Managing food price instability: what have (and haven't) we learnt form experiences?

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Presented at the COMESA, CAADP, and ACTESA policy seminar

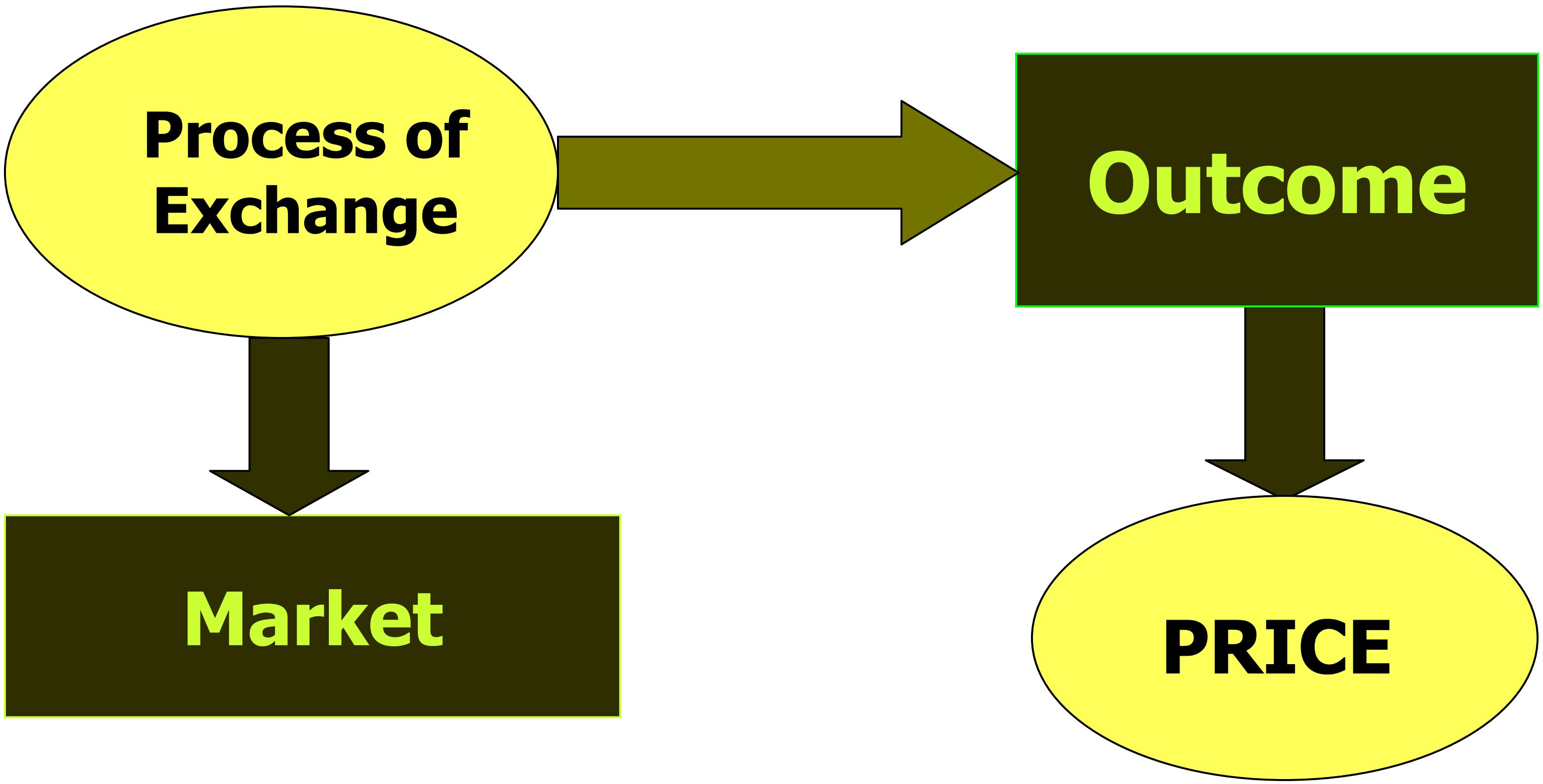
"Awakening Sleeping Giant: Making Grain Markets Work for the Small Farmers and Consumers in Eastern and Southern Africa"

On 10 May 2010 in Lusaka, Zambia

Outline

- Rationales for managing food price instability.
- Sources of food price instability and traditional policy response
- Critical determinants of policy success.
- The challenges and lessons learned .

