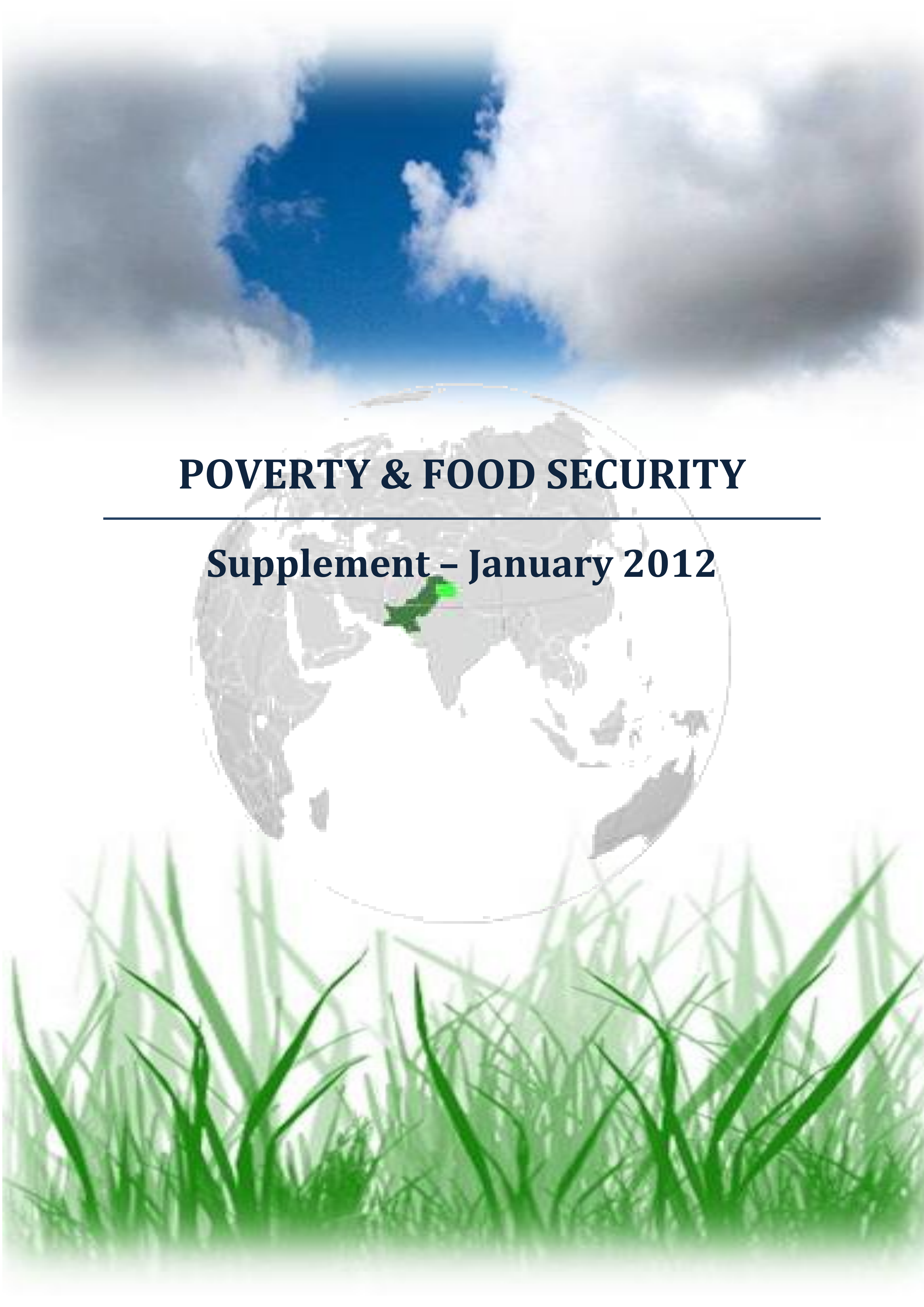
POVERTY & FOOD SECURITY

Supplement – January 2012



POVERTY & FOOD SECURITY

Inflation & Food Security

Domestic Context

No Free Lunch: Rising Price of Wheat Flour: Trust the Market to Deliver

There is a famous Urdu couplet which translates like this: you go back to the same 'hakeem' for medicine, whose very prescription has caused you illness. This self-defeating tendency was featured in the policy prescriptions announced at the policy forum organized by Oxfam GB recently on 'Food Price Volatility and Policy Options' in the wake of rising food prices. While correctly noticing alarming price hikes in basic food items such as wheat flour and sugar the government is asked to intervene to regulate prices and save farmers and consumers from the exploitation of middlemen. The correct policy prescription should have been the exact opposite: save the consumers, producers and middlemen alike from the all-knowing, benevolent government. By analyzing some factors in the pricing mechanism of wheat flour, it is argued how government policies have distorted the market of the wheat flour and what should be corrective course of action. Despite bumper wheat crop this year and a flour processing industry having 300% excess capacity, Pakistani citizens have still to reap benefit from the surplus production which should have brought prices of wheat flour (Atta) considerably down. Instead, prices of wheat flour have risen by 78% in last three years. The free flow of supply and demand forces that drive prices does not seem to work here. The fundamental hurdle is the government. The rules which the government enforces actually define the conduct of individuals, encourage cartelization and facilitate exploitation.

The typical critics of Free Market Economy would hold the free market responsible for the shortage and price hikes and would name the erstwhile middleman as key culprit. The judiciary will even take a *suo motu* notice on any letter that remotely relates the price hikes with human rights violation. The government will send in the price magistrates who will lock up the greedy and selfish shop keepers. The public will continue to suffer: perhaps more so by the absence and shortage of commodities, and less by their prices. Despite all these self-defeating approaches, even an old parrot will tell us that price escalation of commodities usually results from shortage in supplies. These shortages can occur due to bad policy; any illegal coordination amongst the suppliers like cartelization; or due to a fall in production. The government response should match the fundamental reason behind the shortage, which could range from a policy correction to an assertive pro-competition act to play golf aka do nothing. In the flour processing industry, no single player out of the 915 registered flour mills is large enough to influence the market. With this vast multitude of competing interests, this industry appears to function like a perfect competitive market. However the presence of quotas, as a tool to determine the level of production, not only distorts the market but almost guarantees rent seeking and corruption. These quotas are given by the government defining the level of production, which any mill can achieve.

