



Commodity Dependence, Market Volatility & Global Crises

IV United Nations Conference on Least Developed Countries

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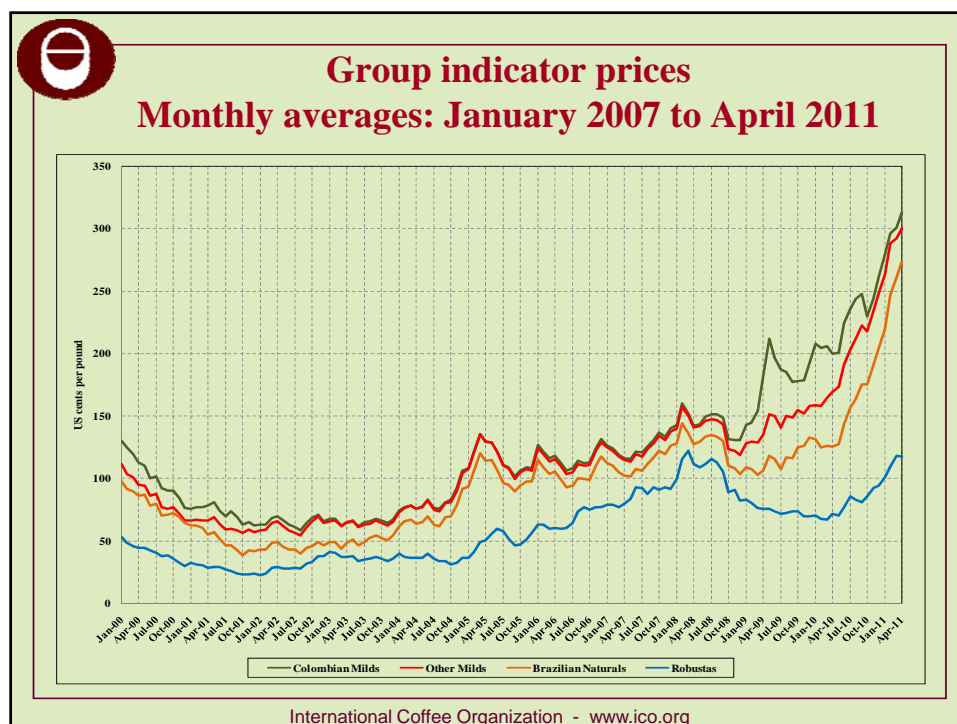
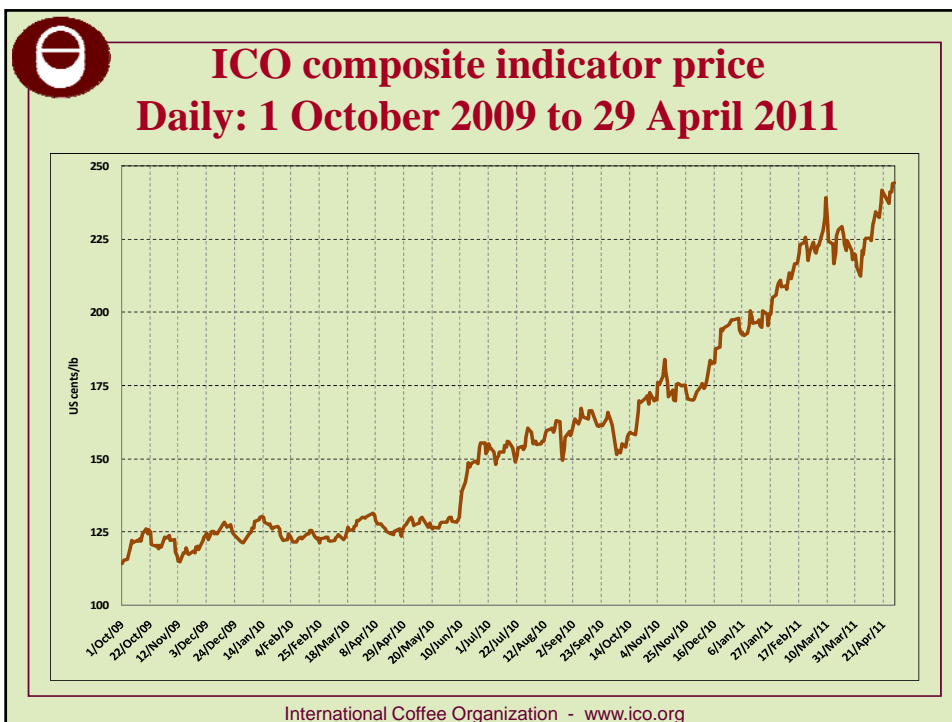
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SUMMARY

