The new political risks in the global food and beverage supply chain

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Section 1: Introduction by WTW

By Sam Wilkin,
Director of Political Risk Analytics, WTW

Three months after the escalation of the conflict in Ukraine, Sri Lanka defaulted on its debts, its government fell in the face of a mass uprising, and the president fled the country.

The link between Sri Lanka's troubles and a conflict some 4,000 miles away was not immediately obvious. But the timing was no coincidence. Russia and Sri Lanka were in fact linked by global supply chains. Sri Lanka had borrowed excessively (in our summer 2021 Political Risk in Renewables report[1], Sri Lanka had been flagged as a country likely to suffer a debt crisis). International tourist arrivals, a key foreign exchange earner for Sri Lanka, had collapsed during the pandemic. And an ill-timed effort to adopt environmentally-friendly fertilizers had sapped the output of the country's agricultural sector. But most notably, Russia and Sri Lanka were linked by the global energy supply chain.

The conflict in Ukraine then sent global food and energy prices surging. The Sri Lankan government subsidizes the price consumers pay at the pump for petrol. The additional costs would have broken the budget, but when the president tried to remove the subsidies, he found himself with an uprising on his hands, and protesters occupied the presidential residence.

Russia plays a key role in world energy supplies. Ukraine, Russia, and Belarus, taken together, are even more central to the global food supply chain, including not only direct production of wheat and edible oils but also agricultural inputs such as fertilizer.

The shock to global energy markets from the conflict in Ukraine contributed to social unrest in 92 countries in 2022, perhaps most dramatically Sri Lanka and Haiti;[2] the shock to global food supplies from the conflict contributed to further unrest and a global food crisis that helped to push Ghana into sovereign default and Egypt and Pakistan into international bailouts. These crises came at a moment when political leaders were already focussed on the security of supply of vital goods in the wake of the pandemic.

How have such shocks reshaped the global food and beverage supply chain? Can agribusiness, commodities trading, and food and beverage companies manage the associated political risks? What risks will companies face if the world food crisis resurges in 2023? What political risk perils might be lurking 'under the radar'?

We asked Oxford Analytica to aid us in conducting research into these questions. Oxford Analytica and WTW convened a panel of nine external affairs and risk management professionals, representing agribusiness firms, food and beverage companies, food and beverage packaging, and agricultural commodities trading.

Oxford Analytica and WTW then conducted in-depth interviews with these professionals, to produce the risk radar that appears in the next section. For one of the top risks the executives identified, Oxford Analytica commissioned scholars in its expert network to produce a peer-reviewed essay, covering "Which countries are most vulnerable to food price shocks, and why?" and providing a risk index of countries that could be impacted.

Several panelists were convinced that the globalized food and beverage supply chain would change profoundly in the years ahead. "We are moving from a world of global supply chains, where you could source anywhere, to one where you need to ask whether you are allowed to buy it, allowed to transport it, able to transport it, and whether it arrives on time," was one such comment. "This trend is exacerbated by regulations that seek to ensure that locals are supplied first."

We hope you find the report useful. We sincerely thank the Oxford Analytica contributors who authored the following essays, but most of all we thank the expert panel of executives who guided the research for their time and insights.

CALLOUT 1

How are food and beverage companies addressing the new risks?

One question Oxford Analytica and WTW posed to the executive panel was: “how are you managing the new political risks in the global food supply chain?” In this callout, Oxford Analytica presents a summary of the findings. The views expressed do not necessarily reflect those of WTW.

“Supply chain risk was an operational issue,” said a food packaging executive based in Europe. “It has now become a strategic issue.”

Managing the risks associated with a complicated international supply chain has long been a challenge for globalized firms. Companies were required to look first to their own direct suppliers, and then farther upstream, assessing whether business continuity plans were in place and if there were single sources at any point.

And yet, in the final analysis, these challenges were operational. It may have been time-consuming to conduct the due diligence required, but it was relatively easy to define both the risks themselves and key risk indicators.

As supply chain risks become increasingly strategic in nature, that conceptual simplicity is evaporating. “We are now moving to a world of geopolitical issues as risk management topics,” the food packaging panelist continued. “It is difficult to evaluate these risks.” For instance, components or raw materials can become an issue – for example the global microchip shortage has impacts across entire industries. “We now have to be accountable for not only direct suppliers but entire supply chains,” our panelist concluded. “We have no control over this.”

In many sectors, leveraging an international presence to achieve scale was a winning business model for the past several decades. It is far from clear that this will continue to be true. This reality adds to this strategic nature of supply chain risks. “It’s hard to do a one-size-fits-all solution,” said another panelist in the food manufacturing sector. “Different pressures are meaning we now must adapt to local differences. Both regulatory pressures and consumer preferences are driving this.”

How can companies address these hard-to-evaluate geopolitical risks in the food and beverage supply chain? Scenario planning was a popular solution among the companies we interviewed. “We have a much stronger link between scenarios and our corporate strategy,” said an executive at a packaging company. “We are also engaging in more dynamic strategic planning with a much more regular review, and we closely follow signposts that tell us when a scenario is emerging.”

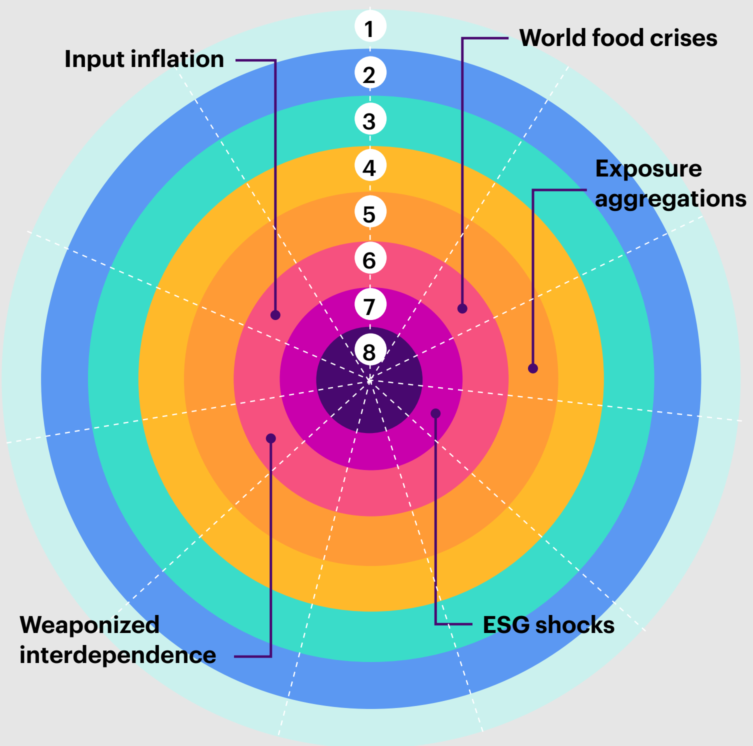
A panelist at a commodities trading company, however, expressed skepticism that even scenario-based approaches could work. “We can run the scenarios, but it will never be the scenario you expect,” he said. “I think as a result, rather than be prepared with a plan, you need to be prepared by having people who are just agile enough and good enough to react. I may be pessimistic that we have to be reactive rather than proactive, but I think I am right.”

Other panelists argued for resilience as an approach. “Ultimately the food supply chain is only as viable as its weakest link,” said another executive at a commodity trading company. “So, we have to identify those weak links and provide adjustment support.”

