



# Institute for Agriculture and Trade Policy

**A Time of High Prices:  
An Opportunity For the Rural Poor?**

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## **A Time of High Prices: An Opportunity For the Rural Poor?**

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The Institute for Agriculture and Trade Policy works locally and globally at the intersection of policy and practice to ensure fair and sustainable food, farm and trade systems.

## A Time of High Prices: An Opportunity For the Rural Poor?

### Abstract:

Eyes all around the world are turned toward agricultural markets. Climate change, the rising price of oil, biofuels, speculation on financial markets and income growth in emerging economies are some of the factors that have combined over the past two years to cause an unexpected rise in commodity prices.

After decades of low prices, this increase should be good news for farmers and countries that produce agricultural products. To some extent, we argue, higher prices can bring some benefits, although not necessarily in the short term. The rapid price increases are causing enormous stress for the urban and rural poor in regions dependent on food imports. Net food-importing, low-income countries are struggling to pay the food import bills, which diverts money from other needed investments. It is time for an urgent rethink of the respective roles of markets and governments. Strong agricultural policies will be needed to make high prices work for development.

Ministers gathering in Accra for the UN Conference on Trade and Development, UNCTAD XII, need to take a hard look at the record of three decades of commodity market liberalization and must take action to rebalance power relations in agricultural markets.

### Introduction

Attention to international agricultural markets has reached an unusually high level. Sudden and sharp increases in prices have surprised policy makers, enticed investors and caught the media's attention. Over recent decades, low agricultural prices were considered a given. Even two years ago, discussions on global agricultural commodities were all premised on persistent low prices and the importance (and difficulty) of diversifying developing country economies into higher value-added activities.

All that has changed. The spike in food prices is making headlines around the world. The UN Food and Agriculture Organization (FAO) reports that of the 37 countries worldwide facing food crises, 21 are in Africa. Food riots started in Mexico in early 2007 over the rising cost of tortilla flour. Many more countries have since experienced similar protests, including Egypt, Cameroon, Cote d'Ivoire, Senegal, Burkina Faso, Ethiopia, Indonesia, Madagascar, the Philippines and Haiti in the month of March 2008 alone. In some countries, the World Bank fears that food price increases will cancel gains made in recent years to alleviate poverty. The World Food Program worries that higher food prices threaten not only the poor's access to food, but also to health and education.

The devastating effect of high food prices for consumers in poor countries are well-documented, and a lot of attention is—rightly—focused on how to avoid a major humanitarian crisis. But since three quarters of the world's 1.2 billion extremely poor people live and work in rural areas, the huge backlash against high agricultural prices needs careful thought. Weren't low commodity prices identified as a major obstacle for development since the 1960s? Wasn't international trade liberalization supposed to get rid of harmful subsidies in the North in order to improve prices for farmers in the South? The liberalization of global agricultural trade was in part being sold to governments as a way to raise world prices. Higher world prices were supposed to be a good thing. What has changed?

Agricultural commodities are critically important to many developing countries' economies. They determine whether those economies produce sufficient jobs, food, foreign exchange and economic activity to keep people out of poverty. Through its strong linkages with other sectors, agricultural growth provides the basis to build a more diversified economy. Taking a step back from the current food emergency, this paper will look at the effect of high prices on producers at the national and household levels.

There are many unanswered questions around current high prices: what causes the sudden increase in prices? Are high prices here to stay? Can higher prices help the poorest countries get back on the road to development? Are farmers really gaining from high prices?

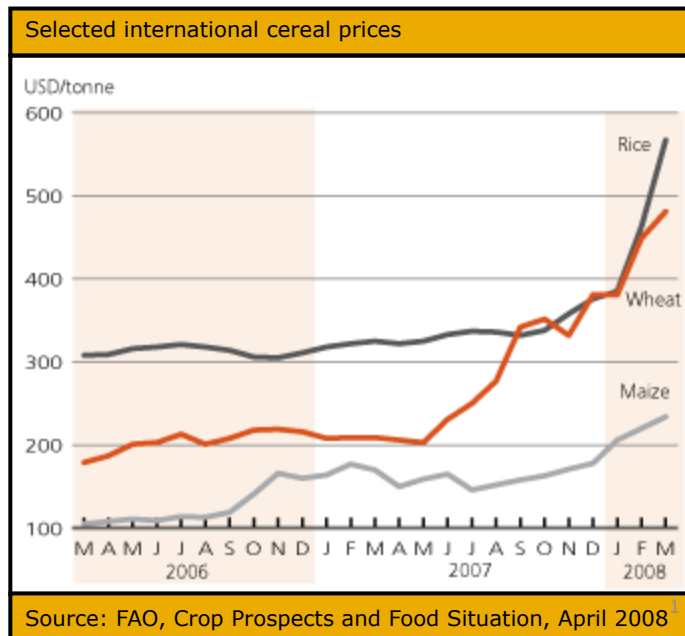
To properly identify the opportunities associated with the current situation, it is important to take a closer look at the mix of dynamics affecting agricultural markets. Climate change, the price of oil, biofuels and income growth in emerging economies are some of the reasons for high prices. Speculation on financial markets and the outcomes of two decades of agricultural market liberalization also have to be considered.

