WORLD FOOD PRICES AND POLITICS

by

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December, 1975

No. 75-26

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During 1972 the food surpluses of North America, Western Europe and Australia suddenly disappeared and food, long regarded the bargain of the Century, was no longer cheap. This sudden reversal in the world's food situation raises a number of questions dealing both with causes and future prospects. Does it mean that the world is approaching a limit in ability to feed its people? Have we entered a new era of chronic food shortages and high prices? Will food continue to rise in price commanding an ever increasing share of disposable incomes, or can we expect food prices to return to former low levels? What are the implications of these uncertainties to agriculture? What will happen to farm incomes? What can we expect in the export market? These are but a few questions that may be in your minds.

Even if the present upheavals in the world's economies are but a temporary aberration, this is a most challenging time to try to put into perspective the complex forces contributing to present conditions. At best, looking backward is a hazardous game because things found in association are not always related and in economics significant relationships often are hidden by time lags. The analyst finds it much easier to explain yesterday's stock market prices than to predict those for tomorrow and so it is with food prices. In prediction, the economist is at his best when social and economic values remain constant--when only one variable is at play--hence his favorite phrase "all other things remaining constant" a postulation that today borders on the absurd. Perhaps this explains why I overheard one of my economist friends say that there is no subject so complex that if studied with diligence and patience cannot be made more complex. Much of the complexity of world food prices results from a blending of politics and economics. A consideration of one without the other is of little meaning.

Food prices throughout the world continue to be high for the third year in a row. Among the major industrial nations outside the planned economies, increases in food prices during the past year have accounted for 30 to 50 per cent of the increase in living costs depending on where you live. As you know, food in both Canada and the United States takes less of the consumer's income than anywhere else in the free world . . . a tribute to both our agricultural and distributive industries. Even so, Canadian food prices between March of 1973 and 1974 accounted for 45 per cent of the increase in consumer prices. There were only four of the 18 OECD nations where food cost increases contributed so much to living costs. In spite of this, relative to other nations, food in Canada continues to be a bargain but the margin of advantage has been diminishing.

Ordinarily, the quickest and most certain cure for high prices is high price, but efforts to expand food production in response to price during 1974 were frustrated by adverse weather, dramatic increases in the

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Klinck Lecture sponsored by the Agricultural Institute of Canada and delivered at selected locations in Canada, March 19-April 3, 1975.

costs of energy and fertilizer and shortages of equipment. As a consequence, world grain production, which is the backbone of world food supplies and trade, fell far short of expectations.

An increase in world grain production of 25 million tons is needed each year to maintain per capita consumption. For a number of years production has increased at the rate of 36 million tons a year but two of the last three years have been disastrous. In 1972 and 1974 world grain production dropped 35 and 42 million tons, respectively, from previous year levels. It is well to distinguish between the two years. The decline in 1974, although greater, had less impact because it followed the record production year of 1973. Also a larger share of the 1974 shortfall was suffered by the major exporting nations. In consequence, grain stocks in the major exporting nations--Canada, United States and Australia--have been nearly depleted while food reserves in Asia are critical.

At the other extreme there were record levels of world meat production reflecting the biological lag inherent in production decisions made several years ago when feed grains were cheap and meat was much in demand. In response to this demand, breeding herds expanded only to run head-on into the double trouble of high feed costs and a general softening of demand. In some instances, trade restrictions placed on meat imports to protect overextended producers have helped stabilize domestic prices but they have severely depressed prices in export nations. It is reported that as much as 300,000 tons of unsold beef is being carried in the E.E.C. at huge public cost. In Australia during 1974 the price of dressed ox beef at the slaughter-works door dropped from 42 to 12 cents a pound.

Displacing food as the major component of inflation, abrupt increases in energy costs have stagnated business as it seeks readjustment to radically altered costs and markets. During 1974 no real economic growth took place in many nations. Gross national product in the United States dropped an alarming 9.1 per cent during the final quarter of 1974 and unemployment rising to over 8 per cent became a major political issue. Canada, in contrast, ranked at the top of the industrialized nations in economic growth enjoying an 18 per cent increase in gross national product, but much of this was the product of inflation.

To round out the current picture several other general comments are appropriate. During 1973 and 1974 high food prices brought a new prosperity to agriculture. For the first time in history, per capita farm income in the United States exceeded that of the non-farm sector . . . a condition that may be short lived depending much on policies for the future. Another factor is the changing nature of international food aid which has shifted from being a surplus disposal program to a charity, from being cheap to costly, from being passively accepted to aggressively demanded. Since 1965, Canada and the United States have provided 87.5 per cent of the developed world's direct food aid contributions. While the size of the United States food aid is impressive, Canada's contribution in proportion to gross national product over the past 9 years has exceeded that of the U.S. Finally, there has been a dramatic rise in world agricultural trade among the developed nations with the future uncertainty of that trade imparting much anxiety to the major agricultural exporting nations--The United States, Canada, and Australia.