Section 2: The political risk radar

Political risk radar for the global food and beverage supply chain (ranked by number of mentions)

To identify the top political risks facing the global food and beverage supply chain, Oxford Analytica and WTW convened a panel of external affairs and risk management professionals representing commodities traders, agribusiness firms, food and beverage packaging, and food and beverage manufacturing companies. Companies headquartered in North America, Western Europe, and Asia took part. Oxford Analytica and WTW conducted in-depth interviews with this panel of executives, to produce the risk radar that appears at left. Below, for each risk on the radar, Oxford Analytica summarizes some of the interview highlights. The views expressed do not necessarily reflect those of WTW.



Source: Oxford Analytica and WTW interviews with the executive panel. "Mentions" count the number of panelists who mentioned each risk topic.

Under the radar: Trade route disruption. Food and beverage nationalism

ESG shocks

Our top risk, with seven mentions, was ESG (environmental, social and governance) shocks. For most executives we interviewed, the main ESG issues of concern relate to climate and the environment, in part because of the perceived environmental impact of the sector. "All the businesses that rely on heavy water usage are under severe pressure from the governing authorities to demonstrate how they are suppressing water use," one interviewee noted. In a similar vein, another panelist commented: "The agriculture industry in New Zealand is responsible for roughly half of [the country's] GHG [greenhouse gas] emissions."

ESG shocks can also reshape demand. One agribusiness executive noted that measures in the European Green Deal could "reduce the use of fertilizers by 20%," with potentially a dramatic revenue impact for the company; another executive in the sector, based in Asia, commented that "Europe's shift to sunflower from palm oil has trimmed our profits from Europe." The executive noted that such bans had an ESG impact over and above the direct impact of the regulation, creating negative reputation effects. Another panelist, a food manufacturer, worried about the shift to veganism, promoted in part by organizations such as PETA (People for the Ethical Treatment of Animals).

Of course, consumer demand shifts also present an opportunity for those companies able to innovate ahead of such changes. "It can be a differentiator, there are lots of ways of looking at it," noted an executive at a food and beverage packaging firm. "If one is unable to adapt then it is a risk."

The global food crisis – discussed further below, and in the essays section – may pose ESG challenges for companies that play an integral role in the global food supply chain. "Companies seen to profit when people struggle might become a target, for instance of press attacks," said one executive at a commodities trading company. "We could even face cyber-attacks or have activists disrupt our meetings."

In such circumstances, the line between hero and villain can be thin. "If we were not here to trade commodities the prices would be even higher," the executive pointed out. "We tend not to communicate well the crucial role that trading companies play during these difficult times."

Weaponized interdependence

The risk is discussed in more detail in the callout, "How will EU rules reshape the global food supply chain?"

Weaponized interdependence

For most sectors, the genteel trade war between US, Canada, Mexico and Europe that occurred under the administration of US President Donald Trump was a mild annoyance. Not so for many food and beverages producers, whose products were a prime target of retaliatory measures against US tariffs on steel. "We had to pay more than $300 million as a result of that decision [to impose steel tariffs]," said a US agribusiness company on our panel.

After decades of post-World-War-II progress in globalization, countries around the world are economically interdependent. Recently, policymakers have begun to seize on this interdependence as a weapon – a weapon that can be used to get better deals on trade, punish adversaries in diplomatic disputes, or undermine rivals in geostrategic competition. The fact that the damage from deploying such weapons tends to fall also on the wielder was once seen as a deterrent against their use. Such considerations appear to be falling by the wayside as geopolitical tensions rise.

When countries seek to weaponize interdependence, agriculture is often on the front lines. Following controversial comments by Australia's government about the origins of the novel coronavirus, China appeared to retaliate against Australian wine and shellfish producers (and not in a small way: retaliatory measures eventually impacted up to 10% of Australia's annual exports). Retaliation against the Trump-era steel tariffs by Canada, the European Union, Mexico and others impacted US agricultural exports worth more than $30 billion annually. One of our interviewees noted that a diplomatic dispute between India and Malaysia had resulted in bans on certain agricultural goods that had led to a "significant loss" to their company.

The conflict in Ukraine has resulted in weaponization of interdependence on an unprecedented scale, ranging from seizure of Russia's foreign exchange reserves (effectively forcing Russia into sovereign default) to a Russian ban on natural gas sales to Europe. "It is becoming increasingly difficult to do business in Europe as applicable sanctions impact commodity trade flows," said one trading company executive. "Sanctions and permits of licenses to operate are changing very rapidly, meaning we have to halt or change our procedures and operations completely." An agribusiness panelist stated: "All businesses involved in the dairy and food industries are paying a significant price [for the conflict], and consumers must bear the cost increase of these essential goods."

It was once said that there would never be an armed conflict between two countries that host a McDonald's restaurant. The presence of the hamburger chain was seen as an indication that a country had reached a degree of globalization that would be too costly to reverse. That era has passed, and even businesses that are distant to the conflict in Ukraine find themselves operating in a divided world. "We are under immense pressure to pick a side to do business with because of the conflict [in Europe]," noted an agribusiness panelist based in New Zealand.

Some trade wars, including the Trump administration steel tariffs described above, have proved temporary. It is possible that current sanctions could be reversed. But most panelists we interviewed were pessimistic about the direction of travel. "Sanctions are a symptom not the underlying cause of disease," as one executive put it, forecasting a "Cold War emerging between the US and China."

Input inflation

The relationship between the global pandemic and inflation has been complicated and often unexpected. As the world went into lockdown, consumers shifted from spending on services to spending on goods, contributing to major shortages, and spiraling prices, in products such as microchips and automobiles. Emerging from the pandemic, consumers shifted back to spending on services. Prices of, for instance, rental cars and airline tickets skyrocketed as demand surged. The fact that many advanced economy households and businesses had saved during the pandemic, and therefore had money to spend, was seen as a sign of economic strength. But these savings meant consumers were able to carry on spending even as prices rose, contributing to yet higher inflation, particularly in the US.

In Europe, wages are often set by collective bargaining arrangements, and therefore have tended to be slower to rise. Hence inflation in energy prices has sapped household spending. "Most European economies are witnessing a slowdown," said a commodities trader on our panel. "We are concerned because almost 30% of our revenue is generated in Europe." A dairy products executive agreed: "we could see a major economic fallout worldwide, directly affecting households, who are our consumers, as inflation causes a direct impact on our sales due to lower demand." It is possible that inflation will trigger further economic risks, as another executive on the panel noted: "there is credit risk and risk of bankruptcy as well."