From April 20–25, 2008, UN member states will gather for the 12th session of the UN Conference on Trade and Development (UNCTAD XII) in Accra, Ghana. UNCTAD is an organization that has a long history of grappling with the "commodity crisis." It has provided developing countries with important thinking and ideas on how to manage their commodity sectors.

UNCTAD has often questioned the prevailing ideological approach to agricultural development, which is based on a largely theoretical version of free trade. The policies pushed by developed countries through the World Trade Organization and the World Bank have encouraged a system that has no way of regulating supply or of managing production shortfalls. Market deregulation has opened the door for extreme price volatility in agriculture. A new set of rules could bring us closer to stabilizing prices, and promote real long-term development. At UNCTAD XII, governments should take steps to transform the new situation into one of opportunity. This will require governments to commit themselves to a new framework to manage international agriculture markets. UNCTAD XII is a place to start.

## WHAT IS HAPPENING IN GLOBAL AGRICULTURAL MARKETS?

After decades of global agricultural prices in decline, the past two years have witnessed exceptional price surges for most commodities, starting with grains and dairy prices.



According to the World Bank, prices for maize and vegetable oils increased by 33 and 50 percent respectively in 2007, while wheat prices increased by 30 percent.<sup>2</sup> By September 2007, the FAO dairy price index peaked to an all time high, some 120 percent more than in September 2006.<sup>3</sup> On average, in 2007, the price of food and tropical beverage commodities rose by 24 percent, according to UNCTAD.<sup>4</sup>

Commodity markets are volatile and short-term price hikes are not uncommon. The recent price increases, however, have drawn renewed attention from observers for several reasons. First, they are affecting all commodities, not just one in isolation. Second, there are new dynamics that are radically changing agricultural markets. Wealthier populations in the most populous parts of the world—Russia, China, India and Brazil—are consuming more meat, dairy and processed foods. Energy consumption is also dramatically increasing, and agriculture, in the form of biofuels, is heavily pushed as an alternative energy source to fossil fuels. Finally, environmental and climatic constraints are affecting farmers' ability to respond to the growing demand.

## WHAT IS CAUSING THE PRICE RISE?

Cereal production experienced a tremendous shortfall in 2006, due mostly to bad weather conditions in some major producing areas (including Australia, the United States and Canada): world production decreased by 70 million tons in 2006-2007 from 2005-2006 levels—almost 7 percent of global cereal production.<sup>5</sup> The effect on world prices was immediate.

The reason for the sustained and widespread increase in prices, though, lies in a more complex web of factors: growing and changing world populations, the biofuels revolution, climate change and renewed interest from financial investors in agriculture. These factors are exacerbated by the fact that government intervention in the market has been significantly curtailed in the past two decades.

## **A growing and wealthier world population**

World population is growing fast: it is projected to reach 9 billion by 2050, from around 6.5 billion in 2008. The increasing demand for food as a result of population growth is not expected to slow down.

Population will also continue to grow in urban areas. According to the UN, 2008 is the first year in history when more than half of the world's population is living in urban areas. This shift is affecting food production through pressure on land and on the workforce active in agriculture. It is also affecting consumption patterns and, as a result, the demand for agricultural products.

Better-off urban middle classes in Russia, China, India and Brazil in particular, are increasing their consumption of meat and dairy products, as well as processed food. In India alone, meat consumption has increased by 40 percent over the past 15 years.<sup>6</sup> In China, per capita meat consumption has increased from 20kg in 1980 to 50kg today.<sup>7</sup> According to the FAO, 7 to 8.5 kg of grain are needed to produce 1kg of beef, and it takes 5 to 7kg of grain to produce 1kg of pork.<sup>8</sup> Rapidly changing diets mean that the demand for grains is increasing at an even greater pace than population growth.<sup>9</sup>

These trends are important, but they are not sudden or unexpected developments. Emerging hopes that agriculture can help the world meet its ever-growing energy needs and cope with failing fossil fuel reserves have had much more unexpected impacts.

## **The rise of biofuels**

Energy crops are not a new thing: they are produced by farmers all around the world. What is new, however, is the scale of production for biofuels—to provide alternative fuels for transportation – which has grown dramatically over the past few years. According to the World Bank, 20 countries now have mandatory biofuels use policies. The U.S. and EU in particular, have set very ambitious biofuels consumption targets.

In 2007, 11 percent of the global maize crop went to ethanol production in the U.S. and this share is set to continue rising. This has an important impact on world markets, since the U.S. provides 50 to 75 percent of global corn exports; most of the corn used for ethanol production is diverted from corn that was previously exported.<sup>10</sup> Biofuels are also made from sugar cane, cassava, oilseeds and palm oil around the world, particularly in tropical countries.

