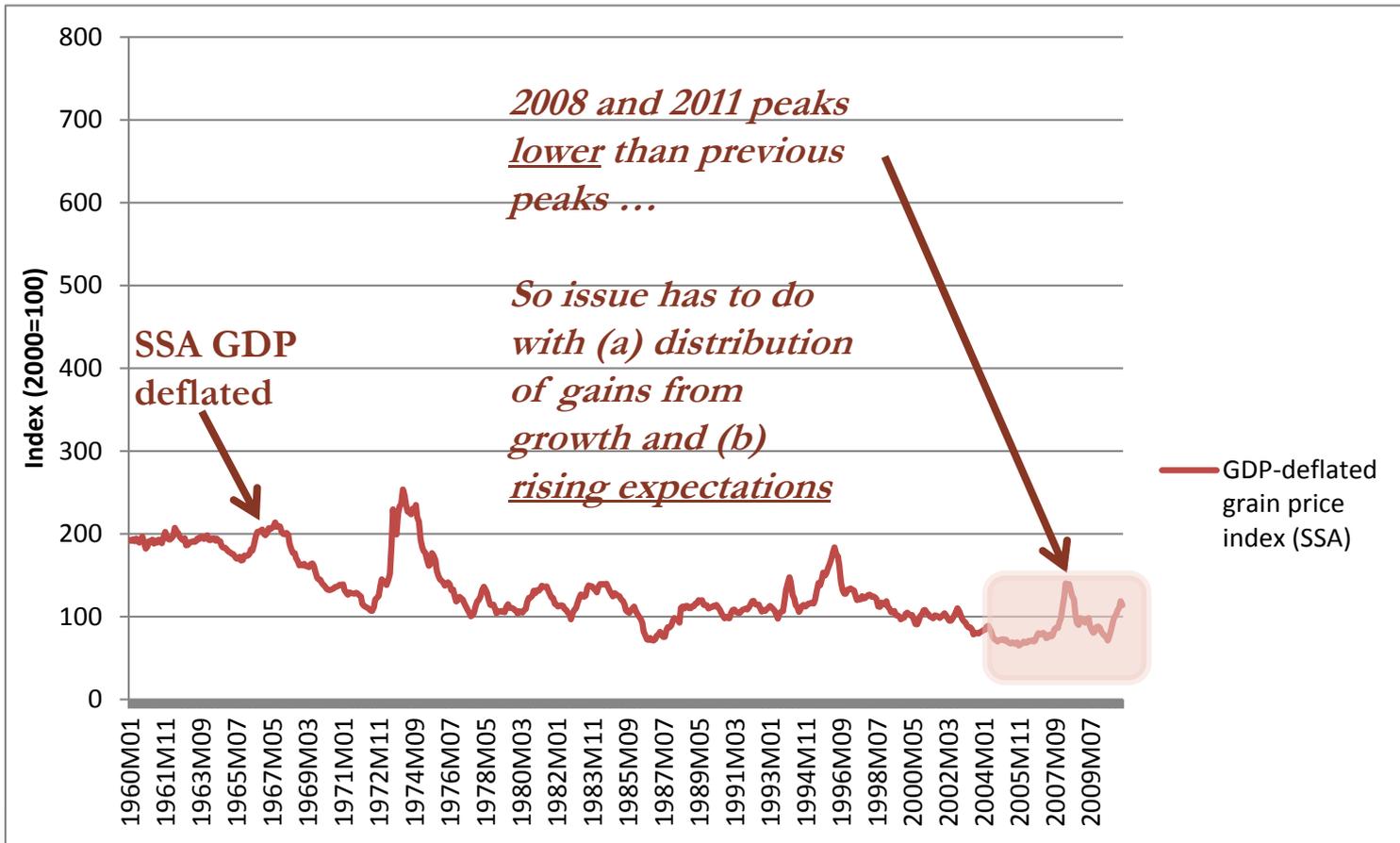
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# Higher price levels? (5)

World Bank World Price Indices for Grains: Nominal and deflated with SSA and World per capita GDP (1960-2011)



