

Grain Reserves: Some Issues and Reflections

CAN THE CAP MANAGE WITHOUT MARKET REGULATION AFTER 2013?
CSA & PFSA
April 1 2009, Brussels

By Sophia Murphy
Institute for Agriculture and Trade Policy
www.iatp.org

G8 “plus”¹ at L’Aquila, 2009

The feasibility, effectiveness and administrative modalities of a system of stockholding in ***dealing with humanitarian food emergencies*** or as ***a means to limit price volatility*** need to be further explored.

¹ = G8 + Algeria, Angola, Australia, Brazil, Denmark, Egypt, Ethiopia, India, Indonesia, Libya (Presidency of the African Union), Mexico, The Netherlands, Nigeria, People’s Republic of China, Republic of Korea, Senegal, Spain, South Africa, Turkey, Commission of the African Union, FAO, IEA, IFAD, ILO, IMF, OECD, The Secretary General’s UN High Level Task Force on the Global Food Security Crisis, WFP, The World Bank, WTO who attended the food security session at the G8 Summit in L’Aquila on 10 July 2009 and by the Alliance for a Green Revolution in Africa (AGRA), Bioversity/Consultative Group on International Agricultural Research (CGIAR), Global Donor Platform for Rural Development , Global Forum on Agricultural Research (GFAR).

Reserves: an ancient and persistent idea

- Joseph and the Pharaoh
- China from 498 A.D. (the constant normal granary)
- International Wheat Agreements (1949-1969)
- Nixon at the World Food Conf., Rome, 1974
- The U.S. farmer-owned reserve (1977-1996)

What issues do reserves address?

- Supply is historically erratic; demand is not
- Prices fluctuate more than supply because short-term supply and demand are inelastic
- The larger the price fluctuations, the greater the temptation to hoard, exacerbating the problem (and sending false market signals)
- World markets remain thin in most commodities; responses to the food crisis did not improve importers' confidence

What purpose can a reserve serve?

- Correct the basic failures of food markets: inelastic demand; lack of producer market power; obligation to do more than just supply “effective demand”
- Smooth out volatile prices (over time and space)
- Complement, stimulate and/or regulate the private sector
- Prepare for emergencies

What can a reserve not do?

- Solve chronic hunger
 - most hunger = lack of access not supply
- Operate at a profit, or even break even (insurance policies cost money)
- Operate without distorting markets
- Operate without mistakes
- Operate without transparent and accountable governance
- Operate without consideration of the dominant players: 3-5 grain companies

The U.S. Farmer-Owned Reserve

- System of 3 year contracts between government and farmers
- Farmers got a loan for planting + money to store part of their harvest
- Government got control over when and how much of the stored grain could be sold in open market

Pro Farmer-Owned Reserves

- Gave farmers more market power in an oligopsonistic market
- Stabilized world prices because U.S. a major exporter
- Was (with hindsight) cheap : millions not billions of US\$

Against Farmer-Owned Reserves

- Grain processors, feedlot operators, food companies looking for cheap inputs
- Claim that made U.S. grain less competitive (in fact, world prices in key commodities tracked the U.S. loan rate through the 1980s and 1990s)
- Claim that was expensive (subsequent policy has been much more expensive)

What happened without reserves?

- Cost of U.S. farm programmes soared when floor prices and on-farm reserves eliminated
- Export volumes stayed flat or declined
- Market power in grains, but also grain processing and livestock grew markedly more concentrated

Economist Daryll Ray on the outcome:

- The United States, ... (has) gone from adopting commodity programs because free markets didn't work decades ago to saying commodity programs are the reason free markets don't work today.”
- How to get the PSE to include the value of public investment in R&D that accounts for the fantastic productivity gains in agriculture? Would a free market have realized these gains for consumers?

International Reserves: Humanitarian

- Different crises need different responses (tsunami versus drought); different regions have different needs
- Internationally, a mix of grain and funds makes sense
- Multilateral coordination of regional or national reserves (not one single granary)
- Focus on administrative readiness: build the roads and ports; have a system in place; etc.

Price stabilization

- Think of it like a central bank: a necessary insurance policy (that must necessarily assume worse not even odds)
- Operate at arm's length with due oversight
- Properly paid and qualified staff
- Adequately financed (it cannot run at zero cost)
- Requires flanking measures, including tighter regulation of commodity exchanges

Proposal from the IWA experience

- A 20% stocks to use ratio avoids the price peaks that cause misery – worth it?

Think of some alternatives

- **Safety nets**

- Not a good response to peaks like those of 2007-2008 (solve a different problem)

More alternatives..

- **More open trade**

- What about the relative purchasing power of livestock for the wealthy and a slum dweller or rural labourer? Or EU's appetite for biofuels? What about the “blink” by exporters in 2007-2008 (Argentina, India, etc)

A third alternative

- **Let the private sector do it**
 - Why would they? Make money on volatility; have no reason to incur the expense of the stocks; have no obligation to realize the universal human right to food