

Gear up to live with high inflation

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Readers will remember the food riots in Egypt as "khabus" disappeared off the shelves in Cairo and surrounding cities due to wheat shortage. There were riots in equatorial guinea where the local population ran berserk as bread and rice went scarce. Much of these events did not get as much attention from the media as they deserved. But the resource depletion experts who have a keen ear to the ground have raised the red flags of caution, inflation and action on a war footing. Unless these issues are tackled seriously and immediately, the situation can get out of hand. The strategy of pacification of the masses, extending hope of reversing the price rise is, in my opinion, faulty. The problem is of supply side constraints and unless we acknowledge the problem honestly, we cannot solve it. High inflation is here to stay!

I had written in my DNA Money column recently why the inflation in the agri commodity space will continue. I had also prophesied that consumers will have to learn to live with rising food price inflation in the coming years. Here are a few points to buttress my argument. Since the last 5 years, arable land acreage has shrunk by 8 % due to soil erosion, rising sea levels and advancing deserts, aided by sandstorms. The situation in some parts of China is so dire that sandstorms manage to submerge telephone poles under the advancing dunes! China is emerging as the "dust bowl" of the world as overgrazing, falling water tables, depleting rivers is leaving the topsoil drier year on year. With dry soil vulnerable to blowing in the wind, especially in northern and western parts of China, the resident population is frequently forced to move rapidly. Africa is another source of sand storms emanating from the Sahara and Sahelian regions. In case you think the menace of sandstorms is exaggerated, consider this - sand storms originating from N W China dumped millions of tons of sand in Arizona (USA) and Canada in 2001. Korea now frequently experiences frequent sand storms that destroy agri crops. The role of temperature in crop yields cannot be emphasised enough. For every rise of 2 degrees Celsius in global temperature, Rice and Wheat crop output declines 8 - 10 %. With the Copenhagen summit pointing towards a very warm 2010 calendar year, save money to buy food!

The Chinese are losing 360000 hectares / year to advancing deserts, Brazil 58 million hectares and Nigeria 3,51,000 hectares / year. All these are heavily populated nations and running out of buffer stocks of grains and pulses. Figures for the FSU (former Soviet Union) are not authentically available but sandstorms are on the rise there too. The Bodele depression in Chad loses 1.3 Bn tons of top soils to sandstorms / year. Africa loses 3 Bn tons of top soil / year to sand storms and the Taklamakan and Kumtag desert are approaching each other, sometimes at a rate of 150 metres per day ! Once these two deserts converge, the frequency and ferocity of the sandstorms can only be imagined. So will the magnitude of crop destruction and food shortage world wide.

Enough has been written about the impending shortage of water - our most necessary but finite resource. Unfortunately, little of what has been written has been taken seriously!

Shortage of water means an automatic shortage of food. Aquifer depletion in non rejuvenating aquifers has been to the extent of 40 % in some parts of India and China in the last 25 years. Pilferage, adulteration and mismanagement of this resource adds to the reckless wasteful consumption that threatens to hasten a food shortage worldwide.

Sugar - Worldwide output of sugar was down 4.7 % in 2008 - 09. India needs to import 2 million tons of sugar in 2009 -10 just to meet this fiscal years target. This is in addition to the 1.80 million that has already been imported. With a demand at 23 Mn tones in 2009 - 10 the production is far shorter at 16 Mn tons. The buffer stock is 3 Mn tons. The sugar crop is measured in 6 - 7 year cycles. With 3 - 4 years of ascending crop yields and 2 - 3 years of descending crop yield. We are in the second year of the downward cycle and unless the yield improves, cane prices are not about to decline. A truant monsoon and late excess rains have impacted the soil productivity. This commodity is at a 3 decade high and barring routine price corrections, do not expect it to get any sweeter.

Wheat - the largest exporters of grain - US, Canada, Australia and Argentina are witnessing stagnating / falling production levels. With domestic consumption rising due to rising population, there is less to export. Average US exports have fallen from 100 Mn tons / year are now at 80 Mn tons and falling. Rapid industrialisation and rising population is exerting a downward pressure on availability of cultivable land and an upward pressure on grain prices. China, the self sufficient nation till a few years ago is facing a crunch in availability due to rapid industrialisation and automobile incursion. The shopping list of China for wheat is expected to hit 80 Mn tons / year in a shortage infested world market. Unless the population growth reverses dramatically, cheaper grains in the coming years will be a fairly tale or a cruel joke!

Rice - Japan is the epicenter of rice consumption and the yield has seen a sharp decline. Rising consumption, limited cultivable land, industrialisation and soil erosion has turned Japan into a net importer. Without getting into macabre and depressing details, I will point just a simple fact - Thailand and Vietnam (largest exporters globally) have refused to step up exports in order to add to domestic buffer stocks and curb inflation. China has been pressing both for long term supply contracts, to no avail. Experts believe, it may escalate into a conflict / political crisis as mankind fights for food. Dont even dare to dream of cheaper pulao / biryani in the coming years.

Cotton - worldwide cotton production was down 9.20 % to 109.51 Mn bales. The reason is not hard to see - the crop needs a long growing season with plenty of sunshine and water. In the harvesting season, dry weather and repelling pest attacks are a major factor for improving yields. With higher carbon emissions and global warming, the climate is increasing hostile for producing high grade cotton. 70 % of the output is actually medium staple and experts predict a deterioration in the quality of output in addition to the shortage in terms of quantity. Your wardrobe bill is going to rise - whether you chose to like it or otherwise.

Tea - problems in Africa of top soil erosion, Sri Lanka of local strife and India of erratic monsoons have seen the output failing to keep up with the consumption. With rising temperatures expected in the coming year, the output maybe lower. Rising population will add to the demand / supply imbalance and buoy prices.

Readers are advised to learn to live with rising prices rather than expect a magic wand from the authorities to ease the situation. Tweaking of interest rates and CRR will be akin to applying band aid to an amputated limb. Sure there will be routine correction in prices but the larger trend is up - long term.

I continue to advocate an emphasis on investing in water companies, food, rare earth metals and ancillary companies. Stocks of water management, farm equipment manufacturing, seeds, pesticides and to a certain extent even fertilizer companies may prove to be good investments and a hedge against a rise in your food bill. You have two options – a) inaction coupled with whining or b) planned action and a good chance of success. Alpha into omega or omega into alpha – it's your call to take !

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