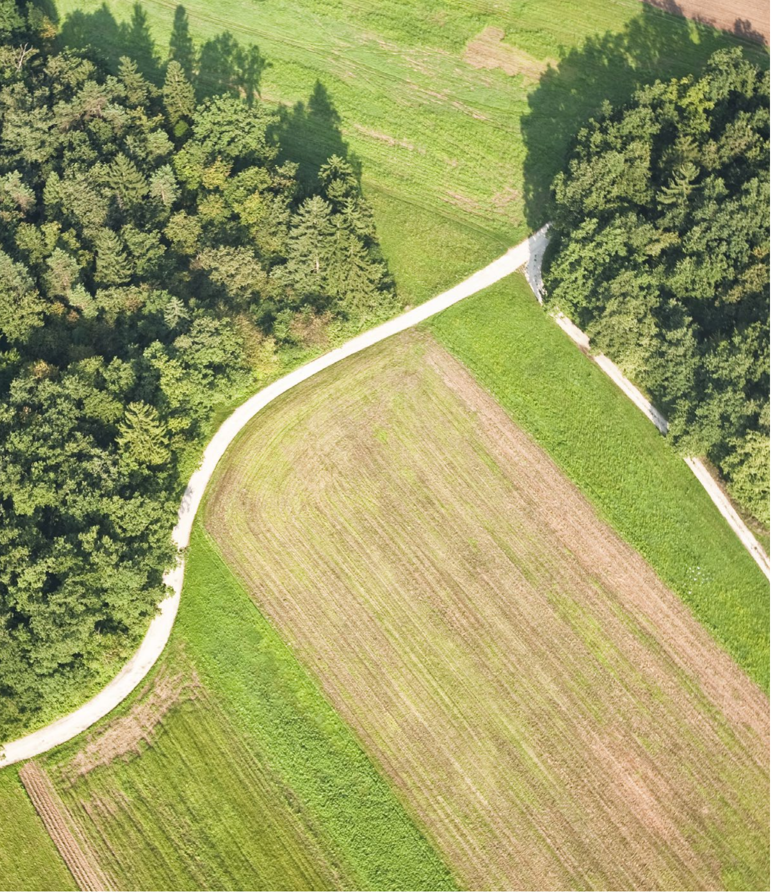
Of course, many companies we interviewed are on the front lines of this broader societal risk. Russia plays an important role in world energy, contributing roughly 10% of world oil supplies; but Russia, Ukraine and Belarus, taken together, play an even more crucial role in global agricultural supply chains. This role includes not only wheat (where Russia and Ukraine account for nearly 30% of world production) but also fertilizers (Russia and Belarus account for roughly 40% of the world's potash, for instance).

Hence the conflict has led to acute disruptions for some of our panelists. "Current geopolitical conditions have caused price hikes for both grains and soybean meal, leading to an increased harvesting cost of our livestock," noted one executive. "We are trying to find alternative solutions for the disrupted supplies but haven't been able to identify any so far." "Fertilizer is a key component for plantations," an agribusiness panelist based in Asia stated. "Although we are still getting fertilizers, there is no fluent supply." In a similar vein, another agribusiness executive said: "Russia is the largest supplier of ammonium nitrate, which is essential for making fertilizers, and also a leading exporter of urea and phosphate, but we have stopped procurement from some Russian suppliers due to the sanctions that have been implemented on Russia by the European Union."

World food crises

Rising food prices are a relatively small element of the consumer price inflation occurring in the US and Europe. Consumers in rich countries tend to spend relatively little of their income on food, and much more on housing, travel, savings and healthcare. In the US, UK, or Singapore, for instance, the share of household spending that goes to food consumed at home is less than 10%.

In poorer countries, by contrast, a far larger portion of household budgets goes to sustenance. That figure has been estimated at more than 50% for Nigeria and Kenya, and 40% for Pakistan and the Philippines. Hence rising food prices have the potential to plunge people into financial distress or even starvation. According to the United Nations World Food program[3], the number of households globally who face acute food insecurity more than doubled from 135 million pre-pandemic to 345 million in 2022.



While the peak of the global food price shock has passed, world food crises are likely to threaten the sector for years to come, due to climate-related disruptions and the ongoing turmoil in Russia, Ukraine and Belarus – countries that play a vital role in the world's grain and fertilizer supplies. "[World food crises] creates the potential for higher political risk and civil unrest," as a panelist from the packaging sector based in Europe noted. "Many countries are struggling with the shortage of fertilizers," an agribusiness panelist added, which combined with political turmoil could lead to smaller-than-expected harvests in 2023." In 2023 and beyond, climate-related disruptions could compound with geopolitical shocks, making global food prices more volatile.

"This year we are dealing with simultaneous floods and droughts," a commodities trading executive noted. "It's extremely dry in the West and extremely wet in the South and East of the United States. Brazil and India are experiencing similar patterns. There are lots of supply and demand imbalances as a result."

The 2022 crisis was exacerbated by the policy responses of food-exporting countries. At the peak in August 2022, 18 countries had put in place export bans on vital agricultural commodities, and five had put in place licensing restrictions (according to the International Food Policy Research Institute)[4]. Such measures may help shield local consumers from rising world prices, but are estimated to have added a further increase of nearly 10% to the already-elevated global wheat price, according to the World Bank[5].

During a crisis, market shocks tend to create ripple effects. "Disruptions in any one commodity create risks for others," as one of our US-based panelists noted. "A ban in India on rice [exports] will have an impact on corn, for instance. Everything is linked because people look for substitutes for commodities that are lacking."

Of course, for some of the companies we interviewed, higher prices have meant higher profits. "It's another opportunity for us," said a food packaging executive, "to make it possible to transport food over long distances and in difficult conditions." "We benefit greatly from the conflict," a panelist at a palm oil producer admitted. "I'm not saying it is a great deal, but it has benefitted us and other producers in our region."

Of course, while profits may be high, producers must contend with the threat of destabilization of key countries, and possible ESG risks (discussed above). Moreover, a world food crisis creates myriad political risks. "We are concerned with domino effects," said one commodities trader. "Risks include SRCC [strike riot civil commotion] and seizure of food commodities by governments that have been impacted."

This risk is discussed in more detail in the section, "Which countries are most vulnerable to food price shocks, and why?" as well as the callout "The increasing geopolitics of food security – what's the beef?"

Exposure aggregations

During the heady years of globalization, particularly during the 1990s and early 2000s, many firms found it relatively easy to manage geopolitical risk. Global companies were usually diversified, such that a loss of any single market or trade route was tolerable. Even those companies dependent on certain key markets were protected by a global network of trade agreements and bilateral investment treaties that raised costs for any government seeking to take arbitrary political or regulatory action.

For better or worse – but mostly worse – those days now appear to be behind us. The conflict in Ukraine has shown that there are some geopolitical tensions that no investment treaty can protect against. The sudden shift of Russia from key global market to international sanctions target has shown that no world economy is too large to be excluded from the globalization system. (The "BRICS" category of emerging markets is now significantly smaller, from the point of view of many Western firms.)

"We grew very rapidly in Russia," one panelist based in Europe explained. As a result of that faster-than-expected growth, the company's aggregation of exposure to Russia became unbalanced relative to the firm's global portfolio, and the company had to write down a significant portion of its equity value because of the conflict in Ukraine. "Now China is growing fast," the executive continued, and the loss of Russia has, ironically enough, made China even more important as a share of the firm's global profits. As a result, the firm's China exposure is now unbalanced, and a key topic of concern. They continued: "We are worried about China being excluded from the global financial system, as has been done to Russia. We are also worried about potential bans on foreign owned entities or public opinion being raised against foreign businesses. You tell me: how do we finance China risks?"

China was the top exposure aggregation concern for several executives we interviewed. "They [China] may decide to restrict our products for public health or welfare reasons," a panelist from an agribusiness company worried. "From a geopolitical risk viewpoint, China accounts for a significant portion of our profit; therefore, this is our priority." Another Europe-based panelist pointed out: "We don't know what lessons China has drawn from the Russia-Ukraine situation. We don't know what they concluded about how the West will react; about the severity of the consequences; and whether they can live with the consequences."

