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RESEARCH NOTE

The Food Price Conundrum: Can Markets Make a Difference?

Emerging Markets Sovereign Team

Leon Ernst, Paris & Ricardo Adrogue, Boston

With Russia's recent interruption of its tenuous deal to allow food exports through the Black Sea, global food prices are set to spike once again furthering global inflationary pressures and raising potential destabilizing political movements across several emerging market economies. While the COVID-19 pandemic disrupted global food markets, the Russian invasion of Ukraine has delivered a much bigger shock that has since been aggravated by drought and food export restrictions. Even if Moscow returns to allowing exports, the market uncertainty will keep prices elevated.

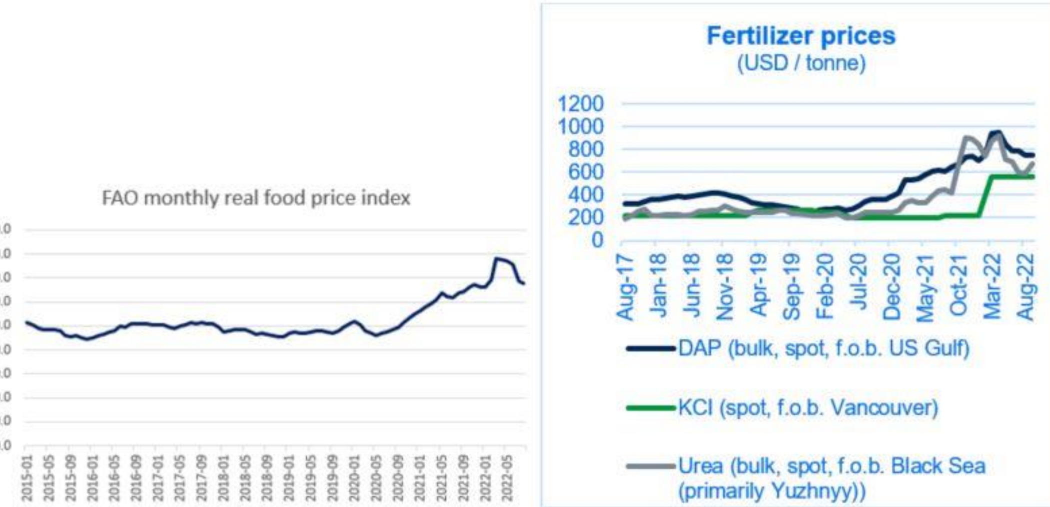
However, as the war continues, some relief is possible if market forces are allowed to work again. For example, a large part of the global food production is held back by export restrictions, which could help to ease tensions on the global food supply and on food prices. While food production is fairly inelastic in the short term, history has shown that pro-market policies over time can lead to increased food production. These policies are crucial to bring down food prices from recent highs. However, more changes will be necessary in the long-term as we face a growing population and, with that, growing food demand. Only a combined global effort is likely to solve the long-term issue of food insecurity and food shortages.

Russia, Ukraine, and the Global Food Supply

Russia and Ukraine emerged as major agricultural producers after the fall of the Soviet Union; in 2021, the two countries exported about 12% of the food calories traded. Both countries are major exporters of wheat, maize, and sunflower oil, where the two countries account for 34%, 17%, and 55% of global exports, respectively. After Russia's invasion, the real food price index increased by nearly 32% from a year earlier—the highest value since the index was created in 1990. Exports of Ukraine's food commodities have been severely hurt due to infrastructure damage and port closures.

Ports that typically channeled about 90% of Ukraine's exports were closed until a deal brokered by the United Nations and Turkey in August. From August to October, nearly 400 voyages carried more than 9 million metric tons of grains and other foodstuffs.[1] To compare, Ukraine in 2021 exported on average 4 million tons of grains, including wheat, maize, and barley, as well as 430,000 tons of sunflower oil per month. Russia announced it would stop allowing exports following attacks on its Black Sea fleet, but quickly reversed the decision, making any supply forecasts all the more difficult.

[1] Source: https://www.un.org/en/black-sea-grain-initiative/vessel-movements



Source: Food and Agriculture Organization of the United Nations, Index Mundi.

Fertilizer prices have also risen sharply. Even before the war, Russia's threat to cut gas supplies to Europe led to uncertainty and price increases. Russia was the largest exporter of nitrogen fertilizers and the third-largest exporter of potassium fertilizers. By September, prices of diammonium phosphate, urea, and potassium chloride were on average still up by 78% Y/Y.

The European drought this summer boosted grain demand and is expected to have further curtailed Ukraine grain production. In September, the Ukrainian grain harvest was still down by 44% Y/Y, to 26.1 million tons.