- 1. Drivers of Volatility**
- 2. Effects of Volatility**
 - Export earnings
 - Producer income
- 3. The Role of International Commodity Bodies**

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Volatility: Concept & Definition

- Generally speaking, volatility refers to the tendency for prices to change in an unforeseen manner over time, usually in response to new information or to an external impact that can affect the situation of fundamental market factors for the underlying commodity or stock.
- Volatility measures the degree of increase or decrease in prices in the short term. It is not defined in terms of price levels, but their degree of variation.

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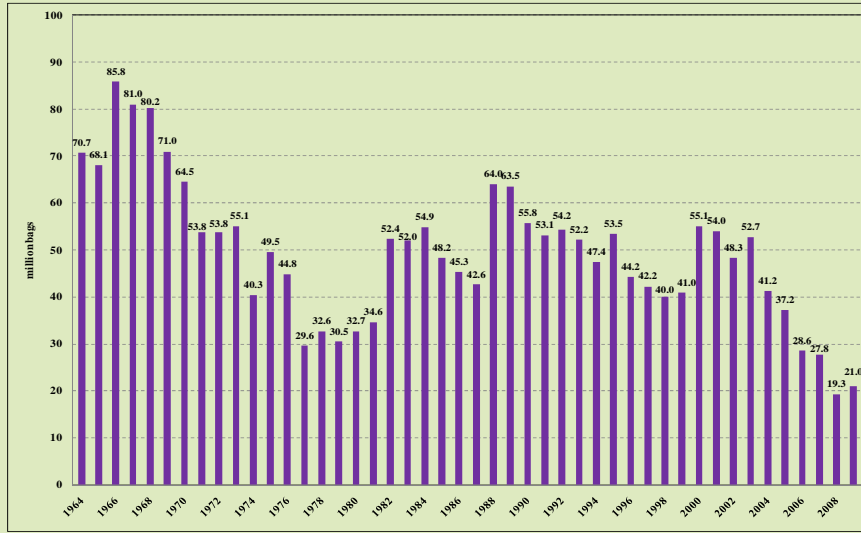
Volatility: Causes

- Levels of stocks
- Sudden changes in the supply/demand balance
- Inadequate information about fundamental factors

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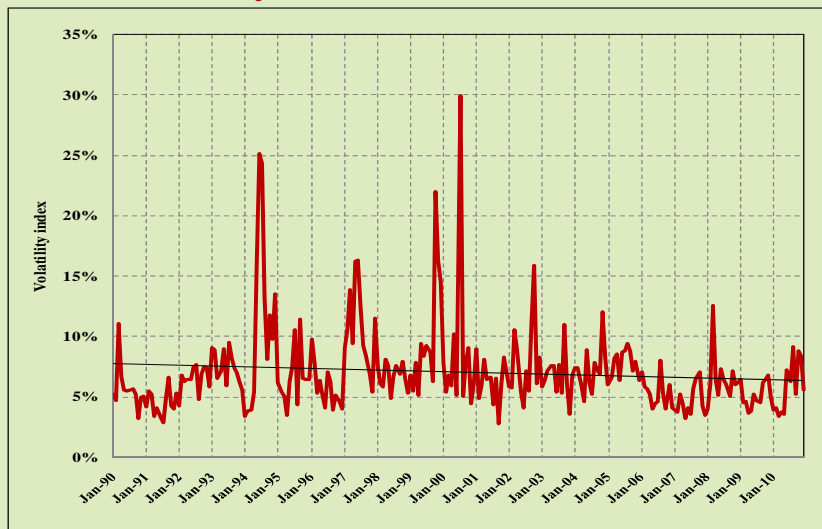
Opening stocks in exporting countries Crop years 1964 to 2010



