



DEPARTMENT OF
AGRICULTURAL, ENVIRONMENTAL,
AND DEVELOPMENT ECONOMICS

“High Food Prices and Riots: Trade Policy vs. Safety Nets”

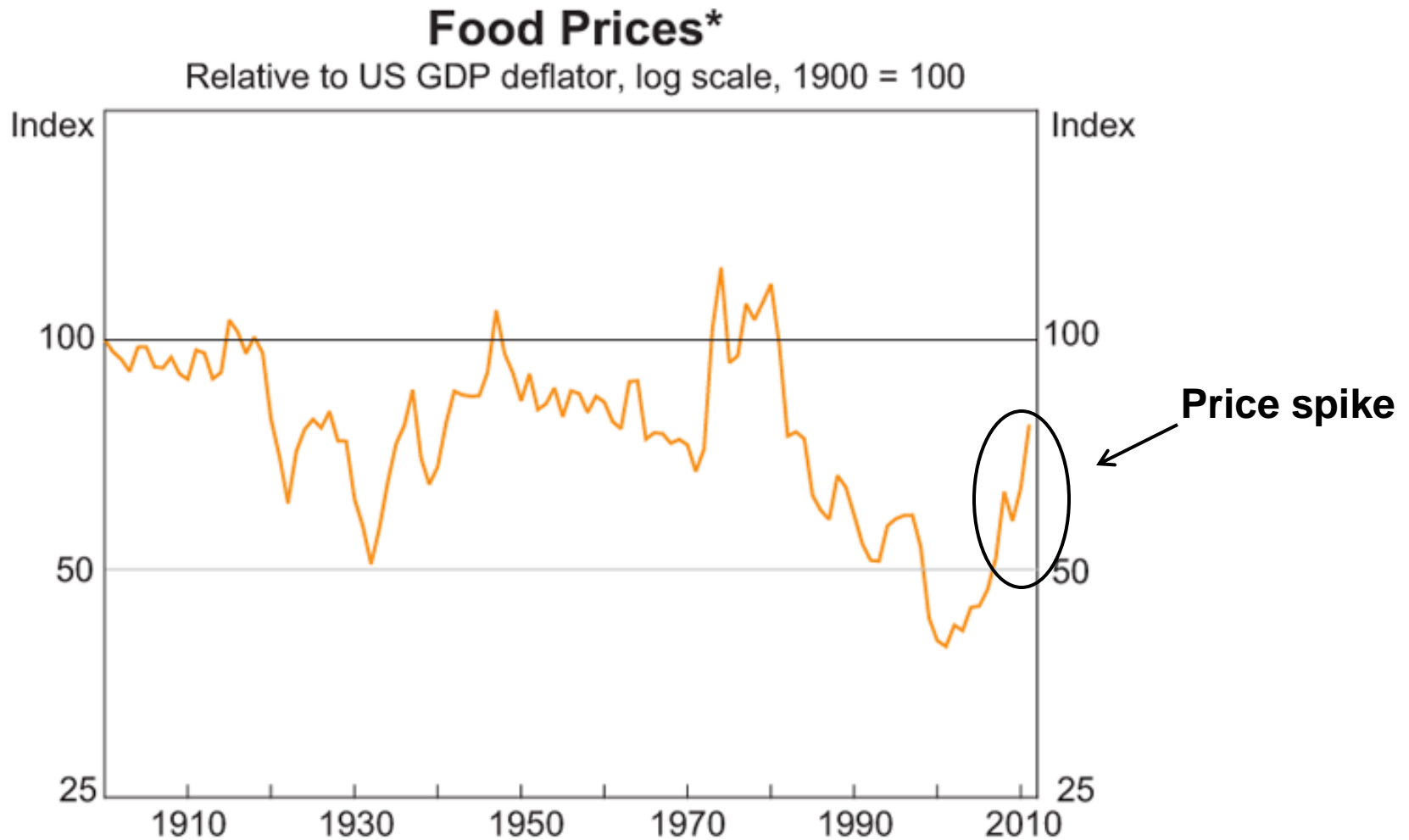
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Spikes in World Food Prices

