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RESEARCH NOTE

Weight to the Plate: Tracking EM Food Inflation

Elevated food prices could potentially add some near-term stickiness to already-high levels of general inflation in emerging markets.

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A combination of bad weather, export restrictions, low inventories, and robust demand has seen agricultural commodity prices surge over the past two years. This has led to a staggering jump in food prices, with the United Nations World Food Price Index hitting another record in January, rising 34% since 2019.

Rising food prices have added more pressure to headline inflation in emerging markets (EM), increasing steadily throughout 2021. As a result, most EM central banks have not had the leeway to wait to tighten policy the way the Federal Reserve and the European Central Bank have so far.

While energy inflation has been the primary focus, food price inflation is equally important for EMs. Companies tend to have shorter contracts with EM food distributors compared to developed markets (DM), meaning prices are more apt to reset much faster. Past spikes have also been connected to periods of social unrest, including the Arab Spring that swept through several nations more than 10 years ago.

Among regions, EM Asia appears relatively insulated against agricultural commodity pressures and may help keep headline inflation tame.

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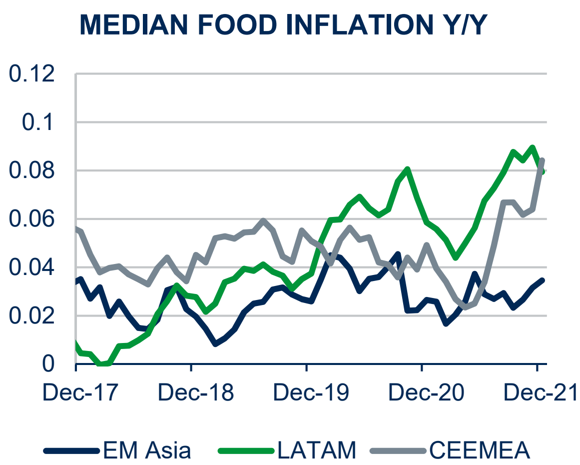
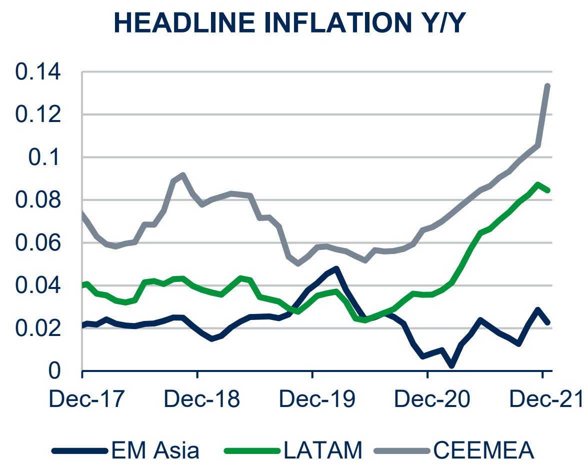
On the other hand, agricultural commodity prices are expected to remain firm this year, particularly among the largest components of EM food CPI—meat and cereals. As a result, economies in Latin America (LATAM) and Central & Eastern Europe, Middle East and Africa (CEEMEA), including Brazil and South Africa, are particularly exposed, potentially adding some near-term stickiness to already-high levels of general inflation.

While EM Asia has the largest weighting of food in its CPI (around 30%) compared to LATAM or CEEMEA (both around 20%), its food inflation has also been relatively more subdued. EM Asia stands out, likely due to the slow recovery in the region, but an important structural difference is the larger share of government-regulated prices there. Indeed, by some estimates, the share of administered prices in the CPI basket is around 20% for EM Asia, versus around 9% in other regions.