Because the enthusiasm for biofuels is so sudden, and grain reserves have been largely abandoned, it has created a new and growing demand that has shocked the system, which has not yet had time to match demand with a corresponding increase in production. The ambitious consumption targets for biofuels set by governments in developed (and some developing) countries are encouraging tremendous investment in production capacity around the world—in some cases at the expense of food production—as well as speculation on further growth in production and prices.

## Investment and speculation on commodities in financial markets

The influence of financial investors, including speculators, on commodity markets has significantly increased since 2000. The UN Food and Agriculture Organization (FAO), in its publication *Food Outlook* from November 2007, highlights the increasing linkages and spill-over effects between commodities and the financial sector. The impressive growth in international financial markets over the past few years has resulted in enormous amounts of money being available for investment. As other assets became less attractive, particularly after the Internet bubble burst in 2000, a growing part of that money has been invested in agricultural commodity markets. UNCTAD explains: "An illustration of the growing interest in commodity investment is the volume of commodity futures and options traded globally, which grew faster than in other market in 2006. The volume of global futures and options in agricultural commodities increased by 28.4 percent."<sup>11</sup>

Because of the lack of transparency on financial markets, it is difficult to assess exactly how much has been invested in commodities as a financial asset, and how much such investment has influenced the level of prices. Both the FAO and UNCTAD think financial investment in commodities is primarily causing increased volatility on commodity markets.

The FAO also notes that "the fact that the dollar depreciated sharply against major currencies lessens the true impact of the rise in world prices."<sup>12</sup> The U.S. dollar has lost a significant share of its value since 2005. Because most international commodity prices are expressed in U.S. dollars, part of their increase can be explained by this loss of value of the currency. It is difficult to make an overall assessment of how much this factor plays a role, however, since buyers are affected differently depending on the relationship between their currency and the dollar. A number of developing country currencies are directly or closely tied to the U.S. dollar; a number of others are linked to the Euro. This is a dimension of commodity price increases that deserves further clarification.

## New environmental constraints: failing oil reserves and climate change

Past experiences have demonstrated farmers' ability to respond to increases in demand, although often after a certain time lag. Throughout the 20th century, productivity gains consistently outstripped the rising demand created by a growing (and increasingly wealthy) world population. This time around though, farmers' ability to respond is affected by soaring energy prices, intense stress on natural resources and unpredictable, extreme weather patterns that are the result of climate change.

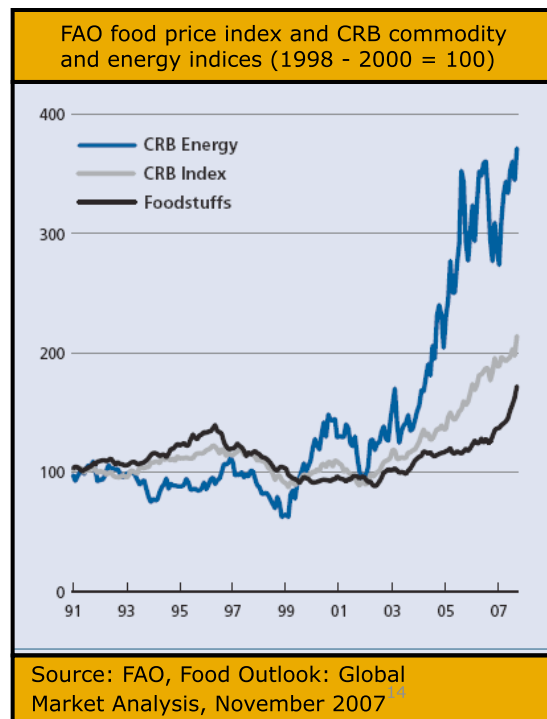
**Oil and energy prices** have been on a sharp rise since the turn of the century. Petroleum prices have more than tripled since 2000, and are experiencing unprecedented volatility, with the price per barrel regularly getting close to the US\$100 threshold. Because of the rapidly approaching exhaustion of the cheapest and most accessible fossil fuel reserves, coupled with geopolitical instability in key producing regions, oil prices are expected to continue increasing.<sup>13</sup>

Rising oil prices affect agriculture and food production in several ways: they increase the costs of production (oil is a big factor in agricultural input prices, for fuel and the production of inorganic fertilizers and pesticides) and they increase costs of storage and transportation. Soaring prices of oil also explain the sudden enthusiasm for biofuels as an alternative source of energy.

Environmental constraints are also affecting agricultural production in unprecedented ways, mainly due to **climate change**. Agriculture production is obviously hugely dependent on climate. The Intergovernmental Panel on Climate Change (IPCC—a scientific body set up to provide governments with objective information about climate change), in its 2007 Synthesis Report, released figures about the anticipated effects of climate change on crop yields in different regions of the world. The outlook is mixed but the challenges are daunting, particularly for the poorest developing countries: in Africa, agricultural yields could be reduced by up to 50 percent by 2020. Weather extremes everywhere (not least droughts, floods and tornados) will become more frequent, with a direct impact on crop yields and thus prices. The long and severe drought that has affected Australia’s wheat production over the past years appears as a warning of how brutal climate disruptions can be in the future. Increased uncertainty and the resulting price volatility is perhaps the most predictable consequence of climate change.