Understanding market



Rationales for managing price instability

	Commonly given rationales	Economists' terms
1	Inadequate infrastructure	Public goods
2	Imperfect price information	Information Asymmetry
3	Missing credit & insurance markets	Institutional failure
4	Technology promotion (green revolution)	Absence of risk management institutes
5	Volatility of international price	Strategic response
6	Limited capacity to import	Self-sufficiency/ strategic
7	Political sensitivity to price instability	Strategic response

Sources of grain price variability

	Source of variability	Explanation
1	Weather-shocks → production variability	Supply shocks → large variation in grain prices
2	Poor infrastructure (including info) and high transaction costs	High transport cost limits trade between surplus and deficit region; and create wider gap in import and export parity.
3	Transmission of global price volatility	World prices are volatile and the volatility gets transmitted if a country in import dependent
4	Unimodal rainfall	Single harvest→ greater seasonal variation in grain prices
5	Reliance on one staple	Makes demand for dominant staple inelastic (small supply shock → big change in price)
6	Trade barriers	Creates wider gap between import and export parity, which are bounds of domestic prices
7	Unpredictable policy interventions	Discourages private traders from investing in and carrying out storage and trade.

Short- and Long term policy options

Effective management of food price instability requires working on the root causes.

- But addressing the root causes of price instability requires time.
- Thus, some short term interventions are thought to be justified, while countries work on the root causes.
- Traditional methods are short term interventions

Short- run approach has been to stabilize prices through public interventions

- Both developed and developing countries have practiced policies of managing price instability; but the vary across countries in terms of design and implementation
- Most African countries managed food price instability through marketing boards, which in some instance eliminated private sector
- Asian countries adopted dual pricing policies, where government control certain share of market, but majority of marketing activities were carried out by the private sector.

Short term interventions: African experiences

- Governments controlled all aspects of markets
  - Set production quota at pre-set prices
  - Prohibited private trade
  - Pan-territorial pricing (no variation of prices across space or time)
  - Private sector became non-existent /very small.

Key elements of Asian dual price policies.

- **Two critical elements: (a) institutions, (b) appropriate regulations**
  - Prices commissions / food security monitoring research
    - Clear research support
      - Monitor costs of production; determine floor and ceiling prices; provide market information (both domestic and international)
  - Linking price policies with social safety net program
      - Price support to farmer → protection to vulnerable
  - Private sector remained dominant