- **Since 2007 – world prices of key staple foods volatile around relatively high levels**
- **Different to pattern over past century where real food prices have trended downwards**
- **Historically, while price spikes are often intense, they have typically been infrequent**
- **Since 2008, three price spikes: early 2008, early 2011, and third quarter of 2012**

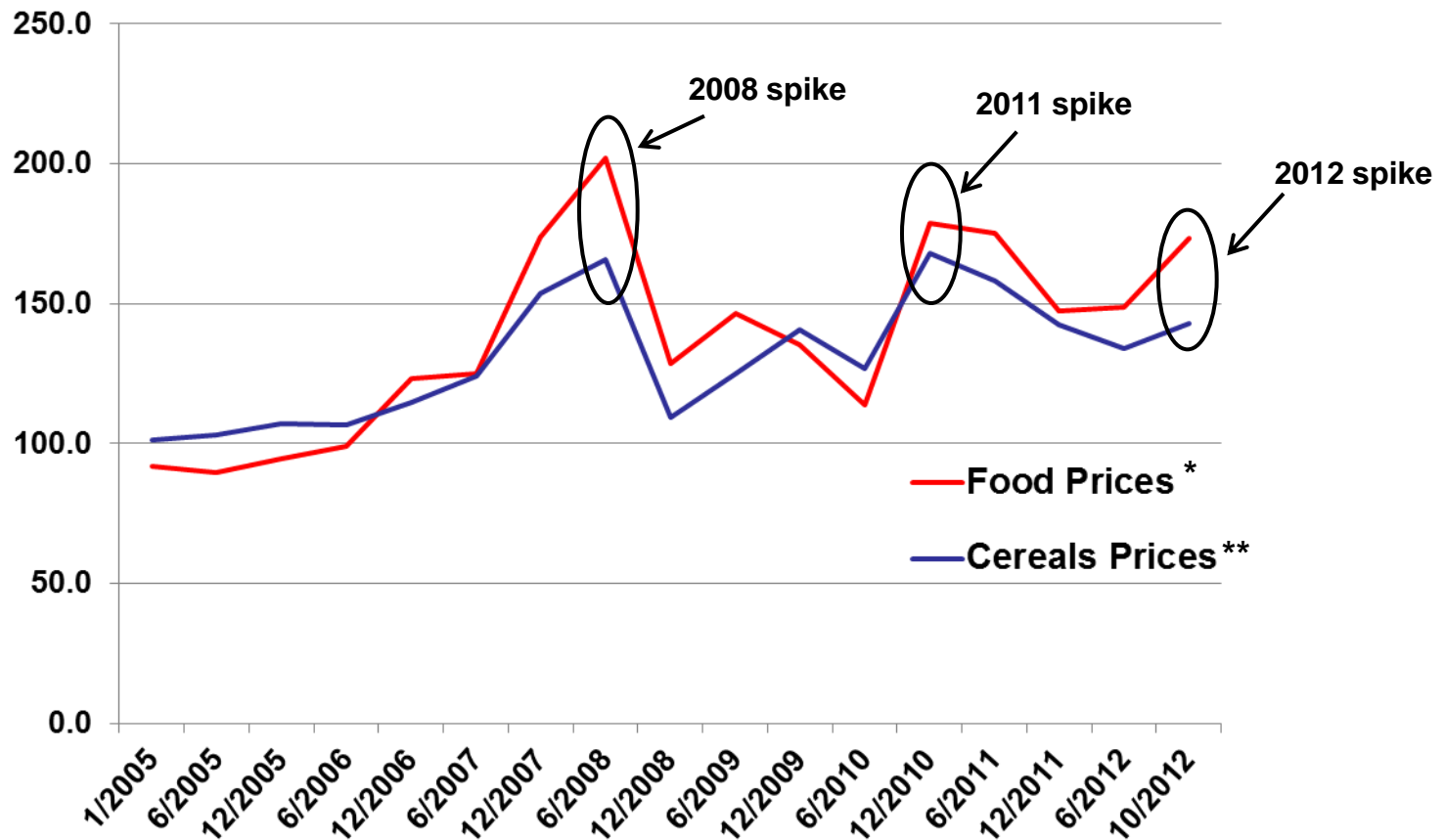
Real Food Price Trend



* Equal weighted (geometric) index of 11 commodities; extended from 2004 using IMF commodity price series; latest data point is 2011 to date
Sources: Global Financial Data; IMF; RBA; World Bank

