

Web Commentary

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The Food Price Crisis in the Arab Countries: Short Term Responses to a Lasting Challenge

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Summary

The response of Arab governments to the unfolding crisis caused by escalating food prices has been extremely varied according to the different countries. Despite responses such as bread subsidies, increasing public sector wages, and tax reductions, there have been no real policy shifts addressing the core problems of the agricultural sector and excessive consumption of energy, especially in the non-oil exporting countries. Arab governments need to revisit agricultural policies by providing incentives and promoting efficient techniques to increase domestic production and create jobs in rural areas. At the same time, they must expand social safety nets to protect vulnerable groups that live on limited resources. Internationally, developed countries must reconsider their policies regarding food production and subsidies. Many developing countries also need assistance in managing public food procurement and need to develop purchasing mechanisms to limit the impact of rapid price fluctuations in commodity markets.

Skyrocketing food prices in 2007 have made basic staples like rice, wheat, and corn unaffordable to lower income groups throughout the world. Arab countries, which import most of their food, found themselves in difficult circumstances with limited options in the short run.

Arab countries can be grouped in two categories: the GCC oil producing countries, which have relatively small populations and ample revenue, thus have room to adjust to the inflation in food prices; and the populous, non-oil-exporting countries in which a significant number of people live below or just at the poverty line. These impoverished populations have little space to adjust their expenditures, particularly since a major portion of their household budget is allocated to basic commodities, of which food comprises the largest share. The lack of maneuverability means that the poor are often forced to resort to non-economic methods to protect themselves. It is within this context

that the riots that erupted in the streets of several Arab countries such as Egypt, Morocco, and Yemen can be understood.

In the face of this crisis, how have Arab governments responded? What are the implications of their responses in the medium and long terms? And what alternative policies can be recommended?

The food price crisis is a global phenomenon with several commonly accepted drivers. According to the IMF 2008 *World Economic Outlook*, the diversion of food crops to the production of biofuels is responsible for almost half of the increase in the prices of major food crops in 2006–2007. Speculative behavior in commodity markets also contributed to the crisis. After the real estate bubble burst in mid-2007, investment and hedge funds moved into commodity markets in order to compensate for their losses in the property market, driving prices up as a result. Moreover, transport costs rose dramatically as world oil prices increased by about 90 percent over the last 12 months, from \$64 in May 2007 to more than \$135 in May 2008. Rising world oil prices also increased the cost of agricultural inputs for farmers. Other factors affecting food prices include rising living standards in China, India, and other developing countries, which increased demand for livestock and feedstock; rapid depreciation of the dollar; water depletion due to climate change; and poor weather that reduces agricultural output in many regions.

Arab economies must deal with these global realities but also have problems of their own:

- An inefficient agricultural sector with serious problems of finance and market access as well as inefficient farming practices and weak training and education. These problems are the result of misguided agricultural policies that offered distorted incentives to unskilled farmers.
- Declining output in the agricultural sector due to massive rural–urban migration and the neglect of agricultural and rural development.
- An unfavorable environment, characterized by water scarcity and minimal arable land. According to the World Bank, the Middle East and North Africa (MENA) region has 5 percent of the world’s population but less than 1 percent of its renewable freshwater resources. Of the 20 countries worldwide with internal renewable fresh water availability below 1000 cubic meters per capita, fifteen are in MENA.
- An inefficient energy sector with one of the world’s highest ratios of energy consumption to national output, even when compared to OECD countries. This addiction to cheap energy makes the agricultural sector in most non-exporting Arab Countries non-competitive.
- A highly concentrated food market with a few producers or traders controlling a large share of the market and hence prices.

Trade liberalization programs in many Arab countries have led to the further decline of their agricultural sectors. The removal of tariff barriers transformed previously net

agricultural exporters such as Egypt and Morocco into net importers, particularly of heavily subsidized wheat produced mainly in the United States.

The response of Arab countries has varied considerably.

The six GCC countries, Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates (UAE) produce about 23 percent of the world's oil and control more than 40 percent of the world's oil reserves. Rising oil prices since 2003 have allowed the GCC to mitigate the social impact of rising food prices and to minimize the impact of rising inflation and the depreciation of their currencies, which are pegged to the U.S. dollar, by almost doubling wages for civil servants. They also kept fuel prices stable domestically and increased public spending.

However, the GCC countries *are* suffering from significant inflation. In Oman, Qatar, and the UAE, inflation is already in the double digits. It is close to 10 percent in Kuwait and Saudi Arabia, leaving only Bahrain with a modest rate of inflation.

Administrative measures by governments can do little to curb inflation especially in non-tradable sectors such as property markets or imported food. Additionally, the cost of foreign labor, which these GCC countries heavily rely on, has increased to keep pace with inflation, and this is further fueling the inflation cycle.