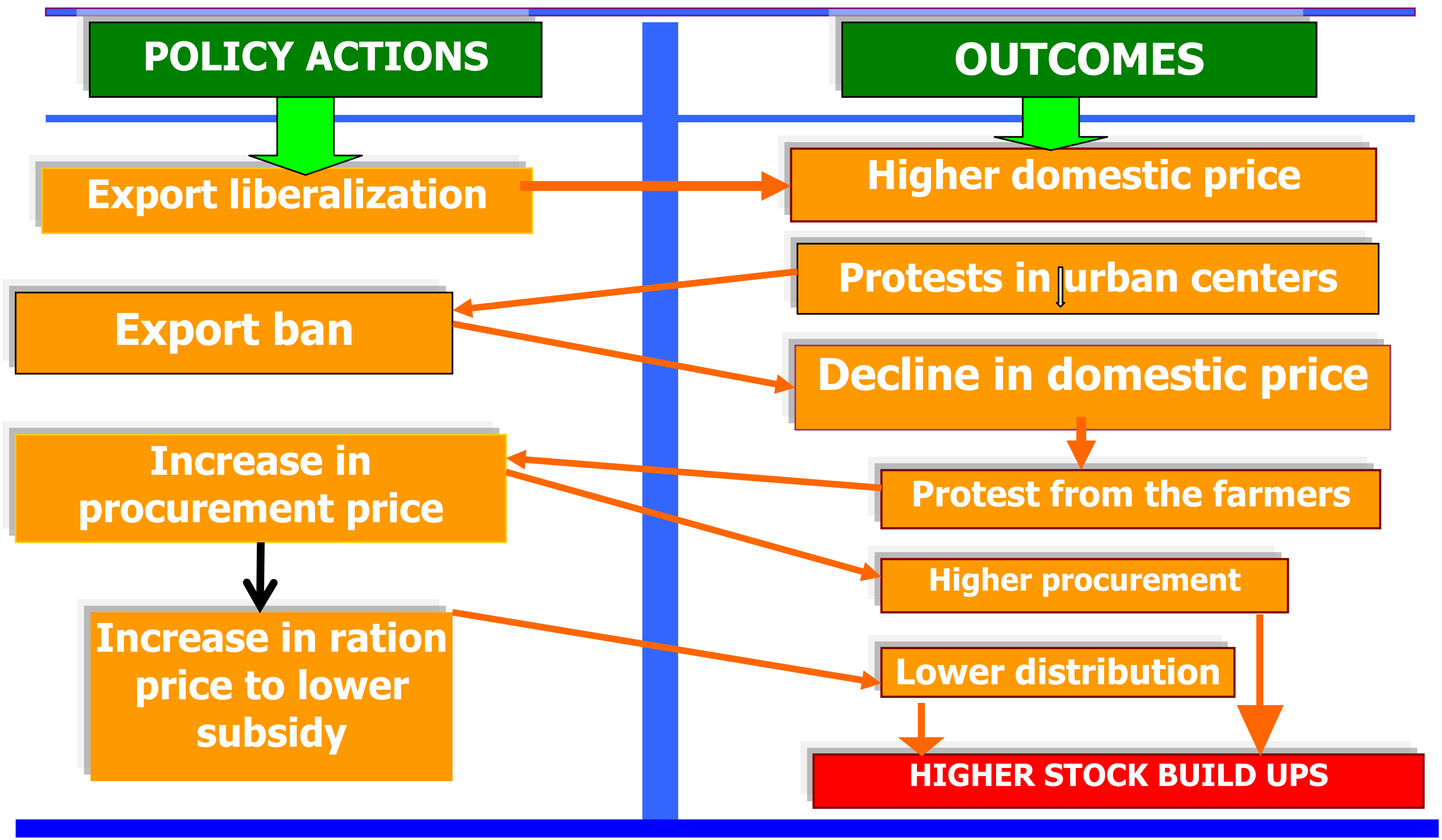
Distinguishing features of price policies in Africa and Asia

	Indicators	Africa	Asia during green revolt.
1	Smallholder dominant agriculture	√ & X	√
1	Institutional / research supports to policy formulation	X	√
2	Links with strategic reserves and social safety net programs	X	√
3	Clearly defined price band (floor and ceiling price)	X	√
4	Analytical basis of stock determination	√ & X	√
5	Panic response (intervention)	√	√

Challenges of managing price instability (1)

- Political pressure from farmers to set high floor (buying) price; political pressure from consumers to set low ceiling (selling) price
- Managing price instability by holding stocks can be very expensive.
  - Example of costs and food safety.....
- Delays in decision-making and funding mean that interventions occur late, sometimes further exacerbating the price instability
- It can displaces private sector from storage activities.

