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Wheat Price Volatility: Panic is Baseless and Hurts Poor People

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Apparent similarities between today's rising wheat prices and the food-price crisis of 2007-2008 are just that: apparent, not real. Suggestions to the contrary serve to drive up prices and hurt poor people, who spend much or most of their incomes on food. They need neither jittery markets nor ad hoc protectionism, which has exacerbated past food crises.

At first glance, the current situation can look like an unfolding rerun of the last crisis. Russia, hit by drought and wildfires, has banned exports of wheat well into 2011. Ukraine and Kazakhstan are weighing possible restrictions of their own. Unrest in Mozambique has been blamed on rising prices. All this evokes 2007-2008, when more than a dozen major food producers halted or restricted exports. This was meant to protect domestic markets as staple prices soared and global grain stocks fell to record lows, but it put even more pressure on commodity prices. Global market stability was sacrificed at the altar of domestic politics. This sparked riots in countries starved of food imports.

However, the situation today is different in a number of ways:

1. We are able to cope with lost production better than we did two years ago. The latest figures from the US Department of Agriculture's World Agricultural Outlook Board indicate that wheat production in 2010-2011 will amount to 656 million metric tons, 7% more than in 2007-2008, even after tallying all known losses. Moreover, global wheat stocks stand at around 175 million metric tons—nearly 50 million metric tons more than in 2007-2008. The United States alone holds reserves of 26 million metric tons—more than enough to cover the combined estimated loss of 18 million metric tons from Russia, Ukraine, Kazakhstan, and the European Union.

2. Bad weather—a perennial wildcard in agriculture and commodity markets—has not hit all producers. While Russia and others tally losses from drought or floods, the United States—the world's largest source—enjoys a good harvest, as do Argentina, Australia, India, and Uzbekistan.

3. The UN's Food and Agriculture Organisation (FAO) food price index rose 5% during August, prompting comparisons to previous spikes. This might seem dramatic, but in actual fact the peak of 176

seen in August was a mere 1% higher than the January 2010 level of 174. This is all the more striking because the index includes not only grains but also oil, fats, and sugar—the prices of which also have risen (and for separate reasons). In other words, for all the recent talk of runaway wheat prices, the impact has been minimal.

4. In order for world wheat prices to drive up the price of bread, they would have to stay high for a prolonged period. In 2007, prices rose continuously for months on end before hitting consumers. Today, prices are volatile. Two points bear emphasizing. The first is that volatility is not the same thing as inflation. The second is that volatility has stayed within the normal range since the end of the last food-price crisis. Indeed, recent spikes notwithstanding, the prevailing trend is flat or slightly downward. In consequence, there should be no knock-on effects.

5. Spot prices for wheat rose by nearly one-quarter in July and by more than 50 percent between the start of June and early August. But weekly price increases, compared with four weeks previously, were no larger in July 2010 than in May or November 2009. Indeed, when compared over a 12-week span, prices have climbed less in the past three months than they did at the end of 2009.

6. Likewise, futures prices for September contracts on the Chicago Board of Trade posted their biggest daily increases since 2008 twice during the first week of August. But these were aberrations, extreme values of return that remain freakish and highly unlikely when viewed against supply, demand, and returns in the futures market over the past six years. Moreover, these spikes involved nearest-delivery contracts, looking ahead one month. Contracts of longer maturity are a better guide to overall market conditions. These also have adjusted upward—but at a much calmer pace. This is contrary to what happened three years ago, when futures prices of distinct maturities climbed relentlessly and in lockstep.

7. The situation today also differs with respect to other key commodities. The World Agricultural Outlook Board and FAO expect maize production in 2010-2011 to exceed the total for 2007-2008 by 4% and 5%, respectively. The FAO expects production to increase by 3% for rice and 4% for coarse grains such as rye, barley, and sorghum. And the price of a barrel of oil today hovers around US$74—against US$131 in June 2008.

If policy decisions such as Russia's appear to have overlooked much of this, so too has public discourse. For example, initial news analysis tied the recent unrest in Mozambique to the price of wheat—wrongly so. Rather, the government raised the prices of basic food and non-food items to reflect the rising cost of imports from South Africa, Mozambique's main supplier. These have become more expensive as Mozambique's currency, the metical, has fallen against the South African rand by 21% since January 2010 and 47% since September 2009.

More thoughtful analysis has followed in recent days but not until after the earlier, more reflexive narrative had already caused another global price spike. That was the last thing consumers—especially poor ones—needed.

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