The combination of circumstances that led so suddenly to the present situation almost defies description and certainly no logical ordering can be given to such factors as the weather, agricultural support policies, international aid, affluence, trade expansion, speculation in gold and commodities, inflation, economic controls and recently the energy crisis. Among them the greatest uncertainty is trade, the greatest certainty inflation. Being an agriculturalist, it is logical to start with the weather.

At least, it appears that the adverse worldwide weather of 1972 triggered a number of political actions. Over the years world food production has been remarkably stable, a product of diversification, but in 1972 it was hot and dry in the Eastern world and cold and wet in the Western world. Crop failures were experienced in many regions--a most unusual circumstance. World food production fell 1.6 per cent--a serious decline on a worldwide basis. Asia was particularly hard hit for in the previous ten years total food production under the Green Revolution had grown a remarkable 35 per cent and people there were beginning to eat with a regularity never before experienced. North America, Australia and the U.S.S.R. were all hard hit with the latter normally a net exporter, suddenly becoming the world's largest importer.

In summary, the weather of 1972 reduced world cereal and feed-grain reserves, stimulated world trade, placed a dampening effect on the Green Revolution, renewed public concern over starvation and malnutrition and created much speculation about possible long-range unfavorable climatological changes. Even so food production variations attributable to adverse weather during two of the past three years explains but a part of recent food price behavior. The adverse weather of 1972 seems to have been the force that suddenly released other accumulated pressures. Generally favorable weather and rising prices made 1973 on a worldwide basis an exceptionally good year for the farmer. Had the weatherman agreed with farmers' intentions in 1974, both farm and consumer food prices would have turned downward. Forestalling the adjustment until 1975 or 1976 or 1977--whenever the weather turns right--can only mean a more abrupt downward adjustment when it does come.

The food plant of a nation is much like a home garden. To insure having enough, there must be too much and the less confidence there is in the ability to trade with neighbors when food is needed the more the desire and need for self-sufficiency. Again, it is annual variations in the weather and the diversity of a nation's agriculture that determines how close to the margin a nation can afford to hold its production. In one year, the weather, along with the trade it stimulated, made obsolete the agricultural price support policies practiced by the developed nations for several generations.

In looking about the world, it is possible to associate and justify the degree of governmental involvement in agriculture with annual variability in production. In addition to serving national interests, subsidization of agriculture finds motivation in the support of a traditionally identified underprivileged farmer who enjoys the public image of being underpaid, overworked, loyal, essential and yet largely incapable of transferring with ease to alternative occupations. Whatever the cause, the agriculturally developed nations have followed remarkably similar political patterns in supporting the prices of agricultural products.

Price supports universally have led to surpluses necessitating restrictions on production. Thus, the agriculturally rich nations, in a hungry world, made it appear that there was too much food! Surpluses hung over the market. Production became oriented to a political rather than to a market determined price. In five years prior to 1972 there was a downward trend in the purchasing power of both food and fertilizer. Increasing amounts of cheap grain were fed to livestock and fertilizer plants were abandoned. Surpluses were dumped on developing nations in direct conflict with programs designed to build their food self-sufficiency through agricultural technology. Thus, international food aid served double duty in helping to create the shortages we know today. It not only served to liquidate surplus stocks but also undermined the developing nations' incentive to produce for their own needs.

The most significant international food aid of recent years is not the shipments of surplus foods to the developing nations but rather the mammoth sales of food at bargain prices to the centrally planned nations. It was the so-called Great Russian Grain Robbery of 1972, the largest single food deal in the world's history, that by eradicating government held inventories made political price meaningless and market price meaningful. The unanticipated entry of the Soviet Union into world food markets was dramatic because it was an abrupt reversal of previous Soviet policies and brought a significant new force to bear on international markets . . . a force that today provides both market opportunity and a conspicuous, destabilizing influence over world food prices.

