



Philequity Corner (April 25, 2022)
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Food Shortage

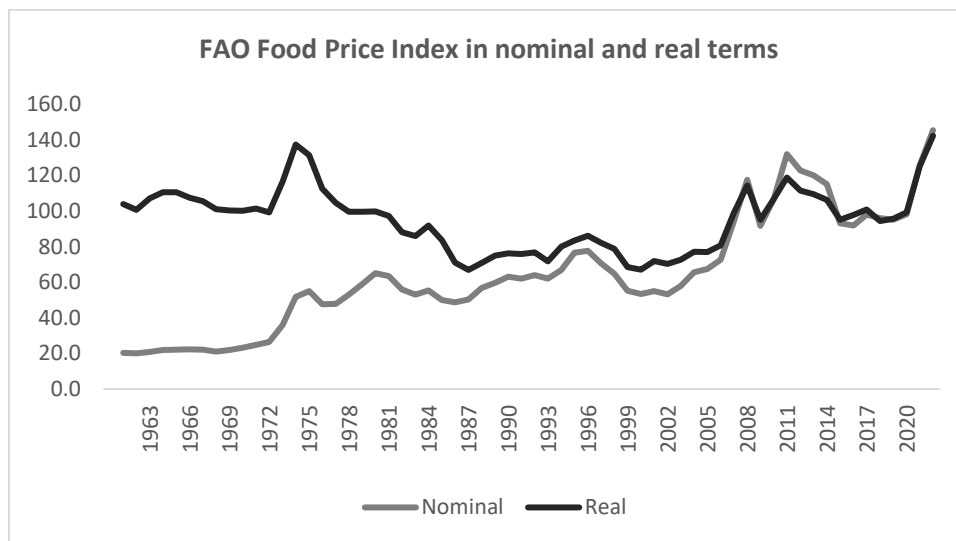
A global food shortage is looming. Driven by surging energy costs, supply disruptions, and escalating war between two of the world’s major breadbaskets, food prices worldwide are surging to record levels, compounding food security concerns and making access to food more difficult.

In Peru, farmers are protesting a shortage of fertilizers estimated to decrease corn, potato, and rice production by 40%. In Sri Lanka, people are lining up at government-run “fair-price” shops to buy essential commodities such as rice, dal, milk, and flour because prices in private groceries are three to four times higher. In the meantime, Sri Lanka elected to default on its debt to pay for imports of essential goods like food, fuel, and medicines.

Even the fast-food chain McDonald’s has suffered from shipment delays and a shortage of potatoes used to make its famous French fries. The company has been rationing its fries in countries like Japan, Taiwan, Malaysia, and Indonesia since late 2021. Last week, McDonald’s Philippines announced it would only be serving regular size fries, halting the sales of its large-sized portions.

Food prices reach all-time highs

According to the UN Food and Agriculture Organization (FAO), food prices today are higher than during the Arab Spring uprising in the early 2010s. As a result, food prices are now at new all-time highs in nominal and real terms, surpassing even the prices reached during the 1973-74 Arab oil embargo. The basket of food items that make up the FAO Food Price Index shows year-on-year price increases of +37% for cereals, +23.6% for dairy products, +56% for vegetable oils, +22.6% for sugar, and +19% for meat.



Indonesia bans palm oil exports

Last Friday, Indonesia – the world’s top palm oil producer – announced plans to ban exports of the most widely used vegetable oil. Indonesia’s finance minister said that this would hurt other countries but is necessary to ensure that cooking oil in the domestic market remains abundant and affordable. Palm oil is also used in cakes, chocolates, margarine, and biscuits, as well as cosmetics, detergents, and biofuels. This will worsen the vegetable oil shortage and raise food prices even more.

Ukraine – breadbasket of Europe

Even before the war, agricultural commodities climbed higher due to supply-chain disruptions and high energy costs. However, Russia's invasion of Ukraine exacerbated the pre-existing price and global food supply pressures. UN FAO estimates that 1/3 of Ukraine's farmlands will not be harvested or planted this year as the war escalates.

Ukraine is among the world's top agricultural producers and is known as the breadbasket of Europe. It accounts for 9% of the world's wheat, 12% of maize and barley, and 50% sunflower oil exports. Moreover, the ravaged Ukrainian farmlands and damaged infrastructure like highways, rail systems, bridges, and ports will make exporting crops more difficult.

Record high fertilizer prices

Another major reason for the food shortage is record high fertilizer prices. According to the US Department of Agriculture, fertilizer constitutes around 36% of a farmer's operating costs for corn and 35% for wheat. Note that Russia and Belarus are top exporters of fertilizers, accounting for 37% of global potassium exports, 14% phosphate, and 16.5% of nitrogen exports. However, Western sanctions have made Russian and Belarusian fertilizers expensive and harder to import. As a result, CRU Group's fertilizer index has recently reached a new record high at 390, well above the 360 record-high set in 2008 and 4x the level it was at the beginning of 2021.

Rising production & transportation costs

The increase in energy prices and transportation costs also drives food prices higher. One-third of food costs are energy-related, while two-thirds of the cost of nitrogen fertilizers comes from gas. Fuel also accounts for around 30% of the expenses for aviation companies and 50% of the costs for shipping companies. The rerouting of trading in Europe plus the high war-risk premium also increased transportation costs for cargo ships and tankers transiting the Black Sea.

China lockdowns

Bloomberg News reported that China's oil demand would fall 20% in April, the most since the Wuhan lockdown. The lockdown in major cities reduces fuel consumption and lessens food demand. However, the lockdowns disrupted the Chinese planting season as villages were sealed off access due to the Covid curbs. As a result, a third of the farmers in the Jilin, Liaoning, and Heilongjiang provinces, which account for 20% of China's grain production, cannot get fertilizer and seeds kept inside in cargo holds in Shanghai.

Rice production set to plunge 10%

Unlike wheat and corn, which have seen supplies cut off from one of the world's major breadbaskets, the global supply of rice has been relatively stable. However, the International Rice Research Institute (IRRI) warned that harvests could plunge 10% next season as fertilizer supply remains curtailed. Faced with high input prices, farmers will use less fertilizer to save costs, reducing future rice yields and further complicating the food supply shock on the global market.

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