The Political Economy of Food Price Policy in ETHIOPIA

Policy Brief No. 3

March 2013

ASSEFA ADMASSIE

Until 2004, food price inflation was not a serious challenge in Ethiopia except for price fluctuations during drought years. Around 2004, however, Ethiopia began to experience high rates of food inflation as a result of changes in factors influencing demand and supply. The price of major staples such as wheat and maize doubled or tripled, and the average inflation for food and cereals was 41 percent and 58 percent during 2007 and 2008, respectively. In mid-2008 annual food price inflation reached a record rate of 61.1 percent.

Though developments in international food markets had some impact, price transmission was low and the high food price inflation was caused mostly by domestic factors. Aggregate demand for food was growing, perhaps because of increased private consumption, remittances, and investments in poverty-oriented sectors. Another factor was the improved purchasing power of farmers due to the injections of cash into the local economy through microcredit services and the country's Productive Safety Net Program. But the growth in aggregate demand was not matched by expected supply increases. Also contributing to the increase in food prices was an expansionary monetary policy, driven by the need to meet surging demand for credit for investment financing, pay the rising cost of imported intermediate inputs, and fill the gap created by the withdrawal of donor support after the controversial 2005 national election.

Ethiopian policy makers strongly believed that food prices could not be left to market forces alone and initiated several policy measures in response to the rising food prices.

The Ethiopian government procured grain from the international market and distributed it at subsidized prices to the urban poor through a food-rationing program and through sales to flour mills at subsidized prices. In addition, it banned cereal exports, reduced import tariffs, raised the reserve requirement of commercial banks to restrict the supply of monetary aggregates in the economy, raised the salaries of public employees, and released grain stocks.

Other measures included production subsidies, in the form of subsidized input delivery, importation of certified improved seeds, and the provision of incentives for long-term agricultural investment. The government expanded social safety net programs for food-insecure households in rural areas, adopted price controls, and launched media campaigns to encourage the public to closely monitor the behaviour of grain traders. It increased support for extension services and research and development of agricultural technology and irrigation, and it established an Agricultural Transformation Agency to improve agricultural productivity and bring about agricultural transformation. The Ethiopian Commodity Exchange was established to facilitate long-term legally binding contracts between farmers and traders and thereby

Assefa Admassie, Principal Research Fellow at the Ethiopian Economics Association and adjunct Associate Professor at the Addis Ababa University, Department of Economics, Addis Ababa, Ethiopia

The author prepared this brief as a member of a research network on the Political Economy of Food Price Policy coordinated by Cornell University, UNU-WIDER, and the University of Copenhagen.
The complete paper is available at: http://www.wider.unu.edu/research/current-programme/en_GB/Political-Economy-of-Food/
The policy briefs can be found at: http://www.foodpolicy.dyson.cornell.edu
The project director is Per Pinstrup-Andersen who may be contacted at pp94@cornell.edu

reduce and manage risk. Some of these measures significantly reduced the lending capacity of commercial banks and constrained imports because most of the short-term loans from private banks were used to finance imports and serious shortages of staple grains.

The Ethiopian government took these measures mainly to address the economic, human, and political costs of food price instability.

The government had long claimed that achieving sustained economic growth by maintaining macroeconomic stability was one of its central objectives. Accordingly, it sought to slow the growth of the money supply in order to maintain a level of inflation that would not be detrimental to growth. It also took measures to prevent social unrest. The 2007–2008 food price crisis occurred just two years after the 2005 national election, which was characterized by serious uncertainties and contributed to the upward pressure on prices when some farmers were reluctant to sell their products.

There were also concerns about the implications of the food price rise on the food security of the most vulnerable urban households and net-buying farm households. The importation and distribution of food grains at subsidized prices to the poor did indeed reduce the potential negative impact of the food price increase on the poorest segment of the population. The interventions also contributed to macroeconomic stability, maintained the trend in poverty reduction, and improved the balance of payments position from a situation of 1 month of imports to about 2.5 months of imports in 2009.

The role of stakeholders outside government in the policy decisions has been limited, and most of the policy measures have been initiated and driven by the government.

Although there was some pressure by some interest groups, both domestic and external, to take certain policy steps, most of the measures were initiated and implemented by the executive branch of the government. Despite Ethiopia's multiparty system of governance, persistent appeals by opposition members of Parliament for alternative policies is believed to have had little or no impact on the design and adoption of the policy measures. There were several media reports on the high food prices in both the public and private media, but it is not clear to what extent they influenced the policy decisions. Similarly, there has been little meaningful activity within the private sector and civil society organizations. Apart from individual complaints, there has been no major organized public riot or protest.

Since Ethiopia is heavily dependent on donor support, some have argued that the government was forced to cut back on investment projects, or at least to delay them, in response to advice from international organizations such as the World Bank and the International Monetary Fund. In addition, policy makers may have considered recommendations forwarded by international research organizations such as the International Food Policy Research Institute, but there has been no explicit reference to such studies, and Ethiopian policy makers have often claimed that they were not influenced by outside sources.

THE POLITICAL ECONOMY OF FOOD PRICE POLICY

This material is based on research funded by the coordinating organizations and a grant from the Bill & Melinda Gates Foundation. The findings and conclusions contained within are those of the authors and do not necessarily reflect positions or policies of the Bill & Melinda Gates Foundation.

UNITED NATIONS UNIVERSITY

UNU-WIDER

World Institute for Development Economics Research

Cornell University

UNIVERSITY OF COPENHAGEN