The responsibility for the market disruption of large purchases by the state trading nations lies not so much with the buyer as it does with those nations whose political policies served to build up stocks of unwanted surpluses in the first place. Since the U.S.S.R. administered its first lesson in capitalism to the United States, we have seen massive purchases of beef and mutton from Australia and New Zealand, of butter and broilers from France, of beef from the Argentine. With the exception of grain in 1973, the purchases have been made at distressed prices. An example is the Soviet Union purchase of 400 million pounds of butter from France at 18 cents a pound or the purchase several weeks ago of 40,000 tons of beef from Australia at prices but a fraction of what it costs to produce beef in the U.S.S.R. In this case it was not the Australians who created the fire-sale bargain prices but rather other nations with which Australia had been trading. Japan, the EEC, Canada and the United States who welcomed Australian beef when prices were rising, eliminated or curtailed imports when beef prices fell because expensive feed forced too many animals to market. After repeated efforts to reopen international markets there was no place to turn except to the "undertaker". Let me put it another way. All the traditional customers of Australia had the opportunity to supply their consumers with some cheap meat. Instead, they opted to keep their own prices high and subsidize the Russian consumer. Perhaps it is not too far fetched to call the massive food sales to the centrally planned economies a form of food philanthropy.

While the net grain imports of 30 million tons by the U.S.S.R. put a shock wave in prices throughout the world, it is interesting to note that retail prices of both bread and meat in Russia have been unchanged since 1962. Russian prices of bread and meat which were higher than world levels ten years ago are now lower than world levels thanks to international bargain shopping. While the Soviet Government continues the struggle to improve its agricultural production, consumer prices have been increasingly subsidized both by those who sell to Russia as well as by the Soviet Food Ministry. In 1974, the Soviet consumer food subsidy was 12.6 billion roubles compared with 6.5 billion six years ago. The willingness of other nations to feed the Russians at lower prices than themselves serves to extend the effectiveness of the Soviet food subsidy.

World trade expansion is not confined to the centrally planned economies, but has been well disbursed among all nations and can be attributed more to a change in demand than supply factors. Aside from the influence of state traders, much of the upsurge in trade can be attributed to an affluence that suddenly seemed to sweep the world. The huge increase in trade during 1973 was almost entirely the product of increased tonnage while the increase during 1974 was essentially all in price. It now appears that world market prices of many agricultural commodities reached their peak in late 1973 and during 1974 and that both dollar value and tonnage of trade during 1975 will decline but will remain for the year well above the pre-1972 levels.

Suddenly the United States, Canada and Australia find themselves the major agricultural exporting nations of the world and their domestic food economies exposed to new external forces. Several major factors are distinct from the past. First, food production is highly variable in the major consuming regions of the world outside of North America and Western Europe. While this has always been true, the distinction is that massive state-sponsored trade deals now impose the effect of a highly variable supply on world markets. And it is well to remember that the amount of variable supply that is translated into demand is very much a political decision. When international trade was in the hands of private dealers they could neither anticipate future needs nor finance them. In addition, their sources of information were unreliable and fragmentary. In contrast, state traders not only have advance information on domestic production and a working knowledge of world stockpiles but also they possess an entirely different kind of purchasing power. If they don't have the cash they can negotiate credit and if it is not sound credit they can, and do, employ many forms of political duress.

The decisions made in the Kremlin can be expected to cast a continuing uncertainty on world food markets. Only time will reveal reasons. A third of the work force in the Soviet Union, compared with 5 per cent in North America is engaged in farming. It is possible that the Soviet Union having shunned world markets in the past has decided that this is too high a price to pay for agricultural independence. Have the Soviets, by adroitly moving in and out of markets, discovered a unique form of economic warfare, or could it be just good economics motivated by opportunity? I rather suspect that the latter accounts for much of the trade but no one can be certain. How much stockpiling is taking place and for what purpose? While we speculate there are very serious trade differences to be resolved between the centrally planned and free market economies. Distinctions in price making and in the use of statistical information call for some reasonable resolution if a continuing trade is to be expected.

Even so, the factors discussed so far offer only partial explanation for the sudden shift from an embarrassment of abundance to an embarrassment of scarcity. The worldwide affluence talked about several years ago, and all but forgotten today, was a long time in the making. Following the devastation of World War II, many cities had to be rebuilt. New plants, new homes and filling the empty pipelines with consumer goods provided jobs for workers and new opportunities for business. Full employment, increased productivity and a free flow of capital soon built an unprecedented affluence that served to escalate the demand for food in poor and rich countries alike. Food prices were kept at reasonable levels only because agriculture greatly increased output. Between 1954 and 1973 total food production in the world increased at the annual rate of 2.7 per cent in the developed countries and 3.0 per cent in the developing nations. On a per capita basis the gains were greater in the developed than in the developing nations but in all areas food per person was becoming more plentiful with each passing year. In response, affluent populaces increasingly turned attention to social problems.