In most non-oil-exporting countries, governments have also increased wages for public sector employees, and have urged liberalized private sectors to do the same. Some governments have also tried to target support more directly on the poor through direct cash transfer or ration cards, replacing price subsidies on essential commodities that helped all consumers. In general, however, non-oil producers have found it more difficult to mitigate the impact of price increases, and many have experienced unrest.

In Egypt, for example, 32 out of the country's 80 million inhabitants live on less than \$2 a day. The five-fold rise in bread prices has led to serious food riots that claimed eleven lives in April 2008 after clashes with the army. The government response included allocating \$2.5 billion of its new budget for bread subsidies, imposing a ban on rice exports, and ordering the army to bake and distribute bread to the poor. Public sector wages were also increased by 30 percent.

In Jordan the cost of staple foods increased by 60 percent in a year. However, the country did not see a repeat of the food riots of 1996 but rather more peaceful protests. In early 2008 the government removed fuel subsidies as a response to serious budget constraints but counterbalanced this with a rise in public sector wages, removing taxes on basic goods, and strengthening safety nets for the poor.

In Morocco violent protests over the cost of bread prompted the government to annul a 30 percent price hike. Violent clashes between police and rioters led to arrests and fears of a repeat of the 1981 Casablanca bread riots.

In Algeria, a 15 percent salary increase for civil servants was introduced in response to a doubling of the price of cooking oil, sugar, and flour. Algeria has not been able to use its oil and gas revenues to mitigate this crisis as most of those revenues are being used to service foreign debt.

Yemen witnessed violent food riots after the prices of wheat doubled and the price of rice and cooking oil increased by a fifth. It is estimated that after record inflation, along with rising food prices, national poverty might increase by a dangerous 6 percent.¹

In Lebanon food prices rose by 30 percent in the last quarter, while in Syria they rose by 20 percent. Syria responded by increasing public sector wages by 25 percent, while in Lebanon the minimum wage was raised from US\$200 to \$330.

Despite some outbreaks of violence, thus far governments in the region have managed to contain popular frustration by increasing wages and rationing subsidies. Protests have not been as severe as they were in the 1980s or 1990s for several reasons. First, government responses, while not tackling the core causes of the food price rises, have been able to provide limited and temporary relief such as tax reduction, improvement of safety nets, and subsidies for staples. Second, the public sector continues to employ large numbers of the work force, thus increasing public sector wages has helped many families in dealing with the effects of rising prices. This dependence on the state has also made many people hesitant to challenge the state that provides their main source of income. Third, as the food price crisis is perceived as a global crisis, people are less inclined to blame their own governments for these problems.

The measures taken by Arab governments, especially in non-oil producing countries, are not sustainable. This is partly because of budget constraints as most of these countries are running serious budget deficits. Moreover, public spending is rigid in nature in these countries—it is dominated by wages and salaries, defense and security spending, and interest payments on public debt. In order to sustain increased subsidies and better safety nets, these countries would have to reduce capital expenditures, i.e., spending on utilities, roads, transportation, and infrastructure. In turn, these reductions would have negative implications for the rest of the economy. Moreover, this is not a time when governments can raise taxes to increase domestic revenues.

In the short run, there is no quick fix for the crisis created by rising food prices. Particularly in non-oil producing countries, there remains a real danger that people will take to the streets in increasing numbers when they see their livelihoods threatened. And in the Arab countries, the consequences of discontent and anger can easily acquire a geopolitical angle.

In the medium and long run, Arab governments need to shift their policies to address the core problems of the agricultural sector and excessive energy consumption. At the national level, each country needs to revisit its agricultural policies by providing incentives such as tax breaks, easy loans, and introducing efficient techniques that increase domestic production and create jobs in rural areas. In parallel, these countries

must further expand social safety nets to protect vulnerable groups living on limited resources. Furthermore, there is a need to enhance market forces to break existing monopolies by strengthening competition authorities in these countries to facilitate the creation of an effective consumer association.

Internationally, developed countries must reconsider their policies regarding food production and subsidies. Promoting biofuels seems unreasonable at this time and the recent “food summit” in Rome failed to reach an agreement on this issue. Developed countries should focus on transferring better agricultural techniques to developing countries rather than relying on cash assistance. In addition, measures to limit financial speculation in key commodity markets would also help keep food prices lower. Many developing countries also need assistance in managing public food procurement and need to develop purchasing mechanisms by adopting best international practices to limit the impact of rapid price fluctuations in commodity markets.

Note

¹ Anuradha Mittal, *Food Price Crisis: A Wake Up Call for Food Sovereignty* (The Oakland Institute, 2008).

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