As of this writing, speculation about the future of Taiwan has increased – and some of this speculation may reflect clumsy analogies that have more to do with perception than reality. That said, as one US commodity trading panelist pointed out, "at the present moment if something were to happen the disruption of logistics would be particularly extreme because alternate [shipping] routes go via Russia."

Moreover, Asia was not the only concern. "Our main concerns are the big origination points and the top destinations," said an executive at a US commodity trading firm that had considered such issues carefully. "For origination, the number one is the US followed by Brazil and then the Black Sea region; for destinations, number one is China followed by Europe."

Under the radar

We conclude our risk radar by looking at what might be flying below the radar – the risks that might become top concerns tomorrow.

The first of these below-the-radar threats is **disruption to trade routes.** Such risks might seem obvious in the wake of the conflict in Ukraine. "Crude prices ... hit the roof due to geopolitical conflicts between nations, so we [faced] rising shipping costs," as one agribusiness panelist noted. "Vessels can't travel," said an executive in the commodity trading sector. "The ... deal brokered by Turkey is itself subject to risk. Going forward with the upcoming harvest we're not sure about the ability of farmers to get to ports."

Other risks to the global food supply chain are less obvious, however. "Container vessels typically follow a China-Europe-US route," said another panelist at a commodity trading firm. "If that route becomes disrupted, then you need to change the size of vessels – because if you're shipping direct from North Africa to Europe, for instance, most ports cannot handle large vessels." Hence there is a possibility that the world's supply of container ships could be mismatched to the available trade routes, a problem that would take time to resolve.

A final below the radar concern is **food and beverage nationalism.** As policy responses to the world food crisis (discussed above, and in the essays section below) have shown, attitudes towards the food supply chain can quickly take a nationalist turn – even when such actions worsen an already difficult global situation.

Some pressures towards deglobalization of the food supply chain may well be unintended. "Regulation, such as sugar and fat content, changes not only the nature of the supply chain but also the nature of the products we can sell," commented one panelist in the packaging sector, "so if you are selling a product in China and Brazil and then regulations diverge you might have to develop two different products."

Other panelists were worried that the post-pandemic focus on securing supply chains for strategic goods would reshape the food and beverages sector, even including ownership of assets. "When these risks began to impact oil and gas in Russia and Europe it was a big surprise," noted an executive in the alcoholic beverages sector. "Therefore, it is a concern that something similar might happen [in food and beverages]. Such measures could, as in energy, eventually take the form of nationalization of foreign-owned assets," they continued.

The loss of Russia has, ironically enough, made China even more important as a share of the firm's global profits. As a result, the firm's China exposure is now unbalanced.

CALLOUT 2

Trade credit - charting a course in uncertain times

Scott Morrison
Director, GB Trade Credit and Political Risks

Historically, the food and drink sector has been resilient to economic shocks due to the essential nature of its products. The sector also proved resilient to much of the consequences of the COVID-19 pandemic, although it was impacted significantly by transportation delays on short shelf-life products and by the impact of lockdowns on the hospitality sector.

Global food price inflation has hit all-time highs and while it is expected to ease from recent peaks, inflation will remain significant.

The Russia/Ukraine crisis has significantly impacted the supply of cereals in light of these countries being the world's second and third largest global cereal exporters. The supply of vegetable oils has also been severely affected as Ukraine accounted for 13% of global supplies while its sunflower oil production made up 50% of global trading, with Russia accounting for 25%.

The fertiliser market has experienced a similar impact, with Russia being the world's largest exporter of fertilisers, and Ukraine and Russia-ally Belarus also being very significant suppliers.

Rising energy costs affect all stages of food and drink production, processing, packaging, storage and transportation. Labour availability and costs will continue to contribute to inflationary pressures on all sectors, including the food and drink sector.

Consumer confidence and levels of disposable income will affect the hospitality sector and follows hot on the heels of the impact of COVID-19, with government schemes that supported the sector having now ended.

There are many ways the trade credit insurance sector can help companies measure, manage and mitigate the challenges of the current environment.

Assessing the risk of both existing and potential new customers is critical in light of the potential impact from COVID-19 and the current macroeconomic factors on those companies.

While market conditions will be challenging for some time to come, business growth will be key for businesses at a time when margins are likely to be under pressure. Insurance can give organizations a competitive advantage that can enable expansion into sectors and markets on credit terms, and allows them to maximise credit lines with existing and new customers that may not have been considered without the insurance cover.

The importance of maintaining and protecting their supply chains will mean many companies will look to expand existing, or consider instigating, supply chain finance programmes. At a time when interest rate rises will put additional pressures on companies, giving suppliers access to early settlement options provided by funders, underpinned by insurance cover, could be an attractive option for both suppliers and their customers.

Global insolvencies are increasing and are predicted to significantly increase during 2023[6]. Protection in the form of indemnification for losses incurred at a time of unprecedented uncertainty and heightened risk is a further benefit of trade credit insurance against this backdrop.

CALLOUT 3

Maintaining resilience and growth in volatility

By Sue Newton
Director, GB Food and Drink Practice Leader

WTW's Food and Drink practice recently published a research report, *Maintaining Resilience and Growth in Volatility*, based on a survey of 250 senior executives in leading global food and beverage companies and qualitative research with senior U.K. leaders of food and drink manufacturing firms, both large and small.

Although early interviews in the research alluded to the worst of the supply chain disruption impacts from the pandemic being over, in later interviews – after the start of the Russia/Ukraine crisis – more respondents rightly predicted further serious supply chain disruptions.

In light of continued disruption, the research indicated how food and drink manufacturers are taking greater control of their supply chains by mean of:

- dedicated specialists at the coalface for overseas procurement and transportation of produce
- in-house freight forwarders
- import teams and customs advisors, and
- onshoring of sourcing

Such efforts to manage risk had promoted vertical integration of key links in the supply chain. "We completely control our own supply chain; we own our fleet of trucks; we have a freezer facility, so we have buffer stock if there's an outage; and a number of production sites to ensure continuity," said one director of risk and insurance at a food manufacturer. A company secretary and head of group risk at a drinks manufacturer said, "we have operational resilience delivered through self-managed and well-established manufacturing and distribution networks."

Other moves the research highlighted as supporting food and drink manufacturers in maintaining greater control over their supply chains include:

- In-advance ordering of raw materials, consumables and equipment and the continuing search for other ways to improve 'buffer stocks'
- Reducing over-reliance on key suppliers, both for existing and alternative ingredients and consumables
- Improved collaboration and effective business continuity planning across internal teams, including procurement, commercial, operations and risk management

When key links in the supply chain could not be brought in-house, many organizations sought to spread the risk, with one Group Risk Director at a food manufacturer saying, "we are analyzing commercial risks, for example, we question if there is over-reliance on certain retailer or certain supplier."

Other organizations sought to exert more control over third parties, establishing new frontiers in best practice to support supply chain resilience. "We are undertaking a program of process improvement, called 'Operating Brilliance,' creating clear standards and expectations around processes across the business," commented one health, safety, environment and risk director at a food manufacturer.

For similar insights, please see our report, available online: https://www.wtwco.com/en-GB/Insights/2022/04/global-food-and-beverage-survey-report

Section 3:
Which countries are most vulnerable to food price shocks, and why?