The record of social legislation during the decade of the 1960's is outstanding. Almost any socially desirable proposition became law. Concern was centered on benefits with little attention to costs. Consumerism, environmentalism, health and safety, minority and education rights, increased employment and retirement benefits. Probably more socially constructive legislation was passed during the decade of the sixties than during the entire first half of the 20th century. At least it was ordered, if not paid for. In possibly an effort to accomplish too much too soon, they were social benefits bought largely on credit by an affluent society. In many cases the social reforms were merely mandated, leaving the financing to others in the future who could worry about increasing taxes or deficits.

The social reforms of the 1960's account for much of the growth in the gross national products of many of the developed nations. Used to buy more government services, deficit financing created an inflation that in itself generated windfall tax dollars which with debt leverage were used to further expand government programs. Thus, inflation became increasingly critical. Too much currency was put in chase of too few goods. First treated as a domestic issue, inflation gradually has been recognized as an international phenomenon. The difference among nations is but a matter of degree . . . a difference that temporarily alters trade advantage until currency devaluation is required to restore reasonable trade equilibrium. Variable inflation rates among nations constantly alter trade flows. This contributes a disturbing price variation to a general pattern of rising prices.

The political response to inflation has been routine throughout the world. In early stages it is ignored. On recognition it is interpreted as economic growth. As it begins to bear hardships a political search for scapegoats ensues. Commissions of enquiry are established with investigations commonly centering on food because people are sensitive to food prices. First the finger points to the retailer then the distributor, manufacturer and finally the farmer. Failing to find a culprit, various forms of economic controls are tried limiting prices, wages, margins, profits. The controls usually so stimulate the consumption of scarce goods and discourage their production that they are short lived. When controls are cast aside, governments finally resort to a reduction in deficit spending, cutting services, increasing taxes, tightening credit. This gets results but both the unemployment and reduced production that accompanies the cure are less acceptable than inflation. The price increases now ignored are greater but accepted for a time as essential to restore economic growth and employment so the cycle can be started all over again.

The repeated performance of this cycle in the many independent representative governments of the world indicates that society by choice will continue to force inflation. Many of our frustrations with food prices and politics today are traceable to the distortions in price relationships created by inflation. There is much difficulty in relating present prices with past prices, in identifying what is a bargain and what is not, in knowing what to keep and what to sell, in relating costs to prices. Farmers tend to make production decisions on the basis of present prices and costs experienced in the past, a practice that can be disastrous in times of rapid inflation. But perhaps most serious of all, the distortions of price relationships created by inflation cause us to search for scapegoats and support self-defeating political actions.

For example, increased taxation is a commonly proposed means to drain money out of the market and thereby reduce inflation. The idea makes economic sense but not political sense because governments are more indiscriminate spenders than are taxpayers themselves, particularly when inflation is offsetting the gains of social legislation. Another example is the inherent distrust of business, and big business in particular, that develops with inflation. This distrust in turn leads to restrictions on business and in extreme cases the nationalization of businesses which adds to costs and hence more inflation. In the political world, inflation with its accompanying distortion of price-cost relationships tends to force income redistributions in attempts to protect the living standards of the poor majority at the expense of the rich minority, an action which serves to destroy the capital investment essential to both employment and production. These few examples demonstrate the difficulty involved in learning to live with inflation . . . in such a way that the economic growth and full employment benefits of inflation are maintained at reasonable levels. We will learn to live with inflation because there is overwhelming evidence that inflation is a political necessity in any democratic society.

In fact all of us have a very selfish way of looking at inflation. You see the increased dollars in my paycheck last year I earned. It's the increased dollars that you got that makes for inflation! Aside from the pleasure of seeing one's income increase there are many social benefits of inflation which are not to be ignored. By contributing to the maintenance of full employment, inflation contributes to real productivity--hence the economists' support for policies contributing to a mild inflation. In addition inflation enhances the value of private investment and eases the liquidation of private debt. A home mortgage placed 10 or 15 years ago is scarcely a burden today. The deficit spending that builds inflation finances many forms of socially popular welfare programs many of which are designed to ease the burden of those at the bottom of the income scale hurt most by inflation. And not to be ignored is the fact that inflation provides many windfall tax dollars through such automatic escalators as graduated taxes. The cost of inflation in terms of the rising consumer prices that devalue savings makes inflation a political bargain--in fact a political necessity for those seeking to stay in office. In a very real sense inflation is nothing more than a form of income redistribution producing revenues which can be and are to a large extent employed to offset the losses incurred by the democratic majority at the bottom of the scale.

