

THE GLOBAL FOOD CRISIS: CAUSES AND POLICY RESPONSE

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Introduction

The recent increases in the price of food, especially of staples, have reduced access to food for many people - particularly the poor - in a large number of developing countries.¹ This has created significant humanitarian, socio-economic, developmental, political and security-related challenges. The consequences of the crisis are most pressing in low income, net food-importing countries - particularly Least Developed Countries (LDCs), where, on average between 50-80 per cent of personal income is spent on food.² The Food and Agriculture Organization (FAO) has identified 37 developing countries facing the most immediate hunger needs, 20 of which are LDCs. But the crisis also has a significant impact in the larger developing economies such as India and China, as well as in some countries in Latin America. Even developed countries are not immune to the negative consequences of the crisis - rising food prices have added to inflationary or poverty tensions already being felt as a result of rising energy prices and crashes in financial and housing markets.

The global food crisis directly undermines one of the most fundamental human rights - the right to be free from hunger and malnutrition, recognized under the International Covenant on Economic, Social and Cultural Rights and the Universal Declaration on the Eradication of Hunger and Malnutrition.³ Unless addressed urgently, the crisis also threatens to hamper the achievement of the Millennium Development Goals, as reduced availability or affordability of food compromises health, education, maternal well-being and many other social indicators, as well as the capacity to earn a living. In particular, a food shortage is likely to impact most heavily on women and girls, who are often the last fed in poor households. The high food prices, shortages, reduced food consumption and worsened nutrition associated with the crisis thus has far-reaching and multi-faceted repercussions for all countries. It is incumbent upon the international community to respond decisively and comprehensively to this crisis so as to promote food security for all.

This paper aims to examine some important causes and challenges of the global food crisis from a developmental perspective. It also discusses some possible policy responses to this crisis.

Nature and Underlying Causes of the Crisis

The current global food crisis is due to the depletion of food stocks and increase in prices, especially of staples. Prices roughly doubled over the past three years, with an 85% increase between April 2007 and April 2008 alone. (see Graph below) This price rise has been broad-

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¹ This paper draws on the UNCTAD report "Addressing the Global Food Crisis: Key Trade, investment and commodity policies in ensuring sustainable food security and alleviating poverty", available on http://www.unctad.org/sections/edm_dir/docs/osg_2008_1_en.pdf

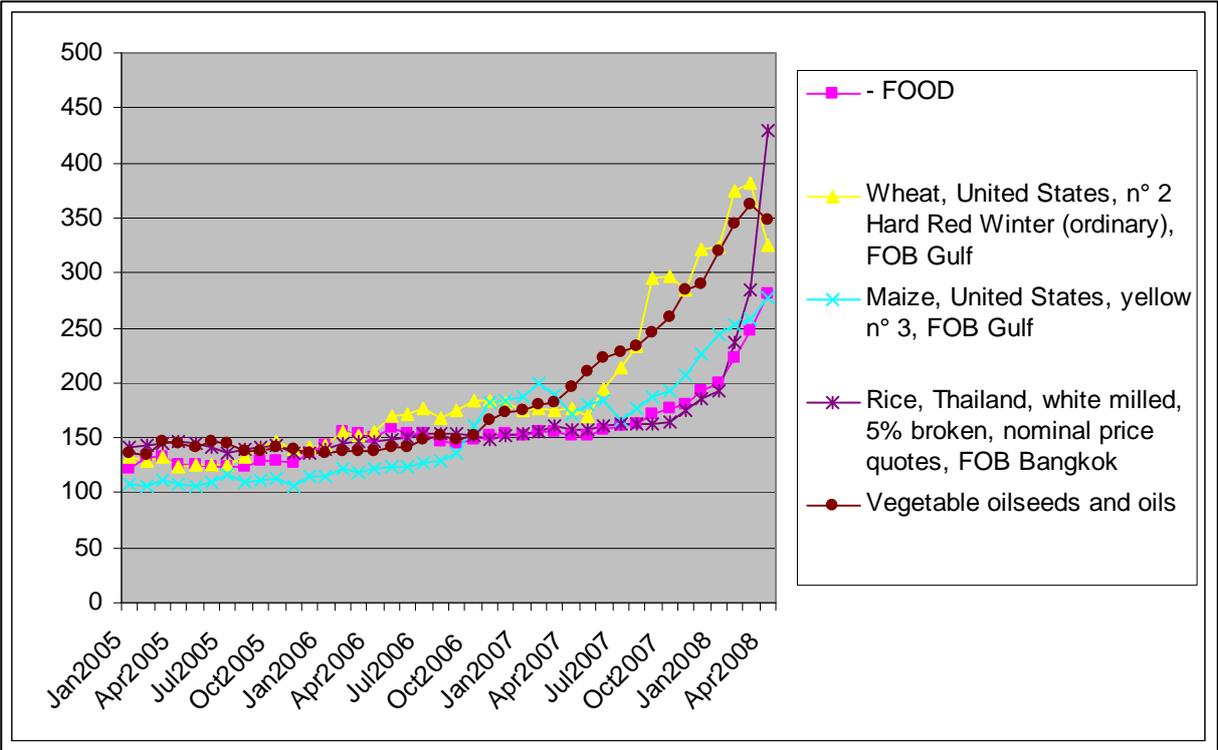
² FAO.