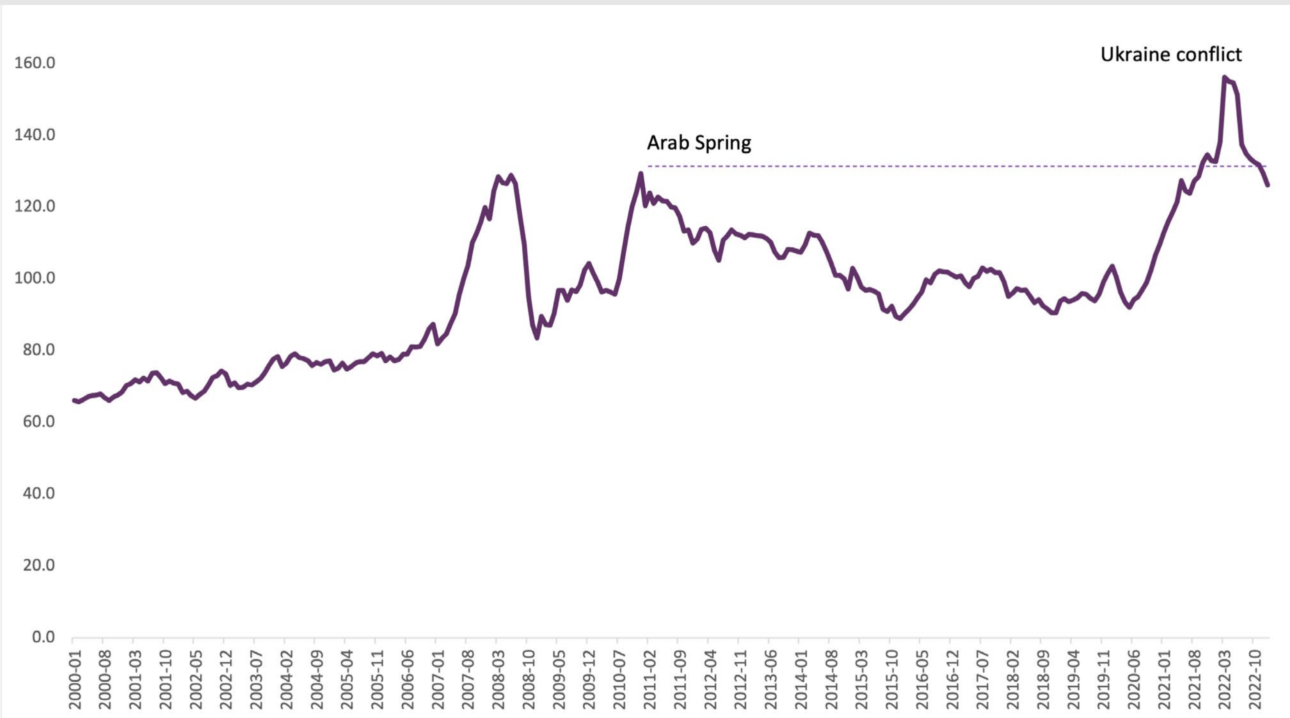
Some of history's most significant incidents of political instability can be linked to food prices, from bread riots in colonial Boston to the Women's March on Versailles in the French Revolution, to rice riots in Japan in 1918.

More recently, high food prices have been linked with instability worldwide. Beginning in 2006, there were rapid increases in the global price of food, particularly cereals. Prices increased faster than at any time in the previous 15 years and to levels almost four times more than at the start of the decade. The high prices of 2007-08 coincided with riots in Haiti (during which the prime minister lost power) as well as in Bangladesh, Egypt, and elsewhere in Latin America, Africa, and Asia.

Food prices began spiking again in 2010, when cereal indices jumped more than 40% year-on-year. The overall FAO Food Price Index was in fact higher than in 2007-08 and remained persistently high for years thereafter (see graph). This price shock contributed to the Arab Spring, particularly in Egypt. Protestors in Tunisia waved baguettes, those in Algeria cried "bring us sugar," and protests spread through a region dependent on food imports.

In 2022, world food prices exceeded levels associated with the Arab Spring and other prior incidents of political turmoil. Fuel prices also spiked, and related social unrest struck more than 90 countries[7]. What can we learn from the recent crisis that will help us prepare for future food (and fuel) price shocks?

Inflation-adjusted global food prices, 2000-2022



SOURCE: United Nations Food and Agriculture Organization, https://www.fao.org/worldfoodsituation/foodpricesindex/en/

A misunderstood connection

Much analysis of the link between food prices and political instability reflects views of the causes of social unrest that both survey and experimental evidence suggest are untrue.[8] For example, many comments about the 2022 food price shock reflected a perceived link between intolerable social conditions and riots. For example:

- "When people can't feed their families, it's an almost inevitable recipe for large-scale civil unrest" – Financial Newswire[9]
- "Food is a key element of any community's culture. When that element is removed civil unrest can occur" – Business Insider[10]

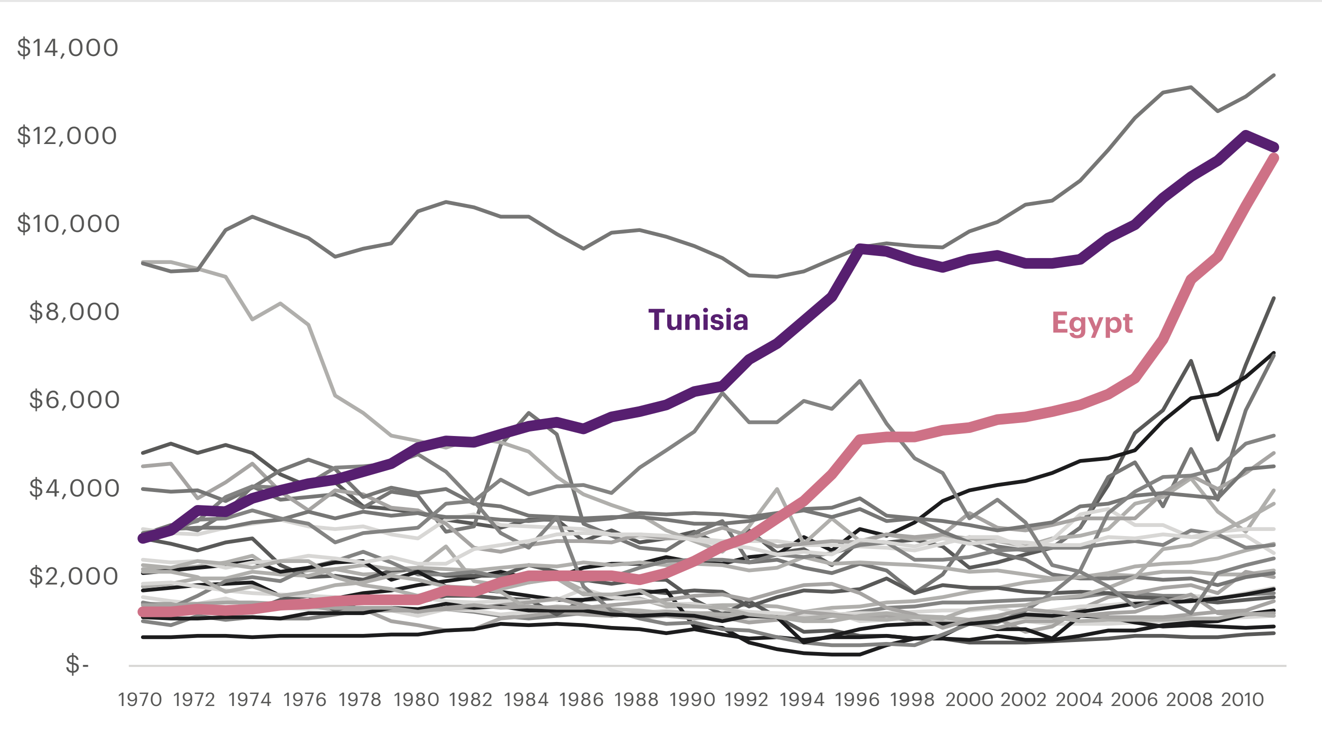
In a similar vein, much commentary about the Arab Spring reflected a view that dire economic conditions were to blame. For instance:

- "This was an angry explosion of ambitious but excluded youth. More than a quarter of Tunisians under 25 are unemployed" – Times of London[11]
- "Youth frustration grew over their social, economic, and political exclusion, exploding in 2011 into protests across the region" – Brookings Institution[12]

These comments are puzzling in part because the economies of Tunisia and Egypt, in the two decades leading up to the Arab Spring, were among the fastest growing on the African continent (see graph). Indeed, many of the most significant incidents of social unrest in recent years have occurred in relatively well-off countries. Examples include Hong Kong, one of the most prosperous regions of China; Chile, one of the wealthiest countries in Latin America; and major protest movements in advanced economies including the United States (#blacklivesmatter) and France (gilets jaunes).

Indeed, the country that arguably has so far suffered the greatest political upheaval from the indirect consequences of the conflict in Ukraine is Sri Lanka, where riots over rising fuel prices caused the president to flee the country. Sri Lanka is by most accounts a development success story, having enjoyed extremely rapid growth over the past three decades, rising from a per capita income of roughly $2,000 per person in 1990 (on par with Afghanistan or Zimbabwe today) to more than $13,000 per person in 2019 (on par with Mexico or Serbia).

Per capita income in 30 African countries, 1970-2010



SOURCE: Penn World Tables, https://www.rug.nl/ggdc/productivity/pwt/?lang=en

Research on the causes of social unrest suggests that we should not be surprised by this pattern. Generally, mass political action occurs when groups of people share a common political grievance and a common belief in their own political effectiveness – and the latter condition is much more likely to occur in relatively prosperous countries.[13]

So if political turmoil is not linked to intolerable conditions, what is in fact the link between high global food and fuel prices and political unrest? And, if the world experiences another food crisis, what countries will be most at risk of social upheaval?

The trouble with subsidies

When the news agency Reuters researched riots relating to the food and fuel price shock of 2022[14], they found a picture starkly at odds to the image of people rioting because they were unable to feed their families. For instance:

- Tunisian farmers protested to force the government to raise state-controlled food prices
- Thousands of students marched through Santiago demanding higher food stipends
- Thousands of farmers protested in Buenos Aires against government policies to contain food prices
- One person was killed in Guinea's capital during protests over hikes in government fuel price
- Price protests in Iran were sparked by the government's fuel subsidy cut decision
- Indonesian farmers protested in Jakarta against the government's palm oil export ban

These protests were not instigated by heads of households unable to obtain bread; they were usually sparked by special interest groups that had been adversely impacted by specific government policies. In many cases (such as Chilean university students), these groups were relatively prosperous.

One finds this pattern also in historical cases of food riots. For instance, many of the riots that occurred at the time of the French Revolution occurred because the French government closely regulated the price of foodstuffs (and had attempted to deregulate these prices). The resulting "bread riots," which contributed to the revolutionary atmosphere at the time, were focused on that specific policy.

These specific concerns about government policies are examples of political grievances, which research on social movements suggests are one vital spark for mass political action.

Movements in the global price of food and fuel are particularly dangerous as a source of political grievances because in many emerging market countries staple goods are subsidized, or prices are regulated, by the government. A comprehensive 2018 study found that, at that time, more than 70% of emerging market countries regulated the prices of food and beverages (and more than 80% imposed price controls on energy products).[15]

Although often politically popular, such price control regimes make the government, in effect, responsible for the price of bread (or energy). When global prices rise, the government faces an uncomfortable dilemma: to let the domestic prices that the government controls rise as well, which may create political grievances and provoke demonstrations, or to attempt to hold domestic prices constant, often by applying an expensive subsidy, which could threaten to push the country into bankruptcy.

One of the most extreme cases is Egypt. Egypt maintains a generous subsidy regime for bread (and historically did so for fuel as well), providing food subsidies to nearly 70% of the population. Egypt is also the world's largest importer of wheat. The combination of subsidies and imports can be dangerous. Food and fuel subsidies have historically consumed about 10% of the Egyptian government budget. When global commodity prices are high, as they were on the eve of the Arab Spring, that figure can rise to 40% – threatening to bankrupt the country.

Egyptian governments, however, know that they cut the program at their peril. Protests against efforts to cut the bread subsidy contributed to the Arab Spring uprising. In the late 1970s, when global food prices were high, an attempt by the Egyptian government to cut the subsidy provoked the so-called "bread intifada" – three days of rioting in which some 800 people died in clashes with the police – until the Egyptian government backed down and restored the subsidy program.

In sum, the above analysis suggests that a crucial link between high global food prices and social unrest is the existence of subsidy programs, or price controls, which make governments responsible for the price of food. Similarly, the link between high fuel prices and unrest, such as in Sri Lanka in 2022, related to the existence of subsidy programs for energy.

Looking specifically at fuel, a World Bank paper found that government efforts to control fuel prices tended to backfire, leading to larger price jumps than in markets where the fuel price was unregulated. These large price jumps may further provoke the public's ire.[16]

Constructing a risk index

What countries might be most at risk for instability during a global food crisis? As an illustration, we here construct a simple vulnerability index. The index is calculated by taking a set of statistical indicators and a normalizing these indicators onto a zero to one scale. The indicators are then combined and averaged to produce an overall score.

Because the Ukraine conflict resulted in both elevated food and fuel prices, and because the risk drivers for each of these separate factors are very similar, we include both food and fuel price vulnerability in the index.

The purpose of the index is not to provide a precise prediction on which countries may suffer social unrest (at present, the factors in the index are unweighted and thus the predictive power is likely to be low). Rather, the index attempts to make explicit the elements that may link high food prices to social unrest, so that any country of concern can be evaluated for the presence of such elements.

The factors in the index are:

- **Food and fuel subsidies.** Unfortunately, it is difficult to obtain direct data on the most important factor – the existence of food and fuel subsidies. Hence we rely on an indirect indicator: the price of bread at the store, and the price of gasoline at the pump, on a US dollar basis. Countries that have very low prices, by international standards, are likely to be those that subsidize (especially if those countries import these products and thus must pay world market prices).
- **Imports of food or fuel as a percentage of consumption** (also called "import dependence"). A government that both subsidies food, and relies on imports of food, is particularly vulnerable to unrest, because that government must decide whether to offset high global prices with additional subsidies or be held responsible when local prices rise.
- **Fiscal sustainability.** In general, we might expect that professional politicians would be well aware that if they remove subsidies they run the risk of triggering unrest. Indeed, it appears that many governments would prefer to face the risk of bankruptcy rather than reduce subsidies (as Pakistan, Egypt and Ghana elected to do during the 2022 food, fuel and fertilizer price shock). Hence, in most cases, only those governments facing immediate debt crises are likely to opt to remove subsidies. The index therefore includes indicators of debt sustainability.
- **People power indicators.** As has been mentioned above, social unrest is more likely to occur when people feel that their political actions are likely to be effective. In general, people that have a higher level of income, more education, and greater access to new communications technologies tend to be more politically effective.[17] An urban population can also mobilize in protest faster, is usually closer to centers of power, and generally has fewer people working in agriculture. Indicators of income, education, urbanization and mobile phone penetration are therefore included in the index.