# Key observation # 4

*Price policy is a political issue*

# Food is political

- *“Citizens would willingly go to the market to buy food price stability, but such a market does not exist. Food price stability is a public good, not a market good. Understandably then, citizens turn to the political market instead.”*
  - Peter Timmer
- Competing culture, values, world views, pecuniary interests ... all drive the debate
- A multi-dimensional approach is needed

# Summary of key observations

- #1: Short-term price transmission from world to developing country markets has been low and variable
- #2: Drivers of volatility in developing country markets have been more internal than external
- #3: But price levels – and the distribution of gains from growth -- not volatility *per se*, may be the real issue
- #4: The food price problem is a political problem

# Some implications

- Volatility *per se* primarily hurts commercially oriented (market oriented) smallholder farmers
  - Most direct harm concentrated among 5%-10% of (better-off) smallholder farmers
  - But it also makes it harder for other smallholders to become more commercially oriented
    - A broader, longer-term problem
- High price levels help commercially oriented farmers, but hurt consumers
  - Urban consumers: Especially the poor, whose incomes have not risen as rapidly as those at the top
  - Rural net buyers: Though the level of purchases by these hhs is generally very low, reducing the impact on them

# Some implications (2)

- The distribution of gains from growth is a major issue
  - Prices continue to fall relative to average purchasing power
    - Especially in Africa!
      - Per capita GDP growth in Africa has exceeded worldwide averages since 2000
  - But many of the poor have been left behind
  - ... and rising expectations among urban poor fuel discontent

# What to do?

*Fundamental need to reconcile  
urgent short-term needs with  
long-term imperatives ...*

*Reconciling politics with  
economics*

# What to do? Long-term

- Exploit the opportunity to drive farm level productivity growth
  - The marginal value product of all inputs has risen dramatically!
  - Learn lessons about how sustainably to increase access to inputs
    - While building private input markets
  - Invest in varietal research
  - Invest in water control

# What to do? Long-term(2)

- Drive broad-based economic growth
  - Education
  - Health care
  - Water & sanitation
  - Communications infrastructure
  - Road infrastructure

# What to do? Long-term (3)

- Drive costs down in the marketing system
  - Reduce uncertainty with more rules-based government policies
  - Promote regional trade
  - (Invest in road infrastructure)
  - Improve marketing information
  - Promote competitive private trading systems
    - Financial systems
    - Clear rules of the game

# What to do? Long-term (4)

- Pursue regional dialogue to try to keep borders open
- Engage civil society in all these discussions
  - Evidence-based policy dialogue
  - Messy, but no other option
- Build capacity to generate solid empirical information and inject it into broad societal dialogue

# What to do? Short-term

- Safety nets
  - *“It may be that finding a way to ... deliver effective and efficient safety nets will be the key to allowing markets to deliver their long-run promise. If so, designing and implementing them becomes the essence of effective policymaking”* (Timmer, 2010)
    - Related to political nature of food price policy, which has real economic consequences
    - Also related to inequitable distribution of growth

# What to do? Short-term (2)

- Distinguish between emergency reserves and buffer stocks
  - The former are smaller, meant to cover gap until imports can arrive
  - The latter are explicitly meant to stabilize prices and so need to be large
    - Very poor record in Africa: High cost, opaque management lead to market disruption
  - Regional buffer stocks would face even greater problems

# What to do? Short-term (3)

- Combine relatively small emergency reserves with robust safety nets
  - Reserves = 2-3 mths consumption max
  - Layered safety nets
    - School feeding
    - Conditional cash transfers
    - Temporary food aid
- Remember that consumers can substitute in consumption
  - Cassava, sweet potato, sorghum, millet
  - Rice this time!

# What *not* to do

- Trade bans
  - India helped its consumers
    - But farmers lost and world prices were more destabilized
- Large-scale government procurement
  - Zambia lost nearly \$300m on its maize operations last year
    - Opportunity cost!
    - Who wins and loses?
- Generalized input subsidies
  - Poor targeting
  - Opportunity cost of the funds
  - Unsustainable

*Thank you*