FOOD POLICY IS NOW AT THE CENTER of global attention. Rapidly rising international agricultural commodity prices (Figure 1) have pushed up prices of basic food items in local markets, placing a mounting burden on consumers. In some countries, this has provoked social unrest.

Most countries have responded by trying to cushion the impact on the poor. The policies undertaken to cope with these price increases vary considerably across countries. In some cases, they have neither targeted the poor nor been cost-effective. Some countries have implemented measures that caused serious problems, either at home, or for other countries.

Trends, determinants, and stakes

FOOD GRAIN PRICES have more than doubled since January 2006. Over 60 percent of this increase has occurred since January 2008 alone (Figure 1). Individual grain staple prices have increased even more, with monthly average wheat prices doubling and soybean oil prices up by 165 percent since January 2006. Rice prices shot up from $376 per ton in January 2008, to...
over $1000 in April. Prices should start to decline towards the end of this year, given record global production forecasted for 2008 and 2009, but are expected to remain above 2004 levels through 2015. While the extent of global price transmission varies, there have been significant surges in domestic food price inflation over the past year in countries such as Sri Lanka (34 percent), Vietnam (26 percent), Chile (16 percent) and Egypt (13.5 percent). In many countries and regions, food price inflation is higher than aggregate inflation and contributing to underlying inflationary pressures.

A variety of factors has led to this upward price spiral. Underlying structural factors include sharply increased use of cereals and vegetable oils in production of biofuels, high prices for energy and fertilizer, the continuing depreciation of the US dollar, and declining global stocks of food grains due to changes to buffer stock policies in the US and the European Union. Among these, the most important was the large increase in bio-fuels production in the US and EU, in response to policies that subsidized production of biofuels, restricted their imports and mandated their use. Back-to-back droughts in Australia, and growing global demand for grains (excluding for biofuel production) have been modest contributors and on their own would not have led to large price increases. Commodity investors and hedge fund activity also seem to have played a minor role. Although empirical evidence is scarce, the prevailing consensus among market analysts is that fundamentals and policy decisions are the key drivers of food price rises, rather than speculative activity.

The effects of these underlying structural factors have been sharpened by counterproductive policies adopted by key exporters and importers. Export restrictions and bans—such as those imposed by India, China and Vietnam on rice, or by Argentina, Kazakhstan, and Russia on wheat—have restricted global supply and aggravated shortages. Export bans and restrictions, in particular, reduce confidence in international grain markets, while sending a signal to others to hoard or build up strategic reserves. The latter occurs not just at the state level, but at every stage of the supply chain as participants (including even small farmers and urban consumers) become convinced that it is in their interest to hold physical grain stocks. Driven by expectations that some consumers will buy at any price, these restrictions have contributed to sharp price spikes, both in global and national markets, in recent months.

The immediate poverty impacts of rising food prices depend on whether households below or just above the poverty line are net food buyers or sellers. In urban areas, poor or near-poor households are typically net buyers and adversely affected, particularly those on fixed incomes. In rural areas, most poor households are food producers, but in most countries the majority of poor rural households are net buyers, and thus hurt by rising prices. Over time, wages adjust to rising prices, but empirical evidence shows that they typically do not mitigate the full impact of the price increase. Preliminary estimates of the global impact of these price rises suggest that around 100 million people in developing countries could fall into poverty.

The stakes are high. The situation is also complicated by the fact that what governments do now to deal with the immediate problem will also determine how soon more lasting solutions are found. How will governments deal with what looks like an extended period of more volatile grain prices? Will countries develop a series of new policies, instruments and institutions in the near future to ease the plight of the poor immediately, while laying the groundwork for smoother-functioning agricultural systems that can take the burden off the public sector in a reasonable time period and for most, if not all, poor people? Or will large numbers of countries revert to 1970s strategies of trying to directly control physical grain production, marketing and stocks, with even less chance of success than then in an increasingly inter-linked global economy?

Policy responses

There are three broad categories of policy interventions. A first category of immediate interventions comprises those that attempt to lower domestic food prices. First best
options in this category include reducing tariffs and other taxes on key staples. In times of sharply increasing prices, reductions in tariffs and taxes can provide some relief to consumers, albeit at a fiscal cost. Some 33 of 80 countries sampled by the World Bank in March 2008 had reduced such taxes in the wake of rising food inflation (see Figure 2).

A different type of measure that also falls under this category seeks to increase quickly national control over physical foodgrain supplies. About one-fifth of developing countries sampled have begun adding to grain buffer stocks, creating, re-creating, or adding to “strategic reserves.” These are often used to provide subsidized food rations for the poor (e.g. Bangladesh). Recent price spikes in international markets, and the current difficulty in obtaining supplies, particularly in the rice market, suggests that more countries will try to increase domestic stockholdings despite the high costs of management. If so, this is likely to perpetuate the price spike as participants go into global markets with higher orders than normal despite the much higher prices.

A third type of policy response is the use of consumer subsidies. Subsidies narrowly targeted to the poor for rationed quantities of basic staples and financed through the government budget, are unlikely to create major disincentives for farmers or private traders. But generalized subsidies financed by capping producer prices are likely to have significant fiscal costs and create market disincentives for future food supplies.

The least desirable policy responses are export restrictions or bans on key staples. Several grain exporting countries have implemented bans or increased grain export taxes in reaction to rising food prices. This type of measure often has a limited impact on domestic price levels, a significant negative effect on the earnings of domestic producers and exporters, and leads to higher prices in countries that depend on grain imports.