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Volatility index January 1990 to December 2010



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Study on “Coffee price volatility” ICC-103-7 (September 2009)

Conclusions:

- Volatility levels have changed over time
- Trend towards reduced volatility despite emergence of occasional peaks as response to exogenous impacts
- Reduction in supply side shocks in last two decades

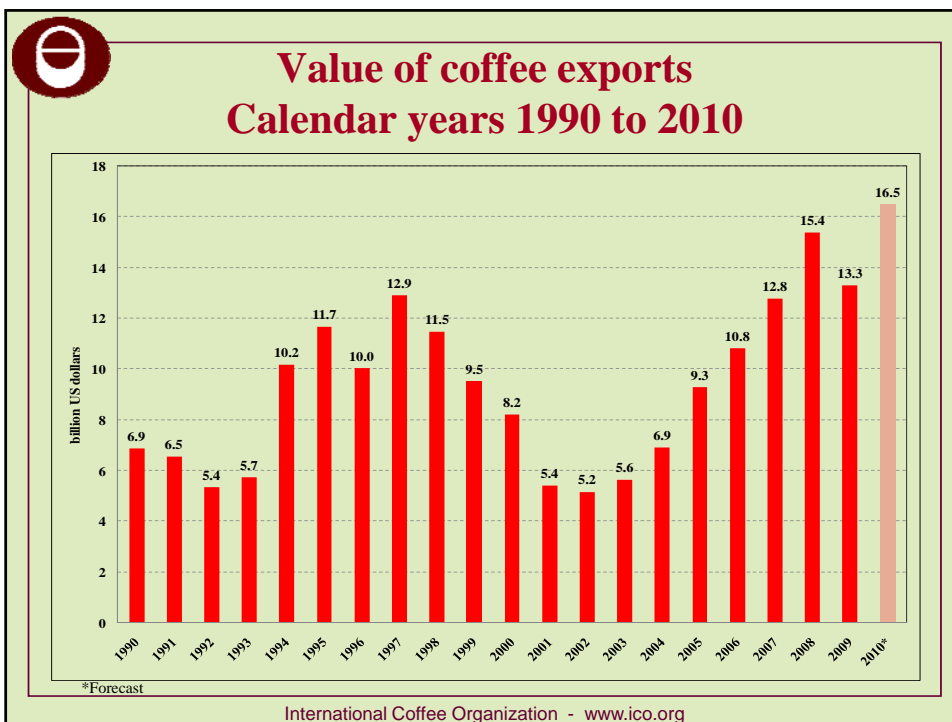
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Volatility: Effects

- Variation in prices is in itself not necessarily harmful, if the parameters of this variation are known in advance and can be factored into decision-making, but this is often not the case with commodity prices, where the variability of prices around apparent long-term trend far exceeds the size the trend itself.
- Policy problems for governments
- Smallholder farmers trapped in risky activity

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**Coffee Exports as % of Total Exports
10 leading producers 2010/11**

Country	PRODUCTION	COFFEE AS % TOTAL EXPORTS	
	(mln 60-kg bags)	1981-1985	2005-2009
Brazil	48.1	9.9	2.5
Vietnam	18.0	1.5	2.8
Indonesia	9.5	2.1	0.5
Colombia	9.0	50.1	6.2
Ethiopia	7.5	61.7	31.9
India	5.0	2.3	0.3
Mexico	4.5	1.9	0.2
Guatemala	4.0	32.3	11.2
Honduras	3.9	23.2	16.1
Peru	3.7	4.0	1.9

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Coffee Exports as % of Total Exports Coffee-producing LDCs