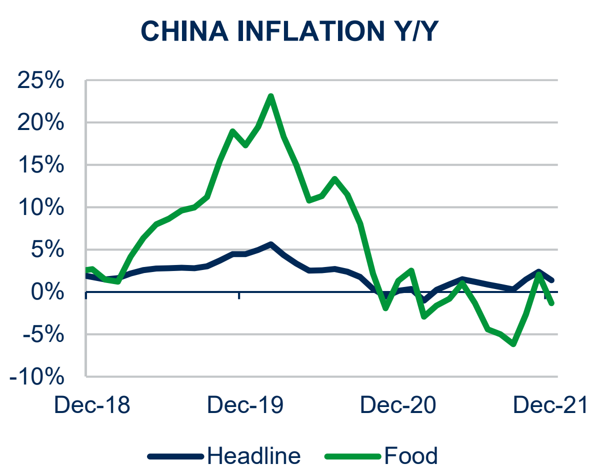


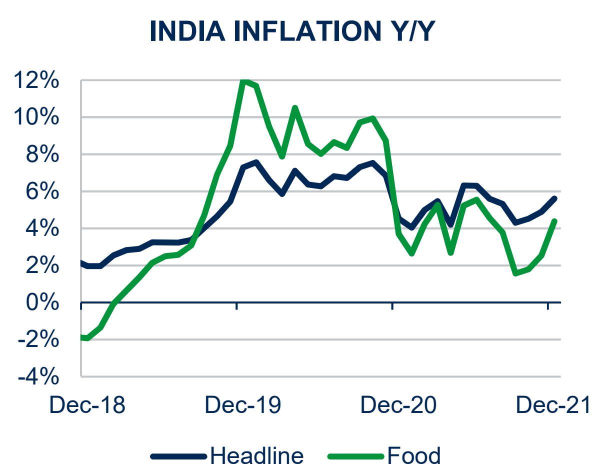


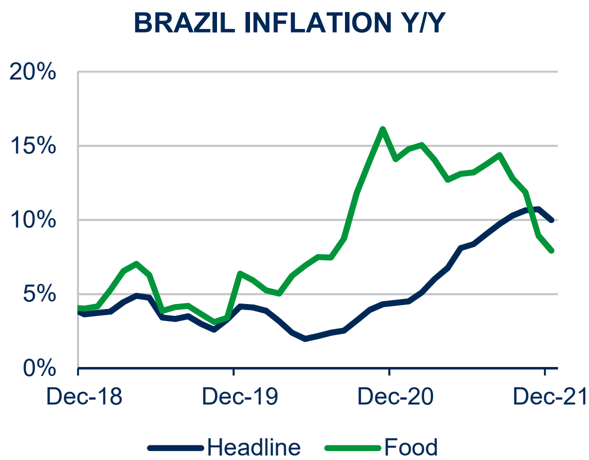
Source: Haver. As of February 9, 2022.
Note: **EM Asia -** China, India, Indonesia, Korea, Malaysia, Philippines, Taiwan, Thailand; **LATAM -** Brazil, Chile, Colombia, Mexico, Peru; **CEEMEA -** Czech Republic, Egypt, Hungary, Israel, Nigeria, Poland, Romania, Russia, South Africa, Turkey, Ukraine.

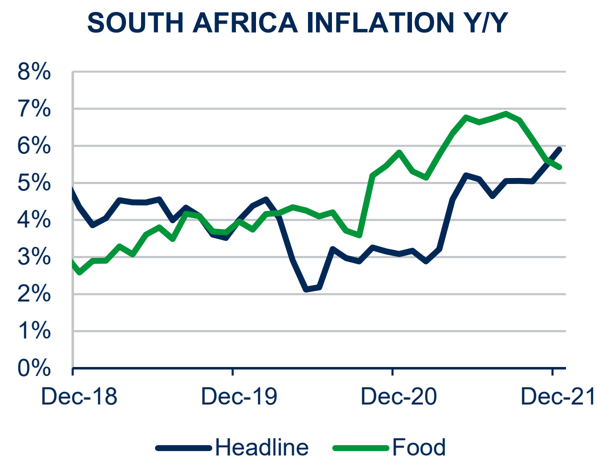
Both China and India actively intervene in managing supply or controlling prices to temper extreme moves in food and energy prices: China makes use of its national pork stockpiles; India has reduced import duties while also using national stockpiles to buffer large commodity price swings. However, government measures such as subsidies usually come at the cost of weighing on the fiscal balance—especially if the run-up in prices is prolonged.

Outside of EM Asia, with food inflation adding to upward pressures in headline inflation, central banks in LATAM and CEEMEA hiked more than 80 times over the course of 2021. There, monetary policy normalization has been well under way despite pandemic risks, with policy rates on average rising above 2019 levels.









Source: Haver. As of February 9, 2022.

	Weight Food CPI	Largest Component	2nd Largest Component
China	20%	Pork (2.5%)	Vegetables (2.5%)
India	46%	Cereals and Products (9.7%)	Milk and Milk Products (7%)
Brazil	21%	Meat (3%)	Bread and Cereals (3%)
South Africa	19%	Meat (6%)	Bread and Cereals (4%)

Source: Haver and Bloomberg. As of February 9, 2022.

While food price inflation has stabilized recently in Brazil and South Africa, meat prices are expected to remain high this year given strong global demand and higher feed costs, adding some near-term stickiness to already-high levels of general inflation.

Predating the pandemic, the Asian Swine Flu in China led to a general increase in consumption of beef as a pork substitute when stockpiles dwindled. This caused beef export prices in Brazil and other South American countries to increase significantly, driving high domestic cattle prices and general inflation.

China's rebuilding of pork stocks since last year also played a key role in the agricultural bull cycle, as Chinese agricultural imports grew about 50% in the last two years. This contributed to an increase in global feed demand and adds to already-elevated prices for grains and cereals, given disappointing production in corn and soybeans in South America.

With these pressures in mind, however, China seemingly stands out amid domestic oversupply issues with pork. This could continue to add weight to headline inflation, at least in the near-term, though with Chinese hog prices unsustainably low (below marginal cost of production), pork pricing should eventually increase over the medium-term.

Overall, as elevated food prices will likely continue to be another important driver in headline inflation, particularly given the outlook for meat and cereals, remaining elevated provides upside risks to the inflation outlook, though EM Asia appears best positioned to weather the ongoing storm.

IMPORTANT INFORMATION

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