Index results

Results for the top twenty countries in the index are presented below (the index is calculated for 93 countries, with Australia and Norway indicated as least likely to experience turmoil).

Both Egypt and Sri Lanka, which have experienced political and economic instability in the wake of the conflict in Ukraine, appear among the top five countries. Pakistan, another country facing current challenges, does not appear, because of missing data (countries with missing data are excluded from the results). If Pakistan is assumed to have the worst possible score on its fiscal position it would rank about 11th in the index. Pakistan's relatively lower levels of income, education, and urbanization would appear (according to the index) to make the country less likely to experience a "people power" uprising than Sri Lanka or Egypt.

In September and October of 2022, Haiti experienced widespread unrest after the government removed fuel subsidies. Haiti is also excluded due to missing data, but if the missing factors are imputed would rank 10th. One reason fuel subsidies are so sensitive is that these subsidies tend to benefit well-off users who own vehicles and have more "people power" (although other groups can also benefit, such as those who use fuel oil for cooking).

Are there important factors not included in the index? Certainly. One such is democracy, an ambiguous factor. Countries that are more authoritarian may be more likely to suppress demonstrations and therefore less likely to experience unrest (a statistical pattern borne out by the differing experiences of Sri Lanka and Egypt during the spring of 2022). At the same time, countries that are more authoritarian are more likely to experience situations where citizens, lacking other channels for discontent, take to the streets to topple a regime (as was the case, for instance, during the Arab Spring). For example, one study of Arab Spring unrest found that "a change in food access motivated protest and violence involving existing grievances rather than explicitly addressing food access. In this way, food changed the meaning and severity of existing grievances." [18]

Two perhaps surprising countries to appear in the top 20 are Malaysia and India. While Malaysia's well-off citizens should have a lot of 'people power', the country's fiscal position is not yet in crisis, giving the government room to maneuver. Over the summer of 2022, the Malaysian government discussed cuts to energy subsidies, but also offered reassurances that ample funds remain available to keep domestic prices down. India is also in a better fiscal position than most of the top 20 countries and has provided free food grains to some 800 million people during the crisis.

The concern has often been raised that high energy prices will lead to social unrest in Europe. According to the index, is that risk realistic? The highest-ranked Western European country in the index is Portugal, ranked 43rd, followed by the Netherlands, ranked 55th. Certainly, citizens of Western Europe are amply supplied with "people power," and many Western European nations import both food and fuel. However, most Western European countries do not subsidize consumer prices of food or fuel, and hence citizens are unlikely to hold their government responsible when prices rise. These countries also tend to have relatively strong fiscal positions.

That said, Germany has recently demonstrated its strong fiscal position by announcing a €200 billion program of energy consumption subsidies. While perhaps appealing to voters, the history of food and fuel price unrest suggests that such programs can be a double-edged sword, as they make governments directly responsible for the consumer price of energy, and thus possibly a target of the considerable pressure a mobilized public can muster.

WTW Food and Fuel Price Shock Index

			Food and fuel subsidies		Import dependence		Budgetary pressure		People Power			
Rank (1 = worst)	**Country**	**Score (1 = worst)**	**Fuel price**	**Bread price**	**Energy imports**	**Cereal imports**	**External finance**	**Debt interest**	**Ave income**	**Literacy**	**Mobile phones**	**Urbanization**
1	Egypt	0.78	Very high	Very high	High	High	Medium	Very high	Medium	Low	Very high	Low
2	Mozambique	0.77	Very high	Very high	Medium	Very high	Very high	High	Low	Low	Low	Low
3	Sri Lanka	0.77	High	Very high	Very high	High	High	Very high	Medium	High	Very high	Low
4	Malaysia	0.76	Very high	Very high	High	Very high	Medium	High	High	Very high	Very high	Very high
5	Georgia	0.76	Very high	Very high	Very high	Very high	High	Medium	Medium	Very high	Very high	Medium
6	Armenia	0.75	Very high	Very high	Very high	High	High	High	Medium	Very high	Very high	High
7	Dominican Republic	0.74	Medium	Medium	Very high	Very high	Very high	Very high	Medium	Very high	Medium	Very high
8	Tunisia	0.72	Very high	Very high	Very high	Very high	High	Medium	Low	Medium	Very high	High
9	Kenya	0.70	High	Very high	High	High	Medium	Very high	Low	Medium	Very high	Low
10	Jamaica	0.70	Medium	Medium	Very high	Very high	Medium	Very high	Low	High	Very high	Medium
11	Belarus	0.69	Very high	Very high	Very high	Medium	High	Medium	Medium	Very high	Very high	Very high
12	Botswana	0.68	Very high	High	Very high	Very high	High	Low	Medium	High	Very high	High
13	Namibia	0.68	Very high	High	Very high	Very high	Medium	High	Low	High	Very high	Medium
14	Panama	0.67	Very high	Medium	Very high	Very high	Medium	High	High	Very high	Very high	High
15	India	0.67	High	Very high	High	Medium	Medium	Very high	Low	Low	Medium	Low
16	Mauritius	0.65	Medium	High	Very high	Very high	Medium	Medium	Medium	High	Very high	Low
17	Philippines	0.64	High	Very high	Very high	High	Medium	High	Low	Very high	Very high	Low
18	Morocco	0.63	Medium	High	Very high	Very high	Medium	High	Low	Low	Very high	High
19	Myanmar	0.63	Very high	Very high	Medium	Medium	Medium	High	Low	Low	Very high	Low
20	Mexico	0.63	Very high	Medium	High	High	Medium	Very high	Medium	Very high	Very high	Very high

Very high   High   Medium   Low

SOURCES: World Bank, International Monetary Fund, Globalpetrolprices.com, Nationmaster.com, WTW calculations

How will EU rules reshape the global food supply chain?

When one thinks of 'food nationalism' one may think of, for instance, the countries that put in place export restrictions during the global food crisis. But several panellists mentioned ambitious new European Union rules that could lead to divergence in products and practices between the EU and its major trading partners. In this callout, an Oxford Analytica contributor summarizes their views on the politics of the new EU measures.

The story so far

The EU's Green Deal[19] aims to transform the EU into a "resource efficient and competitive economy." While a central concern of the Deal is to drive the EU towards net zero by 2050, the Deal also includes a Farm to Fork Strategy[20] that aims to address a wider range of sustainability questions including agriculture and food supply. This strategy seeks to foster a sustainable food system which would have a neutral or positive environmental impact, mitigate climate change, reverse biodiversity losses, ensure food security and access to safe and nutritious food and promote fair trade.

The core objectives of the strategy include:

- A 20% reduction in the use of chemical fertilisers
- A 50% reduction in use of chemical and the most hazardous pesticides
- A 50% reduction in the sales of antimicrobials for farmed animals and in aquaculture
- Mandatory front of pack nutrition information and a sustainable food labelling framework
- A 50% reduction in per capita food waste at retail and consumer levels

With these goals in mind the Commission has set out a package of legislation to be introduced in 2023 including:

- Revision of existing legislation on pesticides, animal welfare, feed additives and date marking
- Harmonisation of front of pack nutrition labelling
- EU-level targets for food waste reduction

In other areas (e.g., fertiliser reduction) the Commission aims to use existing legislation and policies as well as closer cooperation with member states through the Strategic Plans which are part of the new Common Agricultural Policy (CAP) and which are currently under review by the Commission.