Recent Food Price Spikes

FAO Real Food Price Indices (2002-04=100)



*Food price index based on average of 5 commodity groups (meat, dairy, cereals, oils and fats, and sugar)

**Cereals prices index based on wheat, maize, and rice prices

Response to Food Price Spikes

- **Many developing countries have responded to food price spikes by directly intervening to stabilize domestic markets**
- **2008: 68 countries used trade policies and 35 released public stocks at subsidized prices (FAO, 2008)**
- **Trade policies have consisted of export controls, import subsidies and tariff reductions**
- **In contrast, developed countries have typically not implemented such policies**

Standard Policy Advice

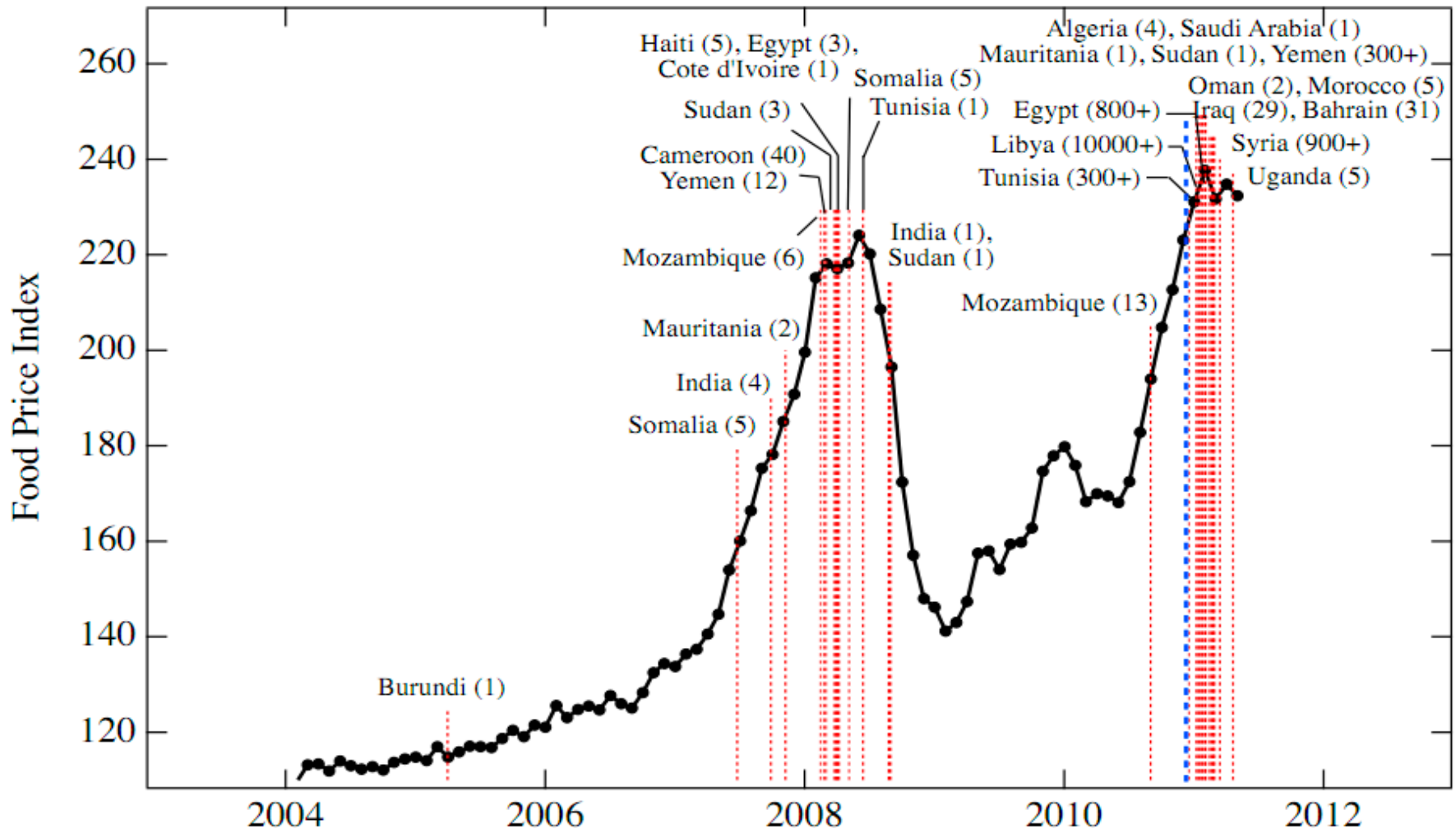
- **1945-80, focus on price stability through production, border and stock controls**
- **Post-1980, price stability considered less desirable - production, trade and storage decisions should be guided by market prices**
- **Policy advice: market-based risk-management tools in combination with safety nets**
- **Drew criticism after price spikes:**
 - **risk-management tools often unavailable**
 - **safety nets too complex to use**
 - **poor food importing countries hurt most**