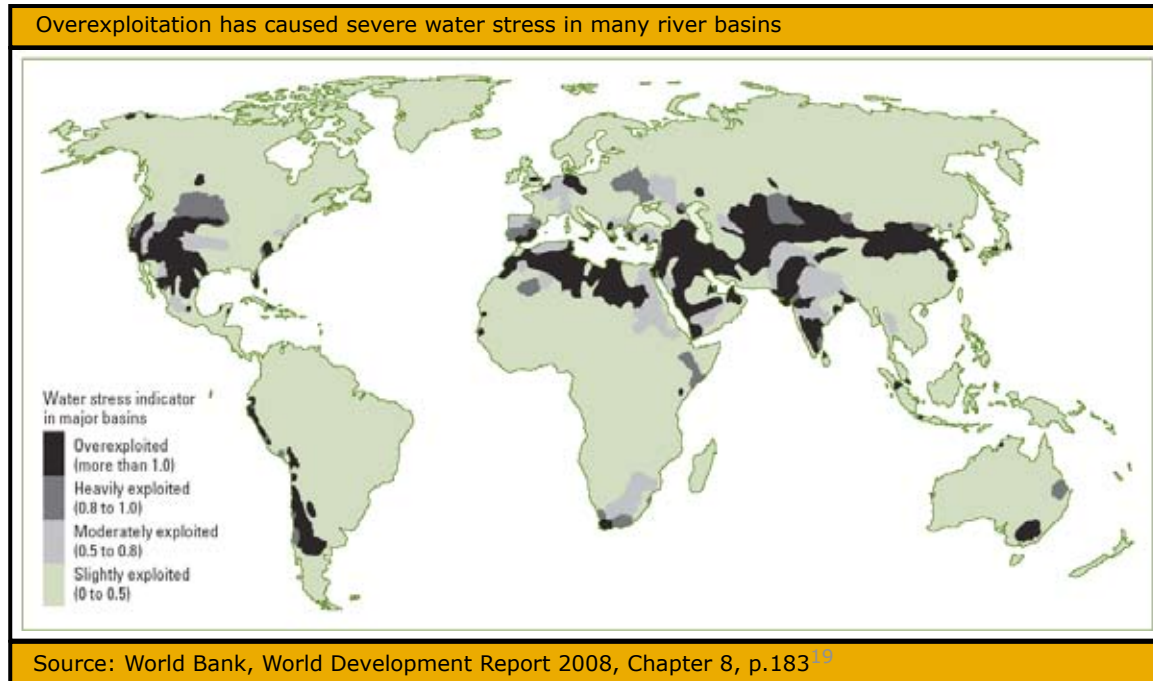
**Land and water** are also under particular stress. Nestlé chief Peter Brabeck put it bluntly to the Financial Times in February 2008: “We will not find sufficient water to produce all the crops... There will be a fierce fight for arable land.”<sup>15</sup> Arguably, there is an opportunity to increase the amount of land available for agricultural production in certain regions. The FAO points in particular to the 23 million hectares that have been withdrawn from production in recent years in Eastern Europe and Central Asia. But concerns over deforestation, soil degradation on existing farm land and desertification as a result of climate change mean that the availability of land for production is, to a large extent, a moving target.<sup>16</sup> According to the World Bank, “land constraints can be relaxed in many regions in response to rising prices, but only at a significant environmental cost.”<sup>17</sup>

The water challenge is huge. According to the World Bank’s 2008 World Development Report, one third of the developing world’s rural population is living “in areas characterized by frequent moisture stress that limits agricultural production” and “many countries are experiencing serious and worsening water scarcity.” The IPCC predicts that by 2020, between 75 and 250 million people in Africa will be exposed to increased water stress. Furthermore, “globally, about 15-35 percent of total water withdrawals for irrigated agriculture are estimated to be unsustainable—the use of water exceeds





the renewable supply.”<sup>18</sup> Gross wastage in existing systems, inappropriate cultivation encouraged by poor water policy, conflicts between urban and rural users, and depleted aquifers are all contributing to rising water costs and lower productivity for agriculture in a number of regions.



## GOVERNMENTS UNABLE TO RESPOND

Global agricultural markets have undergone profound transformations over the past three decades, with prevailing economic theories supporting the dismantlement of agricultural policies and the liberalization of agricultural trade. The implementation of these theories is pushed on developing countries through trade agreements as well as “structural adjustment programs” supported by international financial institutions (the World Bank and the International Monetary Fund). Over the course of the past three decades, developing country governments have abandoned many of the tools that would enable them to respond to the increase in prices with a corresponding increase in production.