In a freely functioning economy, a bumper crop of wheat, free market prices of wheat, and excess capacity in flour mills should only result in this scenario: ample produce for domestic market and value added exports of flour, coupled with a downward pressure on local prices. However, as our market economy is not free from rule-driven distortions, we only notice shortages, price hikes and unutilized capacities. If the wheat prices are set by the government and production levels of flour mills are also set by the government, then two-third of mills should shut down, in case of a free market in this sector. However, they continue to operate and flourish. These mills primarily benefit from quota trade instead of flour trade. Further, a high support price for wheat, another government intervention, raises the cost of production Thus the flour price hike is a direct result of bad policy and not shortages. The government must remove quotas and let inefficient firms shut down and let those firms who can, export their value added flour. Let market forces decide the price of wheat. Allow free movement of flour – both in domestic and international markets. Trust the market to deliver. Only then, we can learn how to deal with its failures. When a private sector firm fails, it has to close down. It is time that we also ask the government to follow this time tested principle of creative destruction.

The Express Tribune - January 16, 2012

Agriculture, Construction Sectors Badly Affected

Skyrocketing increase in prices of fertilizers, cement and compressed natural gas (CNG) during the last one year have affected agriculture and construction sectors and confronted the government's various development projects with "cost overrun". Rising prices of gas and cement have drastically affected the government's arrangements for properly executing various projects of public interests and work on some has been stopped. According to the Pakistan Bureau of Statistics (PBS) latest figures, during the last one year fertilizer prices have jacked up in the range of 31-71 percent during the week ended on January 26 over the corresponding week last year, which may hit the agriculture growth. Besides, cement prices went up by 22 percent to Rs. 425 per bag and CNG prices by 27 percent to Rs. 71 per kilogram. If persistent increase in prices of fertilizers, CNG and cement was not capped, agriculture, the mother sector of Pakistan's economy may face snags in growth, while infrastructure development projects would face costs overrun and swell transportation cost in the coming months. Food prices and transportation charges are skyrocketing, but still there is no respite available to the poor from the government side. The government seems to be indifferent to the plight of the poor and the lower-middle class who find it increasingly difficult to make both ends meet with soaring prices of the foodstuff. Frequent and prolonged gas outages and high energy prices led to reduced fertilizer production, which is an important input for the agriculture produce, they said, adding that this contributes to higher prices for all agricultural commodities and it looks 'permanent'.