Global Market Restrictions

Almost as important as the war and the drought have been selective food export restrictions that drive global prices even higher. Governments try to keep the food they grow for their own populations, but it makes the global situation much worse. Fewer countries have implemented restrictive export measures than during the 2008 food crisis, but the number of restrictions themselves have proved far more severe.[2] According to the World Bank, India's export bans on rice led to a price increase of 12.3%, Russia's restrictions on wheat exports boosted prices by 9%, and Turkey's limits on citrus fruits drove up prices by 8.9%. Turkey exports a relatively small share of global soya bean oil and maize supplies, but demand for these goods tends to be rather inelastic, and therefore the impact on price development has been significant. Prices moved up by about 14% on soya bean oil and by around 6% on maize in the first half of 2022 alone.

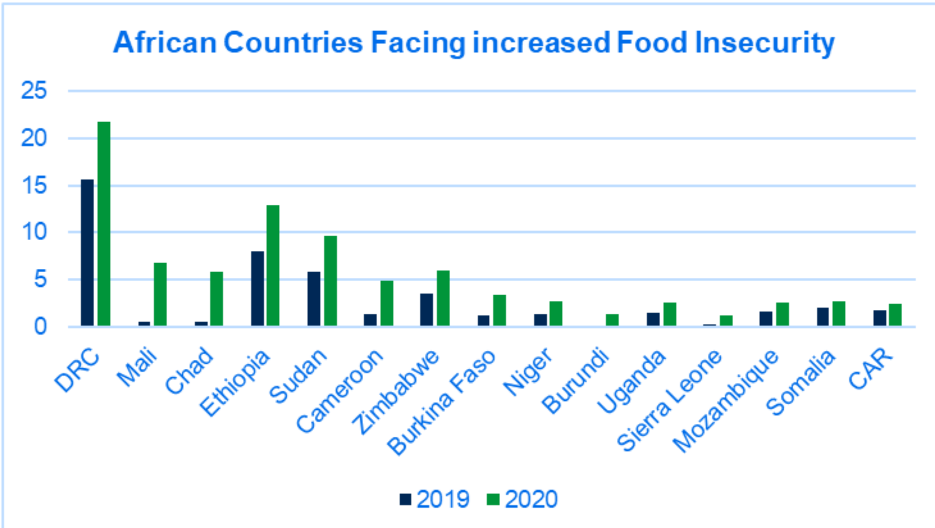
Hunger and Instability

Tajikistan, Uzbekistan, and Azerbaijan were most severely affected by the globally implemented restrictions as a share of overall imported food calories.[3]

Hunger, undernourishment, and socio-political instability are all consequences of the ongoing food crisis. The latest score for the Global Hunger Index, as of 2021, shows the regions most severely affected have been

[2] David Laborde Debucquet and Abdullah Mamun from the International Food Policy Research Institute.
[3] Ibid.

Sub-Saharan Africa, South Asia as well as West Asia, and North Africa.[4] A more precise look at Africa shows how food insecurity increased from 2019 to 2020, the latest available data. As global conditions have worsened since then, food insecurity in some of these countries should have supposedly increased further.



Source: https://africacenter.org/spotlight/food-insecurity-crisis-mounting-africa/.

An alternative look at the same problem is provided by the Integrated Food Security Phase Classification (IPC) and the 2022 Global Report on Food Crises Mid-Year Update, from the Food Security Information Network, showing that large portions of emerging market countries' populations are borderline food insecure or in an acute food and livelihood crisis. South Sudan, Yemen, Afghanistan, and the Central African Republic have been especially hard hit.[5]

Market Reforms Remain Key

Key to avoiding a further worsening of the situation will be to increase food supply globally or stabilization of the geopolitical situation, but it remains difficult to predict how the war will evolve. Looking at potential new suppliers of food might be more fruitful.

If history is any guide, free-market economic policies have proven to be effective at increasing global food production—and their reversals equally as effective at reducing it. Ironically, the example of Russia itself is useful. A large grain-producing region that, following the communist revolution, became a net importer of cereals and roared back to being a major grain producer in 2000, production leapt from 30 million tons per year in the early 2000s to 60 million tons by 2010, to 85 million tons in 2020.[6]

Where might the new supply come from? It is still difficult to tell. The policies needed to boost supply are quite predictable. How likely such policies are to be implemented where they are needed, however, is anyone's guess.

[4] *Source: Global Hunger Index, https://www.globalhungerindex.org/trends.html*

[5] *Source: https://www.fsinplatform.org/sites/default/files/resources/files/GRFC%202022%20MYU%20Final.pdf*

[6] Source: https://www.ers.usda.gov/webdocs/outlooks/39804/34899_whs13a01.pdf?v=4135#:~:text=In%20the%20late%20Soviet%20period,centrally%20planned%20to%20market%20economies

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