At the national level, governments’ ability to support agricultural production using direct interventions in markets has been significantly reduced. Structural adjustment programs and international trade agreements (including the Uruguay Round Agreement on Agriculture) have significantly curtailed governments’ ability to manage commodity production and trade. Tools previously available to help step up production in times of scarcity, to manage stocks to even out supply between good and less good years or to help producers adapt to changing production constraints, are no longer permitted under existing trade and investment agreements. For better and for worse, farmers are now more directly affected by price changes, and have to directly negotiate the marketing and distribution of their crops. Before, public institutions were able to soften the effects of price volatility, and could ensure that farmers got a reasonable price for their production.

Similarly, at the international level, trade negotiations and agreements have focused on the need to free markets from government interventions and to expand trade at any cost. In many cases however, rather than establishing fairer markets, these policy changes have resulted in strengthening the position of the most powerful players, particularly transnational companies. Transnational agri-businesses have thrived on market deregulation, and in many places, have pushed small and diversified growers out of the market in their bid to establish stable and homogenous suppliers for their processing needs.<sup>20</sup> This has led to radical changes in production structures around the world.

In his review of the commodity crisis, development analyst Duncan Green writes, "Since the demise of supply management, corporate concentration has been the most significant change in the global commodity trade and it is only likely to grow in importance and extent."<sup>21</sup> During the current crisis of high food prices, it is hard not to remember policy makers' insouciance about abolishing publicly held food reserves only ten years ago. The claim was that in a deregulated market, private companies would be sure to hold onto stocks, effectively providing the necessary reserve to keep prices stable. In practice, companies have not stepped up to play this role. There are at least two good reasons why not: a) it is expensive to hold onto reserves, and they look bad on the quarterly report to stockholders, and b) transnational grain traders make money from speculation, and thus have a direct interest in volatility, even when that volatility is bad for other aspects of business.

## **ARE HIGH PRICES HERE TO STAY?**

Estimates differ on whether prices will remain high in the long term or whether markets are only experiencing a temporary peak. This uncertainty itself is fueling further price increases and volatility!

Most experts agree, though, that prices will remain high, if also volatile, for at least the next two to three years, as it will take time for farmers to adapt to higher demand. The question is: what happens after the current peak?

The last time prices increased this quickly was at the beginning of the 1970s, following a crop failure in what was then the USSR, traditionally one of the world's big grain producers. Farmers at that time were encouraged to increase their production by all means possible to meet the demand of what was characterized as a growing and hungry world population. It did not take long for production to outstrip demand, which led prices to fall again and left farmers confronted with high costs of production that were unsustainable at lower price levels. Many had made big investments in their farms that they were unable to pay for when supply grew, demand fell, interest rates rose and prices collapsed.

This experience suggests those betting on sustained high prices should be cautious, especially in the current global economic climate. For starters, prospects for the global economy are uncertain as the financial crisis triggered by the collapse of sub-prime mortgages spreads to the banking sector. The World Bank explains that if the U.S. slowdown were to worsen, it would affect emerging markets and as a result, lower the demand for commodities and push their prices down again.<sup>22</sup>

Second, speculation on agriculture commodity markets is significant and highly volatile. Just as speculation drives prices up, it can also drive them down when investors think supply might be catching up with demand again. Even a simple recovery to pre-drought production levels from some of the bigger world producers could make a dent on prices.

Third, the acreage that could be brought into production for biofuels feedstock remains to be determined. As questions arise around biofuels' alleged benefits, the U.S. and EU might consider reviewing their policies and production targets. The possible development of "second generation" biofuels would also affect prospects; cellulosic ethanol could considerably reduce the competition for land between food and fuel.

The combination of these factors and uncertainties reinforces the tendency for agricultural markets to be volatile. As the FAO notes, "international prices of agricultural commodities are renowned for their high volatility, a feature which has been, and continues to be a cause of concern among governments, traders, producers and consumers."<sup>23</sup> The FAO goes on to say, "it now appears more of a permanent feature in the grain markets than was the case in the past." Stretched stocks everywhere contribute to increased volatility, as markets become nervous about their ability to play their traditional buffer role. Increased volatility constitutes a major challenge for stakeholders all along the food chain.

Ultimately, average price levels will depend on farmers' and policy makers' ability to integrate and adapt to the new scarcity of natural resources. Despite the now universal acceptance of negative effects from climate change as presented by the IPCC, the environmental crisis has not yet received the necessary action from decision makers. Only recently did the World Bank recognize that "the agriculture-for-development agenda will not succeed without more sustainable use of natural resources."<sup>24</sup> While growth in agricultural production in past decades has benefited from increased land and water use, the 21st century cannot replicate the same pattern. Sustainable innovation will be required to address new environmental constraints. On the one hand, failure to tackle these issues adequately will result in tighter agricultural supplies, causing high and volatile prices. On the other hand, the internalization of environmental costs in commodity prices is likely to induce price increases as well—if properly managed, they need not harm final consumers, and will provide for more sustainable production methods and more reliable income for some of the world's poorest people.