Elected public officials who remain in office seem to understand the love-hate relationship we have with inflation. In 1948, Cornell Professor F. A. Pearson predicted the election of Harry Truman over Thomas Dewey. This made news because all the major polls and media said it would be Dewey. Even the day after election the Chicago Tribune had Dewey the winner. Pearson didn't take a poll. He merely looked at what prices were doing. In the United States national elections have been held on 23 occasions when prices were rising and the party in power has been returned to office 20 times. Elections have been held 15 times when prices were falling and on 13 of those occasions the party in power was defeated. This may explain why political fights against inflation are short lived and seldom occur near election time.

Inflation to the producer means that both financing requirements and production risks will become greater. Much premium will be placed on one's ability to manage financial affairs so as to keep in reserve adequate resources to ride out the severe but short-lived price declines that will show up from time to time. A reasonable diversification in enterprises will become even more important than in the past but one must exercise care that diversification does not encroach on efficiency. The cultivation and continued education of a friendly banker is all important. Expansion debt in times of inflation usually pays off but the leverage must not be allowed to impair the ability to ride out 3 or 4 years of adverse cost-price relationships such as confront the livestock, diary, and poultry industries today. To most farmers forward integration into marketing will yield less on investment than that applied to horizontal growth provided adequate management is available. In fact most of us are most successful when we stay within our own special sphere of competence.

For the consumer, the task of riding out inflation is even more difficult. While inflation simplifies the liquidation of debt, consumer debt usually is not revenue producing, hence, such debt must be held within the bounds of anticipated income. Consumers who are willing to radically alter their consuming practices in response to market price opportunities will fare far better than those who are inflexible. This is tough for most consmmers because food habits tend to be fixed. But more important than food the consumer faces the seemingly hopeless problem of protecting his savings. Skill in doing this lies very much in one's ability to recognize the various processes by which society, through the instrument of the politician, seeks to redistribute wealth from those who have saved to those who have not saved. The most traditional forms of savings by their conspicuousness always will be the most vulnerable to erosion.

Finally, what is the meaning of this to those of us concerned with agriculture? North America now stands as the only major region of the world producing significantly more food than it can consume. For want of a market, the full capabilities never have been called upon, hence the physical limit of our capacity to produce is unknown. It is known that there is much unused and underused land in the world, but efficient production requires more than land. The agricultural advantage of North America lies much more in its agricultural technology.

Some claim this advantage will be lost because technology is easily transferable. They claim that advantage exists only so long as new technology is forthcoming and that today no new major developments are in sight. In this respect, it is well to remember that significant technologies are recognizable only after they are realized. The momentum of technology is with us but most important it is a technology that must be constantly reoriented in the light of current developments . . . a need illustrated and amplified by the worldwide energy crisis. In recent years cheap energy has been the source of much of North America's agricultural advantage. The emergence of the OPEC cartel has for the time being created disturbances which alter competitive advantage. In the coming year significant cost increases are anticipated for agriculture with energy costs in the form of fertilizer, equipment and fuel being most responsible. With farm prices already on the decline, an agreeable weatherman has the capacity to put a severe cost-price squeeze on commercial agriculture. The reduced consumption that accompanies high consumer prices makes it impossible for the farmer to pass all of his cost increases on to the consumer. In consequence of mounting surpluses, agriculture turns to government for help. It would seem that memories are short lived for we have gone near full cycle in our lifetime.

Because of the events during the past three years agriculture has been able to shed much of its past dependence on the politician. Is it possible to maintain this independence? It seems to me that this independence puts agriculture at the crossroads with the choice of going one of several directions. We can choose the well-traveled route of a price subsidized agriculture . . . one that maintains domestic prices, cushions agricultural adjustment, encourages the production of surpluses which eventually are discounted to other nations. Following this route domestic consumers are forced to subsidize not only domestic producers but also foreign consumers. It is a route that insures domestic supplies, stabilizes consumer prices but sacrifices some of the economic advantages which North American agriculture enjoys over the rest of the world.

Or we can choose a route leading much in the opposite direction--one that regards the world rather than the domestic economy as the primary market. In this direction, domestic prices are residual to world markets, agricultural adjustment is rapid and cruel. The benefits of agricultural advantage accrue to both producers and consumers in the form of more favorable trade balances. Both domestic supplies and prices in response to world markets are unstable and while agricultural expansion is encouraged, cost-price risks are greatly enhanced. One can argue the merits and impacts of a free market but in the face of political realities it is quite academic.

Perhaps it is not a question of going right or left but rather one of choosing some middle route. It seems to me that the great opportunity of serving world markets on a commercial basis must be realized in the formulation of future agricultural policy. If a viable international trade is to be developed--if the full advantage of North American agriculture is to be realized--such a policy must optimize production and efficiency with prices on international markets reflecting the true comparative advantage that exists. In a hungry world it is both economically and morally wrong to follow any policy that sacrifices the capacity of North America to produce food.