RENEWABLE FUELS ASSOCIATION

Response to
Price Volatility in Food and Agricultural Markets: Policy Responses

On June 2, the U.N. Food & Agriculture Organization (FAO), Organization for Economic Cooperation and Development (OECD), and several other organizations released a report entitled *Price Volatility in Food and Agricultural Markets: Policy Responses*.[1] The report was prepared in response to a 2010 request from G20 leaders to "develop options for G20 consideration on how to better mitigate and manage the risks associated with the price volatility of food and other agriculture commodities, without distorting market behaviour, ultimately to protect the most vulnerable."

While the report offers some constructive recommendations for G20 leaders to consider when assessing possible responses to food price volatility, its suggestion that G20 governments "remove policy provisions" that support expanded biofuels production and use is terribly misguided and shortsighted. In reality, eliminating biofuels support policies would lead to higher fuel costs, which would actually aggravate food price volatility. While the report acknowledges that there are a number of complex factors driving food price volatility, the policy recommendations unduly focus on biofuels and entirely fail to suggest actions to rein in high oil prices and excessive speculation in commodity futures markets.

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Most glaringly, this report fails to recommend concrete steps that could be taken by G20 countries to combat the impact of higher energy costs on food price volatility. Remarkably, the report fails to properly address the impact of prices for oil and other energy sources on food price volatility.

- While the authors recognize that high oil prices are a driver of current higher agricultural commodity and food prices, the report fails to offer any concrete recommendations that would help G20 governments mitigate or curb the impacts of rising energy costs and non-commercial speculation in energy markets.
- Recent research suggests high oil prices play a significant role in food price inflation and volatility. A study by Texas A&M found that "The underlying force driving changes in the agricultural industry, along with the economy as a whole, is overall higher energy costs, evidenced by $100 per barrel oil."[2]

The report neglects the role of non-commercial speculation in food price volatility. The report surprisingly fails to recommend any concrete actions that would assist G20 governments in mitigating the effects of excessive speculation in commodities futures markets.

- Despite a wealth of evidence to the contrary, the authors suggest that there is no consensus on the impact of non-commercial speculative investment on food price volatility. The report

[1] Available at http://www.worldbank.org/foodcrisis/
[2] Available at http://www.afpc.tamu.edu/pubs/2/515/RR-08-01.pdf.

recommends only that, "More research is needed to clarify these questions [about the impacts of non-commercial speculation]..." and suggests that little is known "…about whether regulatory responses are needed and the nature and scale of those responses."

- These conclusions are at odds with the results of a 2010 World Bank study examining the causes of the 2007/08 food price spike. World Bank found "…the effect of biofuels on food prices has not been as large as originally thought, but that the use of commodities by financial investors (the so-called "financialization of commodities") may have been partly responsible for the 2007/08 spike."[3]
- Further, Texas A&M University researchers recently found that, "Speculative fund activities in futures markets have led to more money in the markets and more volatility. Increased price volatility has encouraged wider trading limits. The end result has been the loss of the ability to use futures markets for price risk management due to the inability to finance margin requirements."[4]

The report's recommendations to remove policies that support biofuels production and use are misguided and shortsighted. The report broadly suggests food price volatility would be helped by eliminating all policy provisions that "subsidize (or mandate) biofuels production or consumption." This recommendation is at odds with the findings of recent studies, including some conducted by the organizations responsible for the June 2 report. Further, it is inconsistent that the authors would suggest eliminating only biofuels support programs, while neglecting to address subsidies for fossil fuel production and use.

- Recent studies suggest that robust bioenergy industries can enhance food security in developing nations. Information released by the U.N. FAO in May 2011 stated that, "…investment in bioenergy could spark much-needed investment in agricultural and transport infrastructure in rural areas and, by creating jobs and boosting household incomes, could alleviate poverty and food security."[5]
- Also in May, officials involved in the Global Bioenergy Partnership (which includes many of the organizations responsible for the June 2 report) stated that "Modern bioenergy encompasses many technologies that have the potential to not only promote sustainable development, but also help meet two important needs in the developing world by enhancing food and energy security."[6]
- Biofuels indirectly exert downward pressure on food prices by reducing energy prices. A May 2011 study by the Center for Agricultural and Rural Development found that the growth in ethanol production reduced U.S. gasoline prices by an average of $0.25, or 16%, over the entire decade of 2000-2010.[7] Similarly, an analysis by Merrill Lynch found that, "Biofuels are making up a huge portion of oil supply growth…" and, "On a global scale, biofuels are now the single largest contributor to world oil supply growth. We estimate that

[3] Baffes and Haniotis (World Bank Development Prospects Group). July 2010. Placing the 2006/08 Commodity Price Boom into Perspective. Polic Research Working Paper 5371.
[4] Available at http://www.afpc.tamu.edu/pubs/2/515/RR-08-01.pdf
[5] Press release available at FAO web site here.
[6] Press release available at GBEP web site here.
[7] Available at http://www.card.iastate.edu/publications/synopsis.aspx?id=1160

retail gasoline prices would be $21/bbl higher, on average, without the incremental biofuel supply."[8]

- Recent research suggests that biofuels have only a minor impact on agriculture commodity prices, and thus exert negligible influence on food prices. According to a 2010 report by United Kingdom government researchers, "Available evidence suggests that biofuels had a relatively small contribution to the 2008 spike in agricultural commodity prices."[9]
- The report fails to discuss the contribution of biofuel co-products to the global feed and food supply. For example, every metric ton of grain processed for ethanol results in the production of both fuel and roughly 750 pounds of animal feed in the form of "distillers grains." More than 45 million metric tons of this high-protein animal feed was produced and consumed in 2010.
- The report recommends that G20 countries should develop "contingency plans" to adjust biofuels policies when "global markets are under pressure and food supplies are endangered." In an annex to the report, the authors acknowledge that some major biofuel producing countries, including the U.S., already have such contingency plans. The report states that the U.S. and some other countries "…have built flexibility into their legislative or regulatory framework." Indeed, the Energy Independence and Security Act of 2007 that expanded the RFS contains a provision allowing the EPA Administrator to waive or reduce biofuels requirements if they are determined to be causing economic harm.

The report is right to highlight the contributions to food price volatility of underinvestment in agricultural productivity, export restrictions, commodity and food wastage, lack of market information and preparedness, high oil prices, monetary policy and currency fluctuations, weather-related crop losses, climate change, and other factors. The report correctly recognizes that food price volatility has many complex and inter-related causes. However, the authors unfortunately focus disproportionately on biofuels and fall short in providing actionable recommendations to address many of these more serious factors.

Because the report is incomplete and unbalanced, we encourage G20 leaders to reject its findings and request a revision that takes into account the available literature on the impact of biofuels on world food prices, as well as comments from stakeholders.

[8] Blanch, F. (2008). *Biofuels driving global oil supply growth.* Merrill Lynch. http://www.europabio.org/Biofuels%20reports/MerrillLynchJune2008.pdf
[9] Available at http://archive.defra.gov.uk/foodfarm/food/pdf/ag-price-annex%205.pdf