## **CAN HIGHER PRICES HELP THE POOREST COUNTRIES GET BACK ON THE ROAD TO DEVELOPMENT?**

Low agricultural prices have constituted a major obstacle to development, particularly for the poorest developing countries. They depend heavily on commodities for their export earnings. Over the course of the past decade, many have increased their export volumes, but since the value of their exports fell in parallel, they ended up running to standstill. Low-income countries have also sharply increased their dependence on food imports<sup>25</sup> in part because of their producers' inability to compete with products sold at below their costs of production as a result of dumping, without improving their capacity to pay for such imports through development elsewhere in their economies.<sup>26</sup>

Remunerative agricultural prices are critically important to fuel the development engine. Better commodity prices are needed for developing countries to be able to accumulate capital for investment in other sectors. Farmers' inability to make a living out of the sale of their production has been a major obstacle to poverty alleviation. The World Bank estimates that in 2008, 900 million rural people in the developing world live on less than US\$1 a day; most of them are engaged in agriculture. High prices, assuming that they lead to higher income, offer opportunities to alleviate this poverty.

The picture is not that bright at the moment however: rising expenses on the import side, as well as the weakness or inefficiency of their agricultural sectors, are preventing poor countries from reaping substantial benefits of higher prices in the short term.

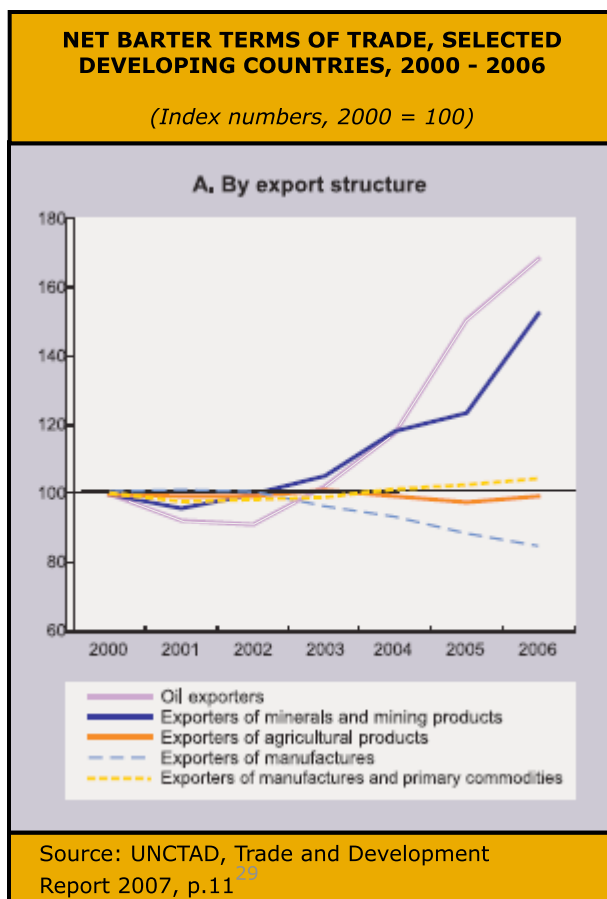
## Increase in food and energy expenses

For commodity exporting countries, higher prices bring increased export earnings, which benefit producers and can have spill-over effects on the economy as a whole if redistribution takes place. For 2006, UNCTAD reports a 15 percent growth in the value of Africa's exports over a year, while the figure is 20 percent for Latin America and the Caribbean.

Because of higher energy and food prices however, these gains have often been offset by rising import bills. Oil-importing countries and net-food importing countries are affected most directly. The FAO expects Low Income Food Deficit Countries' (LFIDCs) import bill to rise by 35 percent for the second consecutive year in 2008. "A higher

increase of 50% is estimated for the LFIDCs in Africa, which will be putting a heavy financial burden on several countries."<sup>27</sup> In countries where food subsidies exist, such as Egypt, Oman and Pakistan, costs are skyrocketing. Whether countries will be able to sustain this situation very much depends on how their export earnings evolve. But according to the USDA's Economic Research Service, "recent trends suggest that prices for commodities exported by [low-income] countries are not growing as fast as grain or vegetable oil prices."<sup>28</sup> In February 2008, the FAO identified 36 countries in food crisis, not only, but partly, due to higher prices.

As the following graph from UNCTAD's 2007 Trade Development Report shows, countries that rely mostly on exports of agricultural products have seen their situation improve only marginally.



## Unfair distribution of benefits

Countries that export oil and minerals have registered important windfall gains over the past few years. However, UNCTAD figures<sup>30</sup> show that in countries where foreign firms are dominant in the mining industry, the firms have extracted important remittances that they send back to their headquarters, considerably reducing the possibility for higher prices to have a positive effect on national incomes in the poor countries involved. Furthermore, even when countries have been able to retain some of the benefits, the money is often not redistributed equitably nor used to realize development objectives.

