# THE G-20 AND THE GLOBAL FOOD CRISIS

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## Framing the Issue

Food prices have reached peak levels not seen since the 1970s. Maize, wheat and sugar prices have doubled or tripled over the last year. Food prices are different from other prices since food is a necessity. The impact of high food prices is acutely felt by all households, especially those that are poor. There are also indirect economic costs. For example, as food prices increase, the discretionary income of households for spending on other items falls, which adds to the contractionary pressures of an already weak economy. In many developing countries, high food prices directly contribute to hunger and poverty. When governments try to shield their populations from the impact of high food prices through subsidies, it can lead to soaring fiscal deficits.

If food prices simply trended higher, one would expect more investment in food production and a significant supply response, which would bring prices back down. Yet, food prices have been very volatile in the last three years. For instance, the price of maize in July 2008 reached $287 per metric ton, fell to $158 in December 2008, remained at these levels through the 2009 recovery, but started to rise again in the second half of 2010. Maize prices peaked at $319 in April 2011, but have since fallen by about 10 percent. Managing food price volatility, as distinct from the price level, has become a serious problem for policymakers. When prices were low, there were high levels of suicides in India among farmers too indebted to provide for their families and sometimes violent protests in rural China against low government procurement prices. But, within a few months, prices spiked and the world saw demonstrations by urban consumers against high prices that may have contributed to the fall of some governments.

Food is one of the most politicized commodities in the global economy. The G-20's decision to address food price volatility is based on the recognition that collaborative solutions are needed to solve this problem. National policies on food and related areas are causing significant spillovers onto other economies, and undermining economic and social stability. Food policies are also a major obstacle in securing international trade agreements. The G-20 must break through the impasse.

## Policy Considerations

The G-20 is faced with three big policy issues on food. First, they need to take action to make food markets work better. Second, they should try to limit the damage to food markets that domestic politics are now creating. Third, they need to promote mechanisms to strengthen social stability to give households and farmers better ways of adapting to future price volatility.

### Markets

Food markets would probably have volatile prices even under the best of conditions. Both supply and demand are relatively unresponsive to price changes in the short-term, so minor changes in either can lead to big changes in the market equilibrium price. Storage costs are high with significant waste. But food markets are also much more volatile than necessary because of distortionary and discretionary national policies that compartmentalize food markets. Tariffs, non-tariff barriers, government procurement policies, subsidy policies and export restrictions affect local and international food prices. Increasingly, so do biofuel subsidies and other energy-related policies. Food prices today have become linked to energy prices through direct costs (fertilizer, pesticides and transport) and indirect costs (land substitution for non-food uses).

Markets work better when the underlying fundamentals of supply and demand are well known. But information on food is highly imperfect. The level of food stocks is a key variable, but only some countries report this information with any regularity. A proxy can sometimes be the amount of food being purchased by hedge funds for future delivery or even the volume of funds being directed into commodity exchange traded funds. But these funds are unregulated with few disclosure requirements.

When the private sector organizes markets, it puts a high premium on good information. In most countries, commodity exchanges are the places where such information is distilled and risks brokered. Such exchanges are just emerging in some African countries but they need to be linked into a virtual network, underpinned by privately-run warehouse receipt systems.

Most farmers, especially small-holder farmers in the developing world, are not yet integrated into global markets and food supply chains. These are the farmers that could make a substantial contribution to increasing global food supply because their yields are well below those that are attainable with existing technology and agronomic practices. African productivity is only half that of India, one-quarter that of China and one-fifth that of the United States. The technology to increase yields is well-known but requires investments. For example, 90 percent of Africa's agricultural land is rain-fed and subject to the vagaries of weather. Mechanized power to till the soil would do wonders to raise yields. So would the application of fertilizer and better seeds. Several African countries such as Malawi have had spectacular success in increasing production by adopting such policies.

### Politics

No progress has been made in dealing with the politics of food. One big issue is how to address biofuel policy. Biofuel could be consuming as much as 6.5 percent of the world's grain output and 8 percent of its vegetable oil, diverting valuable land away from food production. In many countries, biofuel policy is dictated as much by domestic politics toward specific rural constituencies as by technical considerations. Another big political issue is around trade barriers. Most domestic agricultural markets are highly protected, resulting in a fragmentation of markets. That is the opposite of what is required. Food price volatility will come down everywhere if markets are deeper and larger, and better able to smooth weather-related and other shocks more broadly across the globe. The political efforts of some countries to insulate themselves from shocks by imposing ad hoc export restrictions or other means are beggar-thy-neighbor policies that should be shunned.

### Social Stability

The third issue has to do with social stability. Here, the G-20 must recognize that hunger has much more to do with conflict, lack of income, inequalities within households in access to food, and lack of nutritional education than it has to do with global food supply. Most G-20 countries have social safety nets that mitigate the impact of high food prices on the poorest households, but most developing countries lack such programs.

## Action Items for the G-20

The G-20 proposal, endorsed by agriculture ministers, only tackles a small part of the problem. These include:

implementing a new agriculture management information system, developing norms around land purchases, establishing stocks in select locations and regulating hedge funds investing in commodities. But the big ticket items have not been agreed upon and G-20 leaders should push beyond what their agriculture ministers have agreed to. At Cannes, they should:

- Commit to providing more resources for investment in agriculture or at least to honoring their promises to fund the Global Agriculture and Food Security Program;
- Look to institutional development and assist Africa in the development of privately-held commodity exchanges;
- Discuss the links between biofuel policies and food prices, with a view to mitigating the impact of biofuels on food prices;
- Agree to avoid export restrictions on food;
- Make progress toward liberalizing trade in agriculture and reducing the most distortionary aspects of tariff escalation and non-tariff barriers.