Are retailers and food producers exploiting South Africans through higher-than-warranted food prices?

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The Competition Commission's recent report on agriculture and food markets dominated the conversations in the industry groupings last week. Therefore, we thought it was necessary to outline some shortcomings of the report in an essay published in the Sunday Times this past weekend. This morning, we jointly present our arguments in the Sunday Times essay with Professor Johann Kirsten of Stellenbosch University's Department of Agricultural Economics.

We live in a time of higher food prices, part of the global polycrisis triggered by the pandemic and Russia's war on Ukraine, which caused seizures in supply chains and pushed up energy and food prices. In short, this is not unique to South Africa.

This is also the wrong time to cry wolf, as the Competition Commission recently did in its Essential Food Price Monitoring Report. If you raise a false alarm when none is warranted, it undercuts your credibility when danger is afoot. Let us consider the real factors that have influenced recent food prices.

The drought in South America in the 2019/20 season and the growing demand for grains and oilseeds in China were the primary drivers of global prices. China was on a path to rebuild its pork industry, which African swine fever devastated, requiring increased volumes of grains and oilseeds. China's growing demand had a consequential impact on global grain prices because of its share size of imports. For example, the country imports about 60% of globally traded soybeans.

As Covid-19 spread in early 2020, several major grain producers, such as India, Kazakhstan and Vietnam, worsened the increase in global prices by temporarily banning exports. As this unfolded, shipping costs soared, contributing to already elevated global grain prices. Throughout this period, drought in South America didn't stop, weighing on global supplies. This matters because Brazil and Argentina account for half of global soybean production and about 15% of global maize production. Thus, when these countries face drought, the impact is visible in global grain supplies and prices. In sum, a combination of trade policy actions by other countries, logistics and weather conditions placed an upward pressure on food prices.

These are all-important fundamentals that challenge food supplies, further worsened by the Russia-Ukraine war. Russia and Ukraine are substantial players in the grains and oilseeds market. The former produces about 10% of global wheat, while Ukraine accounts for 4%. This is nearly the size of the EU's total wheat production. Wheat is for domestic consumption as well as export markets. Together the two countries account for a quarter of global wheat exports. Moreover, Russia and Ukraine are notable players in maize, responsible for 4% of production combined. However, their contribution is even more significant in exports, accounting for an average of 14%. Both countries are also among the leading producers and exporters of sunflower oil. Pre-war, Ukraine's global exports of the product accounted for 40%, with Russia accounting for 18%. Thus, the start of the war led to a surge in grains and oilseeds prices for much of 2022. As the war intensified, the drought in South America continued.

During this period, there were also sharp increases in energy prices because of Russia's major contribution to global energy supplies, which was suddenly disrupted. These events affected all countries, and food price inflation suddenly became a worldwide topic.

Linkages to South Africa

South Africa, while a net exporter of agricultural products, was not insulated from the price shock, even with its large domestic harvests. This underlines the interconnectedness of global food supplies.

Some may argue that governments should have placed export bans to limit the surge in domestic grains prices. But such policy prescriptions never work. Notably, in the South African case, one must remember that agriculture is highly exposed to global markets given that about half of output by value is exports and that many inputs into the farming need to be imported.

As a country, we import more than 80% of our annual fertiliser usage and 98% of agrochemicals, fuel and equipment. We had limited control over these prices, which increased pre-war and accelerated further when it started. Before the war, China, which accounts for about 12% of global fertiliser exports, limited these to focus on its domestic market. When the war started, Russia, which accounts for 14% of global fertiliser exports, was suddenly in chaos.

As such, if policymakers considered limiting South Africa's grain exports to protect the country from global challenges, the results could be a reduction in competitiveness in maize production and, ultimately, lower plantings and output as farmers would opt for other profitable crops. The long-term effects of such an approach would be higher prices, exactly the opposite of what those policymakers would have aimed to control.

In the past year or so, food producers and processors had to deal with higher agricultural commodity prices and process such commodities further to produce the food products we see on shelves. The activities between producer (or importing country) and retailer do not happen without costs. The food value chain first depends on expansive logistical systems and networks, while processing involves labour, energy, packaging and finance costs, among others. Once the food is processed it must be distributed to thousands of retail outlets, which also bear these costs. We all know what happened to fuel prices and the interest rate in South Africa. On top of that, we can add inflation-related wage increases and the dramatic costs of load-shedding and crime.

It is, therefore, no wonder that food value chain costs soared, amplifying the initial increase in commodity prices. A lot of these cost increases are self-inflicted through state failure regarding energy, crime and local government collapse. We should think about the terrible conditions in which role players in the food value chain have to do business in South Africa today.

If food processors and retailers accounted for all these cost increases across the value chain, consumers would face a much sharper increase in prices. But this was not the case in South Africa. Food prices increased at a moderate pace, having averaged 9,5% in 2022, compared with 6,5% year on year in 2021 and 4,8% in 2020. Countries such as the US, Kenya and Brazil, as well as those in the EU, saw much higher consumer food price inflation rates than South Africa, though some had decent agricultural production conditions.

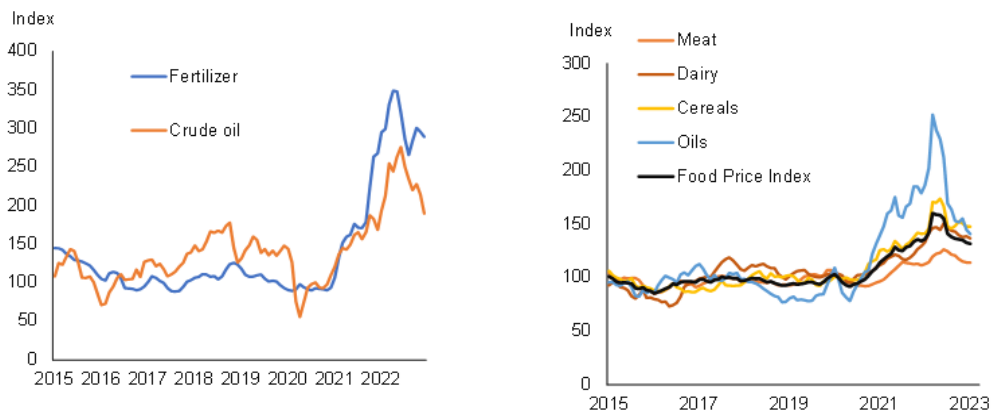
This meant food processors and retailers, if anything, absorbed the costs and didn't pass them fully on to the consumer. Their strategy is understandable, considering this country's economic environment and unemployment. With this in mind, we find the Competition Commission's comments puzzling and irresponsible. It suggested various food price increases in the past few months were "unjustified", insinuating someone in the value chain is taking advantage of South African consumers. This is an unfortunate mischaracterisation of reality. If anything, one could argue that food processors and retailers had to apply smart pricing strategies to benefit the consumer while sustaining their businesses.

A regulating body such as the Competition Commission should be mindful of the critical role it plays in society and be more thoughtful in its research and statements, especially on politically and socially charged food security issues.

The drivers of food prices are evident and a global challenge. In the coming months, as the country faces rolling blackouts, which add to the dynamics, food prices are likely to remain elevated, softening in the second half of the year. There is also a lag (of anything between three and nine months) between farm and retail prices, which some researchers tend to ignore.

Public anxiety about high food prices does not need to be further aggravated. Reporting on such must be done responsibly and with great care.

Exhibit 1: Global agriculture input prices are starting to soften, but there is a lag before all this appears through some food products at the retail level



Source: FAO, IMF and Agbiz Research