Country	Production 2010/11	Coffee as % exports	
		1981-1985	2005-2009
Ethiopia	7 450	61.7	31.9
Uganda	3 200	93.7	16.3
Tanzania	1 083	32.6	4.8
Madagascar	500	36.9	1.0
Guinea	450	0.8	3.4
Rwanda	433	69.5	25.4
Congo, Dem. Rep. of	350	18.3	0.5
Haiti	350	31.2	0.7
Burundi	300	87.5	58.9
Togo	250	18.1	1.7
Yemen	150	n.a.	0.2
Central African Rep.	50	34.7	1.9
Timor-Leste	50	n.a.	69.4
Angola	35	4.1	0.0
Malawi	30	1.3	0.4
Zambia	21	0.1	0.2
Liberia	10	4.5	0.2

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THE ROLE OF ICBs

1. Risk management tools for smallholders
2. Coping strategies
 - Diversification
 - Development of internal consumption
3. Enhanced market transparency

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Risk management

Instruments for managing commodity risks include:

- Stabilization programs
- Marketing strategies involving the timing of sales and purchases
- Long-term contracts with fixed prices
- Forward contracts
- Futures or options to hedge prices through commodity exchanges

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Risk management in exporting countries

In order to successfully run risk management programmes in exporting countries in a way that contributes to reducing rural poverty, the work needs to be carried out in several stages:

- › Strengthening institutional framework
- › Training
- › Development of domestic marketing (e.g. warehouse receipt system)
- › Improving access to agricultural credit

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Coping strategies

- ▶ Crop diversification (food crops)
 - ❖ CFC/ICO/47: Raising income security of smallholder coffee farmers in Malawi and Tanzania through sustainable commodity diversification
 - ❖ CFC/ICO/32: Diversification of production in marginal areas in the State of Veracruz, Mexico
 - ❖ CFC/ICO/31 Reconversion of small coffee farms into self-sustainable agricultural family units in Ecuador


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Coping strategies

- ▶ Development of internal consumption

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World coffee consumption Evolution 2000 – 2010

(in thousand bags)

	2000	2010*	Growth rate (%)
Traditional markets	63 367	70 837	+1.1
Producing countries	26 385	40 280	+4.3
Emerging markets	15 750	22 883	+3.8
World total	105 502	134 000	+2.4

*Estimated

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World coffee consumption: Producing countries Evolution 2000 – 2010

(in thousand 60-kg bags)

	2000	2010*	Growth rate (%)
Total	26 385	40 283	+4.3
Brazil	13 075	18 945	+3.8
Indonesia	1 664	3 333	+7.2
Ethiopia	1 938	3 253	+5.3
Mexico	1 189	2 239	+6.5
India	938	1 400	+4.1
Others	7 581	11 113	+3.9

*Estimated

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Enhanced market transparency

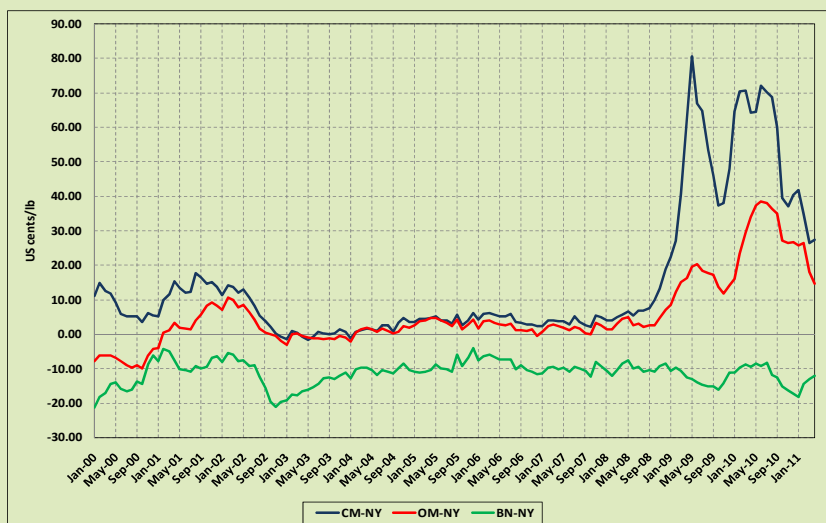
- ▶ Example: basis risk of Arabica coffee

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Differentials: Group indicators and NY futures

Monthly: January 2000 to April 2011



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