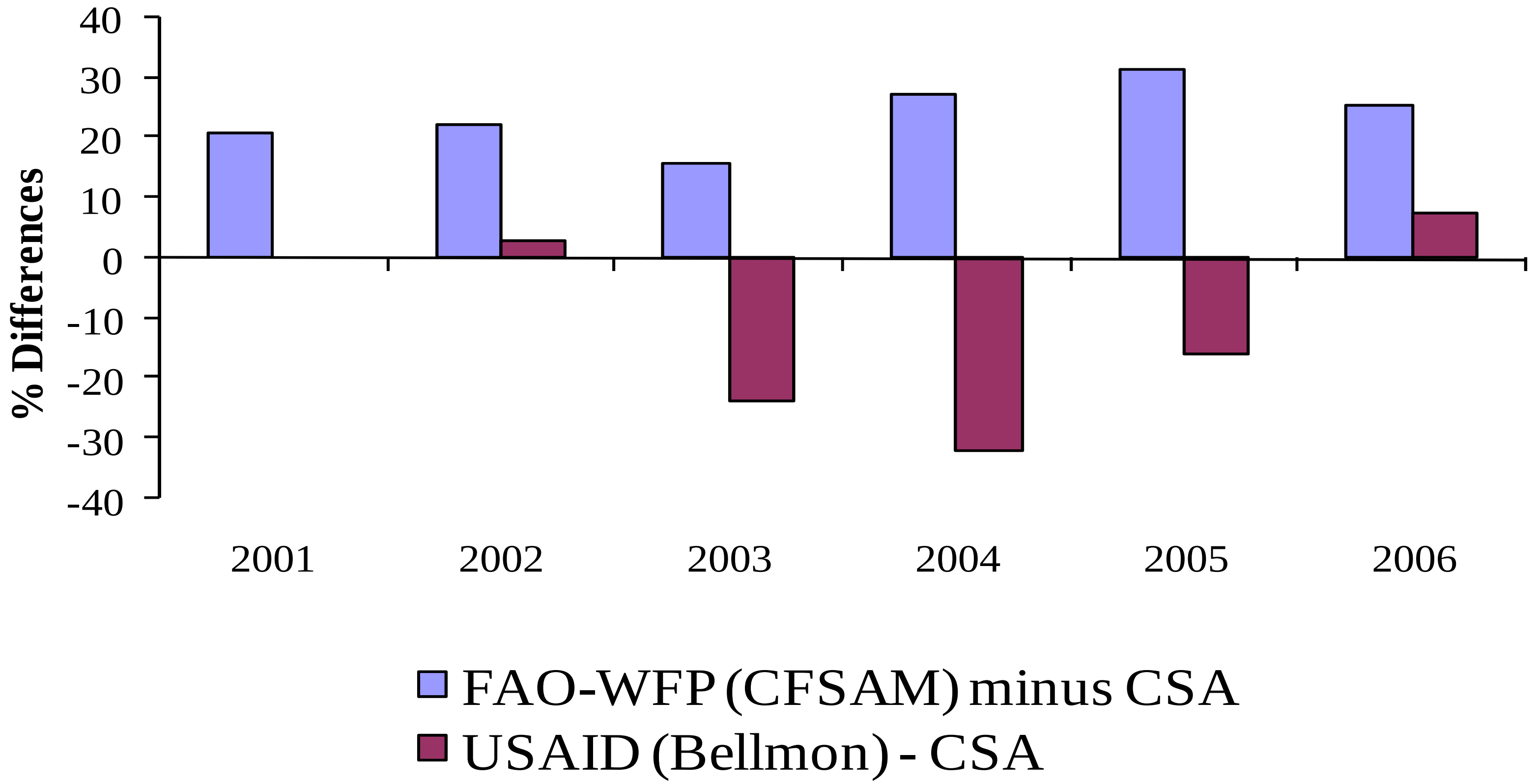
Challenges: once adopted, hard to get out



Long term solutions: how are we doing?

Source of Instability	Remedies to reduce variability	Policy (attention)
Weather-related shocks	Production forecasting, Agric research & extension, supplementary irrigation, develop drought -resistant crops	😐
Unimodal rainfall	Invest in post-harvest storage technology, allow off-season imports	😐
Poor transport infrastructure	Invest in roads, bridges, and ports	☺

Variation in crop forecasting



Remedies for staple food variability (cont)

Source of Instability	Remedies to reduce variability	Policy attention
High transaction costs	Grades and standards, market information systems, commercial credit, contract enforcement	😐
Trade barriers	Commitment to open borders for grain, streamline paperwork at borders	😐
Reliance on one staple	Promote secondary staple crops	😐
Unpredictable policy intervention	Reduce intervention in trade and storage, make interventions predictable	😐

Summary (1)

- The ultimate objective should be working on the sources of instability.
  - **We should work on turning all the sad faces into happy faces**.
- Given frequency of emergencies and political sensitivity of price instability, short run interventions might be necessary. However, they should be:
  - **Rule based and backed by empirical analyses**
  - **This will require setting up / strengthening analytical support units**

Summary (2)

- **Integrating emergency reserves with right kind of social safety nets programs.** This will help:
  - Minimize financial cost of short run policies; reduce disincentive effects;
  - More importantly, such linkage his has the potentials to create demand, protect livelihood, and contribute towards building an educated, healthy, and productive labor force.
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