According to the official data, Kissan urea prices increased by 71 percent to Rs. 1,785 per bag, Sona urea went up by 67 percent to Rs. 1,827, C Ammonium Nitrate 70 percent to Rs. 1,451, potassium sulphate 52 percent to Rs. 3,817, S SP Phosphate (GR) 47 percent to Rs. 1,294, S SP Phosphate (PD) 38 percent to Rs. 1,100, Nitro Phosphate 34 percent to Rs. 2,752 and T SP phosphate (GR) went up by 33 percent to Rs. 3,100 per bag over corresponding week last year. Besides, Di-Ammonium Phosphate (DAP) price increased by 31 percent to Rs. 4,140 per bag and nitrogen phosphate and potassium (NPK) prices raised by 36 percent to Rs. 3,188 per bag during the week ended on January 26 over the same period last year. Due to high agriculture input prices, most of the poor farmers leave their holdings uncultivated. Even with the fact that Pakistan has the largest canal irrigation system in the world, its average wheat yield ranked ninth, rice (paddy) 14th, sugarcane 14th, seed cotton 11th and maize 18th in the world. Since long, the growers' financial woes have multiplied as the government has increased power tariff on agricultural tube-wells and increased prices of fertilizers will further aggravate the situation for the farmers. Besides, cement cartels in Pakistan had got free hand and they are earning abnormal profits of billion of rupees at the cost of the consumers. This is hitting not only consumers, but also development works, which further hit the economic activities, as well.

The News - January 29, 2012

Global Context

World Lacks Enough Food, Fuel as Population Soars, Says UN

The world is running out of time to make sure there is enough food, water and energy to meet the needs of a rapidly growing population and to avoid sending up to 3 billion people into poverty, a UN report warned on Monday. As the world's population looks set to grow to nearly 9 billion by 2040 from 7 billion now, and the number of middle-class consumers increases by 3 billion over the next 20 years, the demand for resources will rise exponentially. Even by 2030, the world will need at least 50 percent more food, 45 percent more energy and 30 percent more water, according to UN estimates, at a time when a changing environment is creating new limits to supply. And if the world fails to tackle these problems, it risks condemning up to 3 billion people into poverty, the report said. Efforts towards sustainable development are neither fast enough nor deep enough as well as suffering from a lack of political will. The current global development model is unsustainable. To achieve sustainability, a transformation of the global economy is required. Tinkering on the margins will not do the job. The current global economic crisis ... offers an opportunity for significant reforms."Although the number of people living in absolute poverty has been reduced to 27 percent of world population from 46 percent in 1990 and the global economy has grown 75 percent since 1992, improved lifestyles and changing consumer habits have put natural resources under increasing strain. There are 20 million more undernourished people now than in 2000; 5.2 million hectares of forest are lost per year - an area the size of Costa Rica; 85 percent of all fish stocks are over-exploited or depleted; and carbon dioxide emissions have risen 38 percent between 1990 and 2009, which heightens the risk of sea level rise and more extreme weather.

The panel, which made 56 recommendations for sustainable development to be included in economic policy as quickly as possible, said a "new political economy" was needed."Let's use the upcoming Rio+20 summit to kick off this global transition towards a sustainable growth model for the 21st century that the world so badly needs," EU Climate Commissioner Connie Hedegaard said in response to the report, referring to a UN sustainable development summit this June in Brazil. Among the panel's recommendations, it urged governments to agree on a set of sustainable development goals which would complement the eight Millennium Development Goals to 2015 and create a framework for action after 2015.They should work with international organizations to create an "evergreen revolution," which would at least double productivity while reducing resource use and avoiding further biodiversity losses, the report said. Water and marine ecosystems should be managed more efficiently and there should be universal access to affordable sustainable energy by 2030.To make the economy more sustainable, carbon and natural resource pricing should be established through taxation, regulation or emissions trading schemes by 2020 and fossil fuel subsidies should also be phased out by that time. National fiscal and credit systems should be reformed to provide long-term incentives for sustainable practices as well as disincentives for unsustainable ones. Sovereign wealth and public pension funds, as well as development banks and export credit agencies should apply sustainable development criteria to their investment decisions, and governments or stock market watchdogs should revise regulations to encourage their use. Governments and scientists should also strengthen the relationship between policy and science by regularly examining the science behind environmental thresholds or "tipping points" and the United Nations should consider naming a chief scientific adviser or board to advise the organization, the report said.

The Nation - January 31, 2012