The power of transnational companies on international agricultural markets is further hampering developing countries' ability to reap more benefits from high prices in the agricultural commodity sectors. Because of the size of their market shares, companies end up being the ones who decide what gets sold or not and at what price: the "invisible hand" of the market is unable to counter-balance their influence. To a large extent, these companies control the distribution of benefits along the value chains, and they significantly constrain developing countries' diversification efforts.

## Volatility limits long-term development

As prices increase, so does the volatility. Intense price volatility is a major limitation to countries' ability to build a long-term development strategy based on a strong and remunerative agricultural sector. Volatility makes planning difficult and can have destabilizing effects on exchange rates.

Since governments, particularly those of industrialized countries, pushed for the dismantlement of International Commodity Agreements (ICAs) in the 1980s and for further agriculture market deregulation at the WTO, developing country producers have been left with very little influence on the prices of the products they sell; they are what is called "price takers." They can try to make the most of favorable situations when they arise, but they remain vulnerable to market failures of all sorts. Unless the uncertainty associated with the current high prices is addressed, the most vulnerable developing countries will not benefit.

## DO FARMERS BENEFIT?

Since developing countries' import dependence has grown over the past three decades as a result of agriculture market liberalization, price transmission between global and national markets tends to be more immediate and widespread. Its magnitude varies depending on the country of course: some are more open than others (typically those with the largest debt burdens have had to liberalize more radically), some protect particular products more than others (rice in some Asian countries for example) and some, because they are landlocked, are less directly affected by price fluctuations in world markets (Mali is an example).

Farmers' share of the benefits thus depends on the distribution of prices along the value chain at the national level. In Pakistan, for example, wheat farmers have not benefitted from higher prices on international markets; intermediaries have not passed the increase on to them. Those farmers who have little access to information about market developments and who depend highly on intermediaries to sell their products are likely to be left out of the price increases.

Even for those farmers who are selling their products at better prices, the final impact on their income is not necessarily positive, because of the rise of their costs of production. The costs of energy are skyrocketing, as mentioned earlier. Fertilizer prices have experienced a 150 percent increase over the past five years, according to the World Bank. The price of seeds is also on the increase, and this is all the more true where corporate concentration has given seed companies the market power to impose prices on producers. Renewed interest for agriculture and its economic value have also attracted powerful interests to increase their investment in land. Many rural households in developing countries are also net-buyers of food: higher food prices affect their overall spending. Whether farmers benefit from the current price dynamic in the short term is thus far from obvious. The question needs further investigation and it is wise to avoid generalizations across developing countries.

### **Will high prices favor production increases in poor countries?**

In South America, corn acreage reached a record high in 2007 and is expected to remain at the same level in 2008. Brazil is significantly increasing its wheat production as a result of more attractive prices. Capital-intensive farming in the South America region is the most obvious winner, in the short term at least, of the price increases.

In the poorest developing countries, however, farmers' ability to step up production is hampered by lack of capacity. Decades of low prices, low investment and market deregulation have undermined their ability to respond to new increases in demand. Access to credit and inputs is difficult for them when they have to rely on private actors: small farmers are not considered a good investment.

The rural poor do not automatically or immediately benefit from higher commodity prices. In the short term, those farmers that are best equipped, and well connected to the markets, are the ones reaping the benefits. World Bank data shows that countries in South America are the ones benefiting. Making sure that high prices reach the poorest and provide benefits for low-income countries will require more effort.

In the short term, the crisis is bringing an increased level of attention to farmers' role in developing countries—the good news of these difficult times. The devastating impact of high commodity prices on the poor's access to food has triggered recognition from policy makers that leaving food security to world markets is not sustainable. Governments should thus feel encouraged to invest in their agriculture sector so that they can respond to domestic needs. Recently, the UN International Fund for Agricultural Development (IFAD), through its Governing Council and Farmers Forum, called on UN Member States to "urgently direct their policy attention and their investments towards smallholder agriculture and rural livelihoods."<sup>31</sup>

### **WHAT IS THE WAY FORWARD?**

Remunerative prices for commodity producers are much needed. Farmers can only get out of poverty if they receive a sustainable income from their production. Commodity producing countries can only invest in and diversify their economies if they improve their balance of payments, including through better and more reliable export earnings. Higher prices on international markets are not enough. They risk missing farmers, especially low-income, resource poor farmers, altogether. If left to highly volatile and concentrated international agriculture markets, agricultural development is unlikely to meet the challenges ahead.

The importance of governmental and intergovernmental action to regulate agriculture markets needs to be reassessed. The international community needs to fundamentally rethink the respective roles of markets, governments and private actors in dealing with agricultural development. Here are some first steps:

- **Urgently step up support to the agriculture sector**

The dismal state of agriculture in many developing countries explains why they are unable to reap immediate benefits from higher prices and ensure their peoples' food security in a time of high prices. The World Bank's 2008 World Development Report showed the growing consensus that support for agriculture needs to be revived, after decades of damaging neglect. Governments and communities need to build the institutions and physical infrastructure they need for a productive agricultural sector that is ready for the challenges that lie ahead. Developing country governments need to dedicate to agriculture a level of attention and funding that is commensurate with the importance of the sector for their development and food security. The proportion of Official Development Assistance allocated to agriculture needs to be increased significantly.

