

Javier Guzmán Calafell: Level and volatility of food prices: challenges and prospects

Remarks by Mr Javier Guzmán Calafell, Deputy Governor of the Bank of Mexico, at the panel on “Level and volatility of food prices: challenges and prospects” at the “Food security in a context of high food price volatility and low productivity in Latin America and the Caribbean: challenges and opportunities” international seminar, Guadalajara, 27 March 2014.

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First of all I would like to thank our three speakers, for having accepted the invitation to share with us their perspectives on the key aspects related to the high level and volatility shown by food prices in the last years. Given the importance of the topic, not only to Mexico but at the global level, and the quality and experience of our speakers, I have no doubt that this session will be of great interest to all of us.

After having shown a pronounced decline for several decades, international food prices started to increase at the beginning of this century, abruptly spiking in 2007–2008. Prices for these products fell at the end of 2008 within the context of the global economic crisis, but rose again to hit levels in 2011 that were even higher than those posted before the crisis. Although in the wake of this spike food prices have diminished, they still remain at very high levels. In addition, forecasts for the next few years suggest a complex scenario. For example, the OECD and the FAO estimate that food prices for the period 2013–2022 will be above, in real terms, those seen on average in 2003–2012.¹

The increase in food prices in the last few years has been accompanied by great volatility. According to calculations of International Monetary Fund staff, long-term volatility of food prices reached in 2009 its highest level in almost 30 years.² Naturally, price fluctuations for these products heighten challenges for economic policy and complicate significantly consumption and investment decisions by families and businesses. Some analysts have even emphasized that, viewed from a very long-term perspective, challenges stemming from the volatility of food prices could be more acute than those related to their level.³

The level as much as the volatility of food prices have significant repercussions for all economies, advanced or not, by affecting economic growth, inflation, public finances, the balance of payments, income distribution, poverty, and in some cases even political stability. However, the magnitude of the corresponding challenges has an inverse relationship with the level of development. Allow me to provide some additional information in this regard:

- The International Monetary Fund estimates that the median food share in total spending in advanced economies is 17 percent, compared to 31 percent in emerging and developing countries.⁴ In addition, it is important to keep in mind that in a number of these countries, or in specific sectors of the population, the corresponding figure is much higher.⁵

¹ OECD-FAO Agricultural Outlook 2013.

² Shaun K. Roache, “What Explains the Rise in Food Price Volatility?”, IMF Working Paper, WP/10/129, May 2010.

³ S.K. Roache, Op. Cit.

⁴ International Monetary Fund, World Economic Outlook, September 2011.

⁵ K. Anderson, M. Ivanovic and W. Martin, “Food Price Spikes, Price Insulation and Poverty”, Policy Research Working Paper, WPS6535, The World Bank, July 2013.

- In this context, it is not surprising that, according to World Bank calculations, the rise in food prices in 2010–2011 resulted in a net increase of 44 million in the number of people living in extreme poverty in developing nations.⁶
- Additionally, some recent studies conclude that increases in international food prices may give rise to a significant deterioration of democratic institutions, and to a higher number of internal conflicts, in poorer countries.⁷

This underlines the importance of clearly understanding the factors that affect both the level and the volatility of food prices, as well as the challenges that public policy must confront in this respect.

Clearly, fluctuations in food prices are largely determined by supply and demand factors inherent to these markets, such as the pace of world economic activity, demographic changes, the implications of higher income levels in some countries for eating habits, climate related factors, and the availability of water and arable land, among others.

However, the analysis becomes more complicated given that there are events outside the strict sphere of food markets which are affecting food price developments. It is worth to highlight in this regard that developments in energy markets affect food prices through a more intense use of energy in the production, processing, storage, and transportation of these commodities, as well as through the more widespread production of biofuels and the resulting rise in the use of food and agricultural inputs for this purpose. Second, a growing interconnection is being observed between financial and food markets, as reflected by the larger number of financial investors in primary product markets and the proliferation of financial derivatives tied to these products. It is likely that this also has had an impact on food price trends.⁸

In this context, it is clear that the design of policies oriented toward moderating increases in the level and volatility of agricultural and food prices, and dealing with their consequences when they are inevitable, faces significant challenges. I would like to highlight four of them, which from my point of view are particularly relevant. First, the design and implementation of the policies required to deal with the macroeconomic impact and the social costs of food price fluctuations. Second, the setting in motion of actions oriented toward overcoming structural difficulties that are affecting food production, such as low investment levels, infrastructure deficiencies, modest storage facilities, and the high concentration in brokerage markets. Third, the need to take into consideration that some of the policies that have been adopted to attenuate the effects of food price increases, such as export restrictions or tariff reductions in several countries simultaneously, price controls and subsidies, frequently end up having the opposite effect. Fourth, the importance of taking actions focused on improving transparency, the availability of information, and in general the functioning of markets for these products, in such a way as to provide adequate incentives for the adoption of schemes that stimulate productivity and competitiveness in this sector, contributing in this manner to a lower disparity in food prices, both across countries and regions, as well as through time.

⁶ World Bank, Food Price Watch, February 2011.

⁷ R. Arezki and M. Brückner, “Food Prices and Political Instability”, IMF Working Paper, WP/11/62, March 2011.

⁸ Nakaso, Hiroshi et al., “Report of the G20 Study Group on Commodities”, November 2011.