³ Adopted on 16 November 1974 by the World Food Conference, endorsed by United Nations General Assembly resolution 3348 (XXIX) of 17 December 1974.

based, led by wheat (whose price almost doubled), then maize (up 67% since July 2007), followed by rice (which has tripled since September 2007 and soared by 160% between January and April 2008 alone). Prices for vegetable oilseeds and oils also shot up, multiplying by about 2.5 since early 2006.

The broad-based prices increases have had severe repercussions for the import bill of developing countries. For example, the cereal import bill of low-income food deficit countries more than doubled in value in the past five years.⁴ Food price rises place a particularly heavy burden on the balance of trade of many developing countries as food imports account for a larger share of their GDP than in other countries.

Monthly prices of selected food products and product categories, index numbers 2000=100, January 2005–April 2008



Source: UNCTAD Commodity Price Bulletin

The rise in food prices was caused by a confluence of many factors - some of which were structural and some incidental. The long-term trend of increased demand for food - due largely to population growth and rapid economic development - was amplified by recent droughts, a slow supply response, a fall in the dollar, high energy prices, as well as concerns over increased demand for biofuels. And, the effects on commodity prices were significantly exacerbated by speculative investors looking to diversify their portfolios into growth-markets after the recent sub-prime mortgage crisis and by export restrictions imposed by concerned governments.

But one of the key factors in the current crisis has to be seen on the supply side, which has been too slow to respond with scaled up production. The agricultural supply capacity of many developing countries has been suffering from distorted incentives and insufficient

⁴ See UNCTAD, "The changing face of commodities in the twenty-first century" (TD/438).

support from both domestic and international policy makers. This development failure lies at the heart of the crisis, and we must urgently reverse this trend, if we are to avoid a repeat of the crisis.

a) Constraints on agricultural production in developing countries

The fundamental factor underlying the supply shortage is that, particularly in the last two decades, *agricultural productivity* has been relatively low in developing countries and even decreasing in many LDCs - a symptom of long term neglect of the agricultural sector. Agricultural productivity in many LDCs is lower today than it was fifty years ago. In LDCs and African countries, low growth rates of agricultural production have had important adverse implications for their economic growth and poverty reduction. Even in rapidly growing large developing countries such as India, however, many farmers continue to lead lives of mere subsistence.

Agricultural productivity, and thus output, is low for a number of reasons, including reduced arable land availability and low crop yield productivity. In many populous developing countries and LDCs, the available arable land is dwindling, often due to urbanization of agricultural land. Average farm size is diminishing and more and more farmers work on ecologically fragile land. In some countries, due to population growth and the loss of farmland, the average farm size has fallen. In Ethiopia and Malawi, for example, average farm size fell from 1.2 hectares to 0.8 in the 1990s.⁵ Lack of access to water and electricity in poor countries and has added to the tardy supply response. Insufficient access to irrigation has become a major problem in some countries, which further reduced the potential of agricultural production and land/crop yield. In most regions that have already reached high levels of production and trade, yields have been growing very slowly. In developing countries between the 1960s and 1980s, yields of the main cereal crops increased by 3-6 per cent a year. Now such annual growth has dropped to 1-2 per cent.⁶ Climate change is likely to accelerate this trend.