Political Impact of Higher Prices

- **Higher food prices found to increase poverty sharply in short-run (World Bank, 2012)**
- **Research suggests food riots are correlated with high food prices (Bellemare, 2011)**
- **Intervention a matter of political survival in countries with large poor populations**
- **Indian Prime Minister and Indonesian President both re-elected in 2009 after campaigns emphasizing ability to limit impact of food crisis in respective countries**

Impact of Higher Food Prices

High Food Prices and Political Unrest

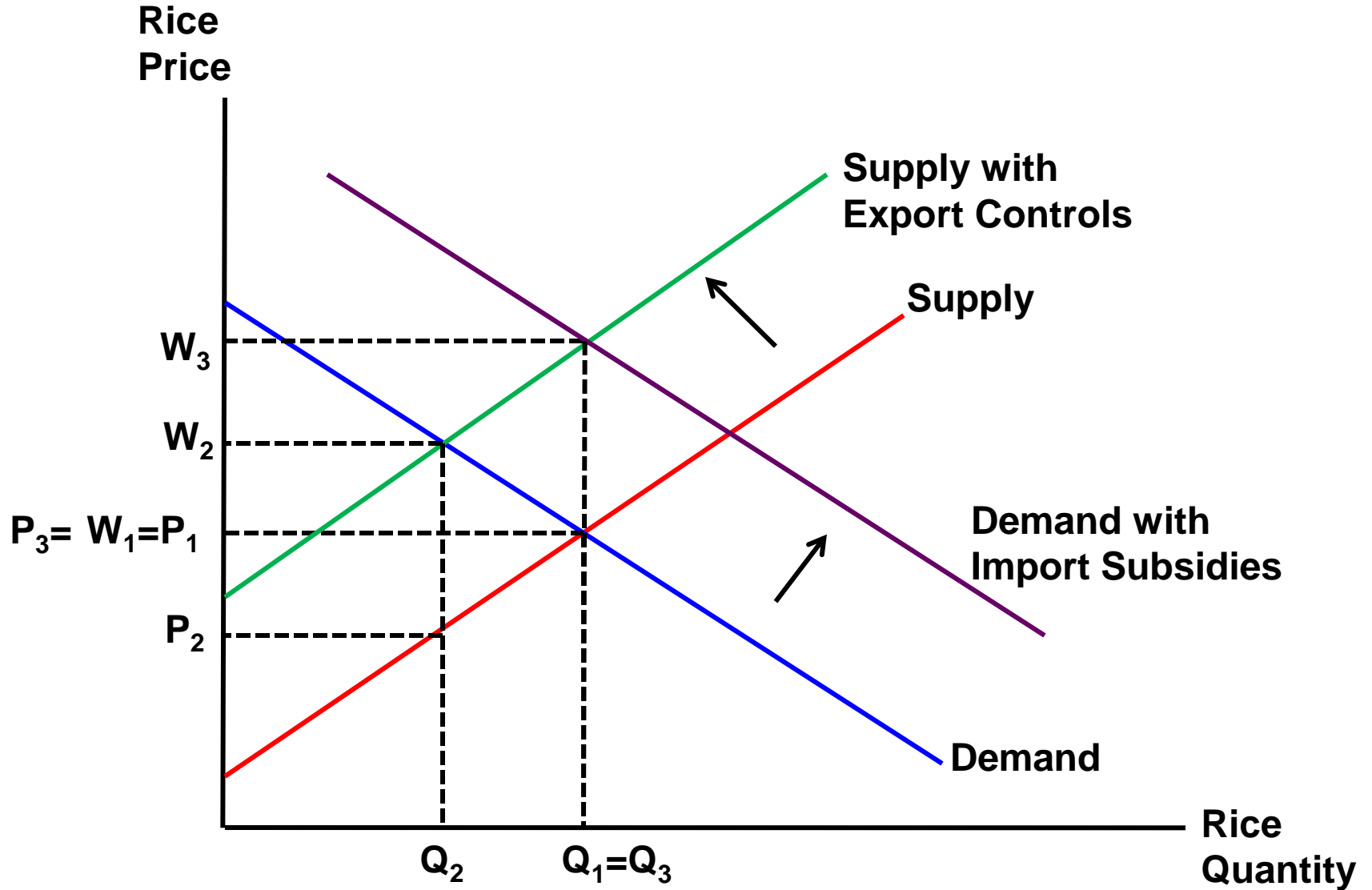


Source: Lagi, Bertrand and Bar-Yam (2011)

Beggaring Thy Neighbor....

- **If enough countries adopt trade policies, end result is increased world food price instability**
- **“...export restrictions play a direct role in aggravating food crises...” (Pascal Lamy, Director General of WTO, 2011)**
- **40%, 19% and 10% of 2007-08 spike in rice, wheat and maize prices respectively due to trade policies (Anderson and Nelgen, 2012)**
- **Unless countries cooperate over not using trade policies, each has unilateral incentive to intervene, but collectively no better off**

World Rice Market



Safety Nets

- **Mixed record of stabilization policies has led to focus on risk management and safety nets**
- **Latter are non-contributory targeted transfers designed to provide assistance to the poor following price shocks**
- **Various forms: cash transfers, food stamps, food-for-work, and cash-for-work programs**
- **Provide insurance to poor who have limited access to formal coping mechanisms – i.e., *entitlements* matter (Sen, 1981)**

Safety Nets

- **Often complement stabilization policies, which may be insufficient to protect purchasing power of poor**
