

Global Food Prices Moving Down, Pointing Up

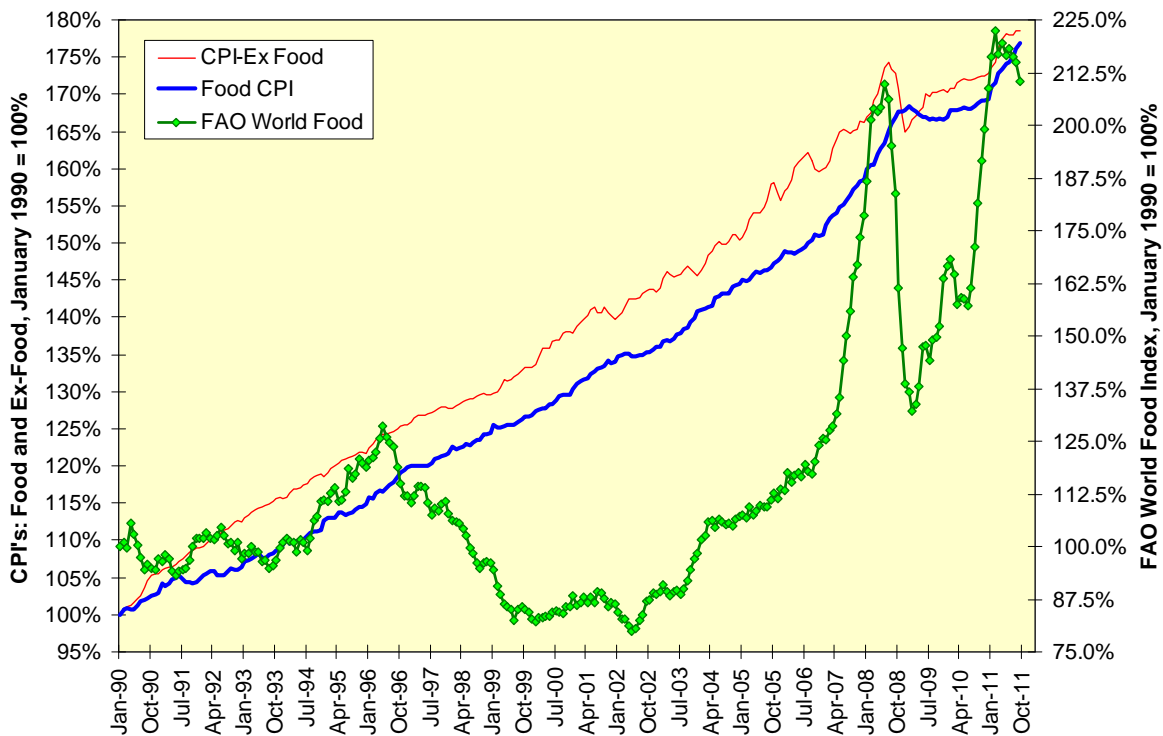
As we enter that time of year when most Americans really start to strap on the feedbags, let's revisit a topic from [January](#), the U.N. Food & Agriculture Organization's Food Price index. That index had just hit a nominal high, and a string of natural disasters such as floods in Australia, monsoon failures in India and droughts in the former Soviet Union (this is starting to read like a high school social studies paper) was combining with the manmade disaster of QE2 to make the prospects gloomy for consumers.

Of course, the FAO index peaked one month later. However, according to a former World Bank agricultural expert whose presentation I just attended, no one should confuse the short-term respite with longer-term trends. While he acknowledged the Malthusian argument has been wrong for more than two centuries and was still very optimistic about developments in both plant genetics and in cross-breeding for traits such as drought resistance, he was less optimistic about the ability to bring marginal new lands into production and to develop the transportation and storage infrastructure needed for an agricultural environment.

Agricultural inputs are high-volume, low-value commodities such as fertilizer and water, and agricultural outputs are much the same. U.S. agricultural markets developed first along natural rivers, then along artificial rivers and then along railways. Much of sub-Saharan Africa is bereft of navigable waterways, rail and port facilities are lacking and much of the external financing by China in particular is being directed to mining roads that can serve farms, but only at a high operating cost. And never forget the problems of market subsidies, taxes, price controls and outright corruption. Finally, if you open new farmland, who is going to tend it? Farming is a lifestyle, not a job, and just as Mexican immigrants are moving into the U.S. farm belt, expect Chinese immigrants to move into marginal lands in Africa and South America. The, um, cultural adjustments here will be fascinating.