- **Address price volatility**

Addressing the harmful effects of intense price volatility requires actions at the national and international levels. At the national level, farmers need to be shielded from excessive price fluctuations so that they can plan and invest in the medium-to-long term. Providing farmers with a more predictable environment should be a priority of new agricultural policies. Making sure that they have access to reliable information on market conditions is a first step. Institutional support for the marketing and distribution of their crop will, in most cases, be needed as well.

At the international level, addressing volatility requires coordinated action to manage agriculture supply. It will ensure a fairer deal for producers as well as a more reliable supply of higher quality commodities for consumers. It will also discourage speculation on commodity prices. At the WTO, the African group submitted a proposal on the need to allow commodity producing countries to strike agreements among themselves in order to stabilize prices. Only if such initiatives receive broad international support and engagement, though, are they likely to deliver.

- **Regulate the distribution of benefits along value chains**

The "invisible hand" of the market has proved unable to deliver a development-friendly distribution of benefits along value chains. Governments at the WTO by and large ignore the incredible market power that a few transnational corporations hold at the expense of other stakeholders in global value chains. In addition to their influence on commodity prices, they also constrain diversification opportunities. International trade rules cannot continue to ignore this reality. As a first step, international disciplines should be developed to ensure that these firms' influence is better documented. A multilateral institution—perhaps FAO or UNCTAD or a collaboration between the two—could be charged to maintain a databank with comprehensive information on the dominant actors in the global food system. The data should be accessible to the public on-line, and the findings published periodically. The question of private standards and how they affect developing countries' export and diversification prospects also deserves more attention.

- **Develop environmentally sustainable methods of production.**

- **Adapt agriculture to climate change**

Environmental constraints need to be better integrated in development policies at the national and international levels. Publicly supported research will need to be stepped up and directed at healthy production models that make a moderate use of fossil fuels, water, soil and pesticides. The IPCC has provided initial ideas on how to make sure agriculture adapts to climate change, and also on how it can contribute to mitigating climate change. They can help governments design development-friendly agricultural policies.

- **Design bioenergy policies adapted to local conditions and needs**

In light of the disconcerting effects of the worldwide rush to large-scale biofuels production, governments need to reconsider their objectives for bioenergy production. There certainly are interesting options available in this area, especially for people who lack access to energy in rural areas. Governments need to explore what can work best for them, and develop national strategies quickly so that they remain in control of how their land is used and how the market develops. Bioenergy strategies should be integrated into a wider rural development strategy, ensure the long-term protection of their natural resource base and pay attention to the sometimes conflicting obligations governments have to face within agriculture.<sup>32</sup>

## WHAT CAN UNCTAD XII DO?

Because of its historical role and strong mandate on commodities and development, UNCTAD has a crucial contribution to make to the current debate on commodities. When they gather at Accra for UNCTAD XII, UN Member States will set UNCTAD's mandate for the next four years. Here are some proposals:

1. **Disseminate timely and relevant information on commodity market developments:**

Functioning markets require transparency, an element lacking in today's agriculture commodities trade. Uncertainty is fueling harmful dynamics on international commodity markets. The provision of relevant and timely information is fundamental for commodity producers, and UNCTAD statistics remain a reference on commodity prices and dependence. However, serious gaps in this monitoring and analysis activity result in only partial information concerning new dynamics. UNCTAD needs to dedicate more time and effort to documenting the activities of new stakeholders on commodity markets, including transnational companies, financial investors and speculators. UNCTAD's mandate to monitor the market presence of transnational corporations in commodity markets should be revived, possibly in collaboration with the FAO, when looking at agricultural commodities. Better collaboration between UNCTAD and the FAO is needed to ensure timely, easily accessible and coherent information about commodity markets.



## **2. Develop disciplines to address the negative consequences of market concentration:**

The influence of private stakeholders on global agriculture commodity markets is expanding. There is more and more evidence of their harmful effects for development: market concentration impedes fair distribution of benefits along value chains, and privately set standards constrain diversification options. Global value chains are highly untransparent. More work is needed to identify how profits are distributed along them. On the basis of the information available, UNCTAD also needs to start exploring how best to address the challenges associated with market concentration through laws and policies at both the national and international levels.

## **3. Support intergovernmental efforts to stabilize commodity prices:**

Commodity dependent countries are expressing the need to strike agreements in order to stabilize their export earnings from commodity prices. UNCTAD needs to be given a strong mandate to support these efforts. International Commodity Agreements were dismantled in the 1980s, under pressure from those who advocated that commodities needed to be left to the market's self regulating function. This approach has failed to deliver on development. UNCTAD should be encouraged to explore how developing countries can have more control on the income they make out of their exports.

## Endnotes

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