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The Food Price Rollercoaster

The year 2008 saw some of the most extreme swings in food prices in decades. Record high prices in June were followed by massive falls. Agricultural fund manager Bryan Agbadian from Allianz RCM talks about the trends shaping the market.



Bryan Agbadian, Allianz RCM

"In the near term, low grain prices could have a positive effect on food prices. But I believe long-term food prices will be at elevated levels because we still have these supply-demand imbalances. We need to build up the grain inventories."

What is an agricultural theme fund?

We look at and invest in agriculture in two different ways, which we call themes. Theme one is the supply side of agriculture. It is about the basic resources like the supply and development of land and water resources, the production of seeds and crops, chemicals, fertilizers, and farm machineries.

Theme two is the demand side. That is product processing and distribution. It includes taking the seeds and processing them for the use of food companies, but also the production of biofuels and tobacco, and the distribution of food products to the customer.

These two themes have totally different characteristics. The higher the grain price, for example, the higher the income of the farmers, which in turn gives the farmers more ability to invest in higher yields. And those investments benefit the whole supply sector. At the same time, processing companies on the demand side are negatively impacted by high grain prices, because their profit margins are being squeezed.

Early this summer food prices were at record highs. Why?

In the last decade, the former Soviet Union, China and India all increased their growth rates and thus their demand for corn, wheat, and soybeans. Demand for beef and other meats in the developing world has grown ten times faster than demand in the developed world over the past 10 years.

But it took until 2002/2003 to finally see rising food prices. At that time food inventories had fallen to such low levels that we really needed to increase supplies to bring supply and demand back into balance. Since then prices have risen, but the last three months have totally upset that development.

What changed the food market?

Things have changed 180 degrees between the month of June and the present time. In June, there were floods in the farm belt in the U.S. and the thought was that there was more need for increasing crop yields. At that time the price of corn was 7 Dollars 50 cents a bushel and the farmers were doing very well.

Right now, however, the price for corn is 3 Dollars 80 cents per bushel, half of what it was in June. So why did grain prices come down while grain stocks were still at historically low levels?

The peak prices in June were due to the perception that we were going to have less grain because of the flooding. But in July, August, and September the growing weather was very favorable and there was much more corn, wheat, and soybeans than expected. And so the prices corrected and came down. But what many people didn't anticipate was the scale of that correction. Farmers are now only at break even levels, whereas before they had money to invest.



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Feeding an expanding world population takes a heavy toll on the planet. Click on the image to learn about sustainable ways to farm (Photo: Reuters)

Will this correction benefit the millions of poor people worldwide that suffered from the peak prices?

In the near term, low grain prices could have a positive effect on food prices. But I believe long-term food prices will be at elevated levels because we still have these supply-demand imbalances. Any relief, I think, will be short lived. In the long term, we need to build up the grain inventories. But right now farmers are not investing because prices are so low. That will create even more supply-demand imbalance, which in turn will create another trend of rising grain prices.

Furthermore, despite this slowdown consumption of meat is still rising. As developing societies become wealthier, they transition from a grain-based diet to a meat-based diet. And for every one kilogram of beef produced a cow has to consume six or seven kilograms of corn.

By the end of the century there may be nine billion people on Earth. Will there be enough food for everyone?

It depends whether we can get supply and demand into balance. Let's look at the demand side: Population growth will be a little over one percent in the future. That is not enough to cause an imbalance. But we also have urbanization. About 50 percent of the world's population is now living in urban areas and that is projected to grow to 70 percent in the next 20 to 30 years. As urban consumers become wealthier they consume more meat. That causes the demand-supply imbalance.

The supply side, on the other hand, is not growing fast enough. The amount of arable land is not growing. So we really have to rely on productivity. In the developed world, we have nearly reached the limits of agricultural intensification. And diets in industrialized nations are moving towards organic foods and an organic field yields half as much as a heavily fertilized field. So growth has to happen in developing countries.

How could we achieve this growth?

If prices rose again that would make it economically feasible to increase arable land for agricultural production. Genetically modified seeds give higher crop yields. In Brazil, where they don't use genetically modified seeds, crop yields are one third of those in North America where we do use them. Fertilizers and the right balance of nutrients in the fields is another important factor.

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How do you see long-term food trends developing?

Higher food prices are going to be a fact of life. Some people say we need to bring prices back to where they were ten years ago because people need to eat. But how do you do that?

In China, they have export tariffs in place because they want to provide for their own people. But that tightens global supplies and it gives producers less incentive to produce more. In Argentina, president Fernandez put export tariffs on farmers so that they sell more locally. But that caused strikes and the farmers stopped production. It is very difficult for governments to dictate solutions.

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