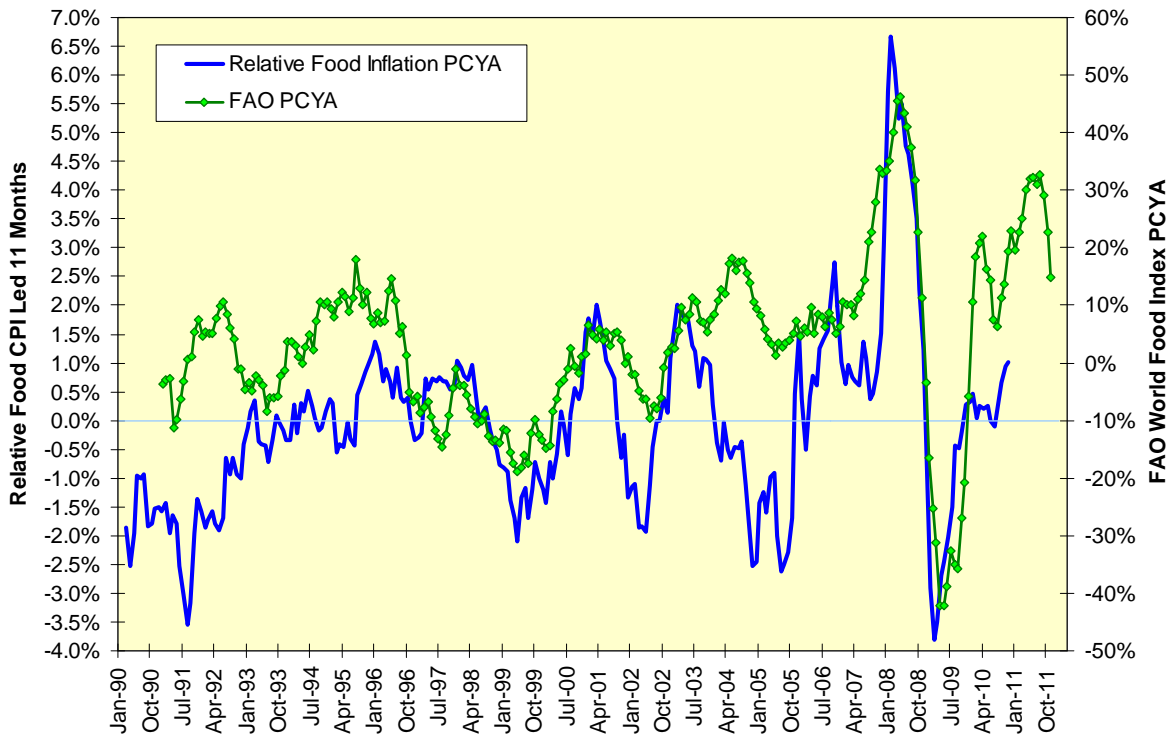
Let's update the FAO food price index and its relationship to U.S. consumer prices. On the surface, neither the food CPI nor the CPI ex-food (I am so proud to live in a country capable of excluding food from household budgets) appears to have much connection to the FAO index.

FAO World Food Index And U.S. CPI Measures



However, if we restate the data above as year-over-year percentage changes, we see the FAO index' rate of change leads that of relative food inflation by eleven months on average. That lead-time embeds growth in the food CPI relative to the CPI ex-food through the first quarter of 2012.

FAO World Food Index Leads U.S. Relative Food Price Inflation



Such an expected lead-time is independent of any developments that may occur in the Southern Hemisphere crop year. If events such as the recent flooding in Thailand, which has a major impact on rice prices, arise, expect food prices to rise further and faster in the U.S.

Finally, even though the logic is [demonstrably wrong](#), the public has linked monetary excess with higher food prices. If the Federal Reserve decides to start spraying money hither and yon one more time and these actions coincide with an upturn in food prices, watch for some real political pushback. It will be justified even if it remains inarticulate.