- **In response to 2007-08 food price spike, 23 countries used cash transfers, 19 food assistance, and 16 chose policies to increase disposable income (FAO, 2009)**
- **Safety nets have been crucial in protecting poor from price increases – e.g., Mexico's *Progresa* program**
- **Options for transfers also improving**

Safety Nets vs. Trade Policies

- **Why are safety nets not used more often?**
 - **Hard to scale up/down depending on need**
 - **Fiscal constraints**
- **Trade policies often less costly, and also politically popular if safety nets leave share of middle-class unprotected**
- **Despite being targeted, safety nets may still distort world prices, i.e., result in exports being reduced/imports increased**
- **However, trade policies tend to over-react to shocks while safety nets tend to under-react**

Disciplines on Trade Policy

- **Trade policies often appear successful in stabilizing domestic prices, but end up exacerbating world price spikes**
- **Solution to prisoner's dilemma is cooperation via a self-enforcing agreement, i.e., the WTO**
- **Current Doha Round pushing for reductions in tariffs and disciplines on export subsidies**
- **Developed countries also pushing for tighter WTO disciplines on export restrictions – but rejected by exporting developing countries**

Reconsidering Biofuels Policies

- **Developed countries did not use export policies in response to recent price spikes as compared to 1973/74**
- **However, developed country policies on biofuels have had large terms of trade effects for coarse grains, oilseeds and sugar**
- **Mandates also result in demand for biofuels being unresponsive to food prices – as a result harder to moderate price shocks**
- **Focus should be on developing biofuels that have a less distorting effect on world prices**