A second broad category of policy options that can improve household food security relate to various forms of targeted safety nets. First best options here include cash or near-cash transfers (e.g. Brazil, Indonesia, Ethiopia) that are conditional upon meeting requirements such as low income, location or occupation, or engaging in a certain type of required behavior such as sending children to school. However, these programs are not always a feasible option in low-income countries with weak administrative capacity. Some countries, such as Mozambique and Cambodia, are using self-targeted food-for-work programs, which reduce the costs otherwise involved in administrative targeting. Others, such as Afghanistan and Angola, are using emergency food aid distribution, often in partnership with agencies such as the World Food Program, to ensure food security for vulnerable groups, but this can be costly in terms of physical transfer and potential leakages to the nonpoor. Still other countries make effective use of school feeding programs, but these do not typically address child malnutrition at its most critical point—when children are in their infancy.

The third broad category of policy responses seeks to make the best of higher food prices for stimulating domestic food production and the incomes of the poor as producers. Short-term policy options that seek to control markets, such as price ceilings, export restrictions, forcible procurement, or direct government involvement in marketing activities all risk limiting the scope for longer-term supply solutions. The substantial increase in fertilizer prices, combined with rising costs of fuel and irrigation have raised the costs of food grain production sharply over the past year. In such a context, well-designed subsidies aimed at poor and small-scale farmers who could not otherwise purchase agricultural inputs could be introduced for a limited period to boost yields.

But such subsidies often involve significant trade-offs with other pro-poor public spending. Malawi’s input subsidy program costs approximately three percent of overall GDP—the same as the entire primary education budget.

Investments in basic rural transport and information systems have been shown to reduce prices and increase opportunities, particularly where farmers are in remote regions, such as Nepal, for example. Improvements in customs facilitation, logistics performance, and efficient grain storage can enhance producer responses as well as benefiting consumers.

In several East Asian countries, rice yields could increase significantly by shifting fertilizer subsidies from urea to potassium and post-harvest losses could be lowered by 25 percent through better use of post-harvest technology and infrastructure. Concurrently, interventions are needed to reduce farmer exposure to commodity price and weather-related risks with a variety of low-cost, market-based risk...
The spread of new information technologies is greatly improving market performance by reducing search and transport costs. For example, in India, the Ministry of Agriculture operates AgMark Net, which collects price information from wholesale markets nationwide and disseminates it through the Internet. In West Africa, a public private partnership set up TradeNet, a trading platform that allows sellers and buyers to get into contact over the Internet and by cell phones. Market information systems also disseminate price information in Kenya, Mozambique, and Senegal, using a mix of Internet, short message service (SMS), voicemail, radio, and market chalkboards. Local FM radio broadcasts market information in Mali and Uganda.

**Education:** While land and water are critical assets in rural areas, education is often the most valuable asset for rural people to pursue opportunities in the new agriculture, obtain skilled jobs, start businesses in the rural nonfarm economy, and migrate successfully. Yet education levels in rural areas tend to be dismally low worldwide: an average of four years for rural adult males and less than three years for rural adult females in Sub-Saharan Africa, South Asia, and the Middle East and North Africa.

Improving basic rural education has been slower than in urban areas. Where demand for education is lagging among rural households, it can be enhanced through cash transfers (as in Bangladesh, Brazil, and Mexico) conditional on school attendance. However, increasingly it is the quality of rural education that requires the most improvement, with education conceived broadly to include vocational training that can provide technical and business skills that are useful in the new agriculture and the rural nonfarm economy.

### New commitment to agriculture

**Most projections suggest** that food prices will be higher relative to the past two decades. Amid climate change and growing pressure on land and water, the pressure is on the agricultural sector to provide food, feed and fuel at affordable prices. Delivering on this demand to help solve the food, feed and fuel crises depends on mobilizing political support, at national and international levels, to invest in agriculture—especially in Africa—as never before. Over the longer-term, seizing this opportunity means finding the skills and resources to invest in rural infrastructure, water and irrigation services, education and agricultural R&D. A sustained effort in these directions promises farmers a chance to be full participants, responding to price signals in busy agricultural markets, and prospering as a result.

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### Rising Food Prices continued from page 8

management instruments e.g. warehouse receipts, futures and options and weather-based insurance products (see other articles in this volume).

All the policy responses reviewed above can have significant fiscal implications. The macroeconomic consequences of higher spending depend largely on how they will be financed. Additional budgetary costs financed via higher domestic borrowing can lead to higher overall inflation, while transferring costs to non-poor taxpayers may or may not be politically feasible. Diverting resources from other social sector spending or core public investments may have medium- and long-run opportunity costs, but may also provide an opportunity to reduce lower priority expenditures and reallocate these resources.

Sound policy choices will be the most efficient economically, yet also take political economy considerations into account. In some cases, first or second-best policies may not be feasible or may involve difficult political choices. In general, government policy choices are likely to be better accepted if accompanied by a transparent and effective communications strategy on the causes of high food prices and accompanying policy measures.

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**Notes**

1. Global grain demand (excluding bio-fuels) increased by 1.3% per year between 2000 and 2007 and in East Asia (including China) it increased by only 0.3% annually during this period. The switch from basic staples as incomes have risen, and the greater efficiency of livestock feeding, has contributed to this slow growth in demand. Droughts in Australia have reduced exports by around ten million tons of grains in 2006 and 2007, equivalent to about 4% of global grain exports.

2. Food stamps are the most frequently used form of near-cash transfer.

3. Self-targeted programs are designed to minimize the incentives the non-poor may have in participating, typically achieved through a mix of rationing benefits (e.g. limiting food quantities), physical requirements (e.g. manual work for food), and queuing.