Low agricultural productivity has been reinforced by the lack of public and private investment in the rural and agricultural commodity sector, which is a prerequisite and important catalyst for agricultural development and food production in developing countries. In many developing countries, the agriculture sector receives limited support in terms of the Government budget and domestic investment, even though it often is among the largest contributors to both GDP and employment. Matters have been made worse by policies that weakened the role of key institutional support measures, including marketing boards or state-supported extension services, without viable alternatives being put in place.⁷

The adverse effects of this upon farmers' costs has been compounded by under-investment in the infrastructure (communications, irrigation, transportation) needed to distribute agricultural products, the removal of state subsidies for agricultural inputs (such as seeds, pesticides, herbicides and fertilizers) and the strengthening of intellectual property rights over plant varieties and new seed technologies.

⁵ The new face of hunger, *The Economist*, 17th 2008.

⁶ *Ibid.*

⁷ For details see UNCTAD's Trade and Development Report 1998.

Despite these trends, international aid devoted to agriculture developing countries has been decreasing. Between 1980 and 2002, multilateral institutions cut ODA spending on agriculture by 85%, from US\$ 3.4 billion to US\$ 0.5 billion. Bilateral donors reduced spending by 39%, from US\$ 2.8 billion to US\$ 1.7 billion.⁸ Furthermore, aid for science, technology and innovation which is critical for enhancing agriculture productivity, is only a small proportion of total aid. Aid for agricultural research remains woefully inadequate to support the productivity improvements and agricultural extension in most developing countries and LDCs. For example, only 3 per cent of science, technology and innovation-related aid is for agricultural research in LDCs, and only 2 per cent and 1 per cent, respectively, for agricultural education and training and agricultural extension.⁹

Foreign direct investment (*FDI*) in agricultural production per se has also been very limited to date - as illustrated by the fact that only US\$300 billion of *FDI* stock, or less than 3 per cent, in 2005 was held in agriculture and food industries.

One of the most critical obstacles to agriculture development in developing countries has been posed by the long-standing agricultural export subsidies and domestic support policies in developed countries. Recent analysis by the FAO and UNCTAD has shown that agricultural subsidies in developed countries have been associated with rapidly increasing food imports in developing countries, alongside a decline in agricultural production. Indeed, a number of developing countries that have traditionally been food exporters – many of them LDCs – have become net food importers over the past 20 years. Recent data for 2006 show that, on average, 20 per cent of the LDCs food consumption is imported, and in some countries the share is much higher (in Lesotho 67%, Gambia 82%, Mauritania 32%, Malawi 31%, for example).

All of these factors brought together a secular decline in agricultural productivity in many developing countries, which has now prevented the sector from responding to stronger demand and higher prices with increased production. Unless this structural problem is addressed, the world will remain vulnerable to the recurrence of crisis like this one.

b) Speculation in the food commodity market

The flow of speculative capital into the commodity sector, including foods, is also likely to have played an important role in the crisis. It appears increasingly likely that the global food price surge is linked to the recent volatility and turmoil in global finance, mortgage and housing markets that was sparked by the collapse last year in the United States' sub-prime market. Speculators looking for assets with rising prices may well have sensed the strains in the world food markets, and re-oriented their portfolios to buy food commodity assets (commodity indices, futures and options contracts). Indeed, the volume of globally traded grain futures and options increased by 32 per cent in the first quarter of 2008 compared with the same period in 2007. While there is no precise information on or analysis of the impact of speculative funds on food prices, the price rises of some key staple-food may well be attributable to a significant extent to speculation by different actors in the food commodity markets.

⁸ Official development assistance to agriculture, Department for International Development, November 2004.

⁹ UNCTAD Least developed Countries Report 2007.

Moreover, countries imposing food export controls (thus worsening global food supply) are indirectly harming the operational efficiency of the futures market.¹⁰ Some countries started imposing food export controls by food stockpiling and banning or taxing food exports. Such actions are intended to temporarily address the needs of local markets, but in some cases they have further distorted national, regional and global food markets.

c) Biofuels and food security

The impact of biofuels on food security and food price rises is also being widely discussed. Yet it appears that this impact is largely related to policy measures that have exacerbated market pressures. The biofuels market in most countries functions on the basis of mandatory blending targets. The United States, for example, has introduced in its 2007 Energy Bill ambitious utilization levels of biofuels for transport which go far beyond those included in previous legislation, namely 9 billion gallons in 2008 rising to 36 billion gallons in 2022. The use of maize for ethanol production is expected to almost double between 2005/06 and 2007/08. In 2009 it is forecast that almost 38 per cent of total United States domestic maize use, equivalent to 100 million tons, will be devoted to biofuels production.¹¹ The EU, India, Brazil and China have also set their own targets to increase biofuels. The EU for instance has declared that by 2010, 5.75 per cent of all gasoline sold to motorists in Europe must stem from biofuels production. The EU is responsible for around 90 per cent of global biodiesel production and the main feedstock used is rapeseed. EU production of biodiesel is estimated to have used 4.1 million tonnes in 2004 or the equivalent to around 20 per cent of the EU-25 total oilseed production.¹²

