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IB Economics HL / Hertz
February 2013

Currency crisis hits Egypt's wheat supply

By Emiko Terazono in London and Heba Saleh in Cairo

Egypt, the world's largest wheat importer, is struggling to buy the staple in the international market because of the impact of a currency crisis, creating a fresh challenge to the government of Mohamed Morsi, the Islamist president.

Grain traders shipping wheat to Egypt said Cairo had cut back on its overseas purchases as the Egyptian pound plunged against the US dollar. The slowdown has depleted the country's grain stocks to unusually low levels, traders added.

Cairo on Wednesday said that government inventory levels of wheat, usually at enough to cover six months' worth of consumption, had almost halved to just 101 days. "They are living hand-to-mouth," said one Swiss-based international grain trader.

The Egyptian cabinet added that wheat reserves would stretch by another month with the arrival of supplies tendered for delivery in March and April.

With more than 40 per cent of Egyptians living below the poverty line, subsidised bread is an important part of the Egyptian government's strategy for maintaining social peace. Lower inventories made it vulnerable to any supply disruptions, analysts and traders said.

"The two things [the government] can't lose control of are bread and fuel," said Firas Abi Ali at Exclusive Analysis, the political consultancy, in London.

The Egyptian authorities have been wary of touching food subsidies since rioting swept Egyptian cities in 1977 after the government decided to raise the prices of a range of staples. The authorities were forced to rescind their decision to restore order.

During the food crisis of 2007-08, which pushed the cost of wheat to an all-time high, many families became reliant on subsidised bread, with long queues forming in front of bakeries and frequent scuffles breaking out. Army bakeries were drafted in to augment the supply.

The low level of wheat stocks was disclosed as Nomani Nomani, the head of Egypt's powerful state-grain buyer General Authority for Supply Commodities, announced he was stepping down.

Mr Nomani was highly respected among international grain traders, as well as being one of the most powerful figures in the global wheat market. His announcements about how much wheat Egypt planned to buy in one season could move grain markets from Paris to Chicago.

The slowdown in wheat purchases – usually at about 10m tonnes a year, equal to the total annual wheat exports of Russia – first affected private importers, who have scrambled for US dollars amid the foreign currency crunch. "Ultimately it comes down to the unavailability of funds," said a leading grain trader.

Wheat traders complain about delays in payments from private importers, and say that wheat shipments are not entering into the food supply chain in Egypt because the cargos are held at ports and warehouses until payments arrive.

Cairo could offset lower wheat imports with higher domestic purchases when the harvest starts in April. But international traders fear that local farmers may retain more of their crop in the expectation that the price will increase. This could affect the amount the government can purchase, said one international grain trader.

Since the revolution which ousted Hosni Mubarak from power two years ago, Egypt has seen a sharp drop in its foreign reserves as continuing political turmoil has scared away both tourists and investors. Foreign reserves dropped from $36bn on the eve of the uprising to $13.6bn at the end of January – a level that was below the critical three months' import cover, analysts said.

Importers have been finding it more difficult to access foreign currency with banks and exchange bureaus citing shortages and delays. The central bank has instructed local lenders to prioritise access to foreign exchange, placing importers of basic food stuffs at the front of the queue. Some private grain importers have been forced to turn to the black market in foreign currency to obtain US dollars.

http://www.ft.com/intl/cms/s/0/828043ca-7608-11e2-8eb6-00144feabdc0.html#axzz2MBRkCGEd

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Outline

- **Foreign funds:** Foreign currency available in foreign exchange offices of a state. In this case, US dollars
- Drop of currency's value coupled with dramatic decrease in Egyptian foreign funds
- Decrease in available government funds: results in an inability to purchase necessary amounts of wheat imports, as well as the development of a black market for USD
- This leads to an excess of demand as supply of wheat in Egypt shifts to the left
- Impacts the price mechanism of supply and demand, wherein there is an upward pressure on the price of bread, since wheat the major FOP of bread
- Bread being a necessity good = low elasticity of demand, therefore consumers get damaged a lot by a higher price
- Measure: Government subsidies on bread production to sustain availability to society
- Alternatives: Increase local production of wheat through subsidies to discourage imports -> problem of climate and cost of the factors of production
- Long-run: Egypt's economic policy will deal with the currency rates and foreign funds, re-kindling the ability to purchase the necessary amounts of wheat
- This was a special case, as it was triggered as an aftermath of the revolution: "Foreign reserves dropped from $36bn on the eve of the revolution to $13.6bn at the end of January – below the critical level needed for three months import cover"

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Diagram 1: Excess of demand of wheat

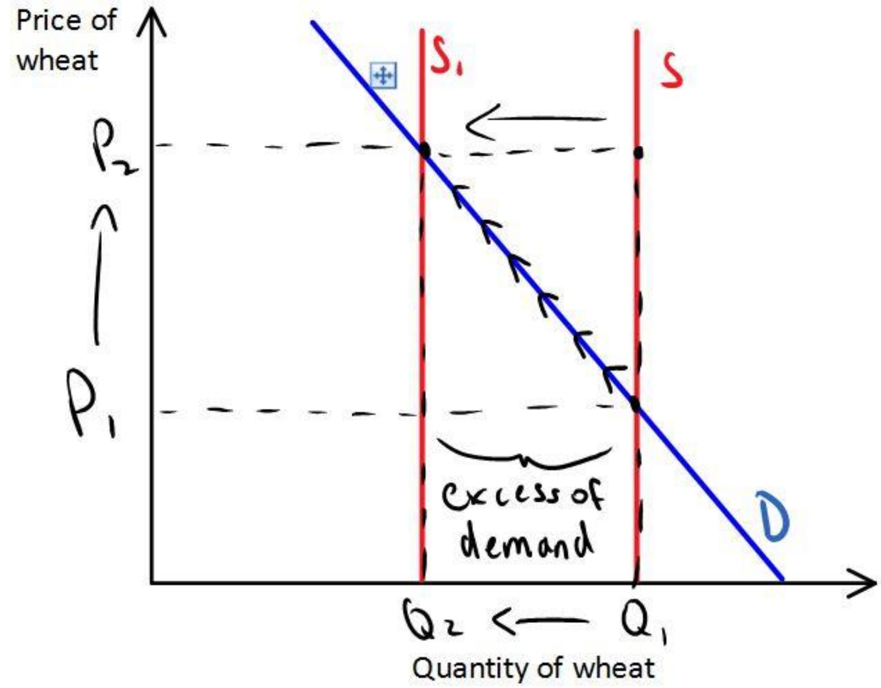

Diagram 2: Subsidies on bread production