In addition to putting in place ambitious blending targets, both the United States and the EU apply tariffs and technical regulations to imported biofuels. Those instruments, combined with the long-standing subsidies for agricultural production, lead to diversion of land and food crop production for food consumption to biofuels use, and thus result in food shortages and in turn in food price hikes.

However, the extent to which the demand for cereals in the EU to produce biofuels has contributed to the recent food price increases is not clear. Only about 1.4 per cent of wheat is used for biofuels production in the EU, and about 0.6 per cent globally.¹³ Also, the price of rice has experienced one of the most dramatic increases (165 per cent during the year April 2007 to April 2008), even though it is not used for biofuels production and there is no evidence in rice growing countries that rice cropland has been shifted to produce biofuels feedstocks. Accordingly, determining the impact of biofuels on food security will require further research and assessment.

¹⁰ See IFPRI, *Ibid* at 6.

¹¹ DEFRA, *Ibid*, .at 15.

¹² The recent raise in palm oil production has been associated with the boom in biodiesel production, however at present only 1% of palm oil is used for biodiesel. Some indirect impact may have taken place, since more rapeseed is used for biodiesel, but overall, the use of vegetable oils for biodiesel remains small compared to other uses, especially for food production (see DEFRA, *Ibid* at 16).

¹³ The Impact of Biofuels on Commodity Prices, April 2008, DEFRA, Economic Group, at 15.

C. Policy response

The policy responses to the crisis will have to include both short-term and longer-term measures, reflecting the fact that the crisis has both short-term and structural causes and implications. Of course the immediate and urgent priority is to ensure that adequate food is delivered to the areas of need, and this task is being addressed by the humanitarian and emergency agencies, including the FAO and WFP.

In the medium-term, we must also better assess the precise role the biofuels-production and speculation in contributing to the crisis, and take measures to limit their adverse impact. This could be done by promoting "second-generation" biofuels (such as woody cellulose, grasses and algae) that can help limit the direct competition between food and fuel, and by allowing more trade in biofuels. This will reduce price pressures on the feedstocks currently used, decrease the costs of achieving biofuels blending targets, and create opportunities for developing countries to produce and export biofuels to countries that need them. The impact of speculation on commodity markets could also be addressed through a number of regulatory measures.

The task does not stop there, however. The recent food crisis must also be seen as a wake-up call for the international community to rectify the systemic imbalances in global agricultural production and trade, which over the years have contributed to today's problem of low productivity. Ultimately, it is a development failure that is at the heart of the crisis, and if this failure is not rectified, crises like this one will keep recurring. A sustainable solution to the crisis will require addressing the fundamental distortions and policy failures in the agricultural sector and providing strategic support to farmers, so as to build a foundation for sustainable food security and development.

At the international level, we must begin to remove the distortions in the international market for agricultural products. Current high prices provide a good opportunity to phase out agricultural support and subsidies in the developed world through the Doha Round. Addressing the crisis will also require reversing the decline in ODA to the agricultural sector, and financing the necessary infrastructure, especially transport and logistics networks, for transporting food. Particular efforts must also go towards strengthening agricultural R&D, especially through knowledge-sharing, support to modern farming technologies, and adapting proven technologies to suit local conditions.

But increases in international assistance or other international measures will not suffice without concomitant national measures. Developing countries must design a policy framework that creates the right incentives for investment in agriculture, as well as provide the necessary infrastructure and extension services. National trade policy should be calibrated to promote agriculture production, including by eliminating tariffs on agricultural inputs. They must also provide better training and knowledge to farmers, as part of a broader, nationally owned commitment to strengthening this sector.

The global food crisis has demonstrated the fragility of the global development progress we have achieved so far. It must therefore be an alarm signal for the international community to embark on a fundamental reform of global agricultural policies, and to strengthen the agricultural sector in developing countries. Nothing less will do to build a sustainable basis for growth and development, and prevent a recurrence of the current crisis.