Reactions to the Farm to Fork Strategy have been mixed. Animal welfare, environmental groups and some farming groups have been broadly supportive. However, the main farming organisations as well as the fertiliser and pesticide industries have been more sceptical and critical. A number of assessments of the strategy (including one prepared for the Commission) have indicated that while the strategy may have a number of beneficial impacts (e.g., on environmental impacts and public health), it will lead to a reduction in food production in the EU and "carbon leakage" as the gap is filled by imports from producing countries where standards are lower.

The debate over Farm to Fork has shifted following the escalation of the conflict in Ukraine and the resulting disruption to global food and fertiliser supplies. Critics have argued the disruption necessitates a suspension and re-examination of the Strategy with the French President calling for the EU to develop a food autonomy strategy instead. Even the Agriculture Commissioner indicated that some rethink might be required (though subsequently he reiterated his support for the strategy).

In response to these developments, measures which were to have been introduced in early 2022 were postponed and some existing requirements (e.g., controls on some animal feed imports and rules on fallow land) were suspended with the aim of increasing EU agriculture output. The Commission also published a review of food security earlier in the year. While this identified a number of short-term measures to combat the disruptive effects of the global food crisis, it reiterated its support for the broad principles of the Farm to Fork, arguing that the transition to a more sustainable agriculture and food system will enhance food security.

First measures

Thus the first measures on Farm to Fork have been put forward by the Commission over the last few months and more are to follow.

Pesticides Revision: The Commission is proposing to revise the pesticides control regime to set legally binding targets at the EU and member state levels. While the legislative proposal, published earlier in the summer, only sets out the overall target of reducing by 50 percent the use of chemical and more hazardous pesticides by 2030, there will be individual targets for member states depending on their current usage and their existing efforts to reduce usage. The legislation also proposes a ban on the use of all pesticides in environmentally sensitive areas.

Animal Welfare: The European Food Safety Authority is embarking on the publication of scientific opinions on animal welfare which will provide detailed recommendations on how to improve conditions in which animals are bred and reared. These opinions will inform new legislation on animal welfare to be presented by the Commission next year.

Food labelling: Another strand of the Farm to Fork Strategy addresses consumer-focused initiatives to promote healthy and sustainable food choices and to reduce food waste. The first significant measure in this regard will be a forthcoming proposal to harmonise the way in which nutrition labelling is presented on the front of food packaging. While draft legislation has yet to be made public, there have been reports that the Commission would follow the system in place in a number of member states – Nutriscore – which ranks foods according to their nutritional quality, which in turn is based on a mix of positive (protein and fibre content) and negative (fats, sugars and sodium content) criteria. However, the system is rejected by a number of member states, notably Italy, who argue that it favours some diets at the expense of others. These disagreements mean that the Commission has backed away from a mandating a single type of labelling while still encouraging greater harmonisation.

Global impacts

While Farm to Fork is likely to remain the principal source of regulations shaping the EU's food supply chains, other areas of EU policy also have an impact. This is particularly true of the EU's trade policy which has become increasingly informed by a wider range of concerns including environmental protection and climate change. Indeed, as the Farm to Fork strategy is rolled out it is likely to inform the EU's negotiations with its trade partners. There are plans to introduce so-called "mirror clauses" into trade agreements. These would require that imported food and other agricultural products meet broadly equivalent welfare and environmental standards to those prevailing within the EU.

Building on increasing concerns about the standards followed in exporting countries, the EU plans to act on concerns that its consumption of certain commodities impacts on deforestation and forest degradation in the countries supplying those materials. The Commission has proposed legislation to promote the use of deforestation-free products. The draft Regulation would set mandatory due-diligence rules for operators supplying those commodities (soy, beef, palm oil, wood, cocoa and coffee) to ensure their traceability and thereby ensure that only materials cultivated sustainably (i.e., without contributing to further deforestation) would be imported into the EU. The rules would apply to both legal and illegal deforestation activities.

Political impacts

While Farm to Fork has been politically contentious, so far this contention has mainly been manifesting in policy debates and lobbying activities. As the policy pipeline generates explicit legislative proposals, the measures may increasingly impact electoral outcomes and provoke reactions from social movements.

Just how contentious such proposals may prove to be was recently demonstrated by a dispute between farmers and authorities in the Netherlands. The source of the controversy predates Farm to Fork, but ultimately overlap with the new strategy's goal of cutting fertiliser use and tackling excess nutrients.

Following EU and national court rulings, which found against the government's system for overseeing nitrogen emissions and for permitting new construction and agricultural activities, the Dutch government has been trying to develop a new strategy for cutting such emissions. At the end of 2021, it produced a plan to spend 25 billion euros in cutting the country's livestock numbers by switching to less intensive agricultural activities or relocating these activities. These plans were followed in June by targets for pollution reduction of up to 70 percent by 2030.

In response to these proposals, Dutch farmers have engaged in a series of demonstrations and protests. Although some of the protests have been disruptive and even violent, the farmers have enjoyed considerable public support within the country as reflected in growing support for a new centre-right party, BBB (BoerBurgerBeweging). While BBB secured one seat in the 2021 general election shortly after its formation, it is currently enjoying remarkable support as the second most popular party in recent polls, indicating support well beyond the communities immediately affected by the agricultural proposals. At the same time populist movements both in and outside of the Netherlands have sought to capitalise on the crisis. Provincial elections are due to take place in 2023 and a shift towards the BBB could, in theory, disrupt the work of the government, given that the Senate can reject legislation.

Elsewhere in Europe there has been a revival of agriculture-related protests though not on the same scale as those seen in the Netherlands. Generally, the motivations for those protests are different. However, it is possible that as Farm to Fork measures call into question established farming practices and lifestyle choices, the tension between agricultural productivity and sustainability might become more politicized, particularly if populist movements are able to exploit the issue as part of a climate-sceptic agenda that many of them follow. This in turn might translate into food and farming issues becoming a contentious issue in the 2024 European Parliament elections.

CALLOUT 5

The increasing geopolitics of food security – what's the beef?

Laura Burns
Political Risk Product Leader, Americas

"Control oil and you control nations, control food and you control the people," so goes the historical quote commonly attributed to Henry Kissinger. But as food security continues to be under enormous pressure, might food increasingly control both people and nations? If so, how might affected multinational companies (MNCs) operating in this sector manage the geopolitical risks?

As a recent geopolitical risk commentator stated, "Food is the essence of geopolitics. There is no more basic human need than securing access to food and water and, as a result, there is no more important geopolitical imperative for national governments than to ensure their people do not starve. A government that fails to provide food security will not stand long."[21]

Further, Henry Kissinger stated, "We must begin here with the challenge of food.... A generation ago many farmers were self- sufficient; today fuel, fertilizer, capital and technology is [are] essential for their economic survival."[22] That quote is from an address he gave 1974, arguably before the next boom of globalization of the 1980s-2000's. What should we infer about the economic pressures facing farmers, today?

As this report highlights, in the wake of the Ukraine/Russia crisis, in which one of the world's largest breadbaskets has been severely disrupted, there is ongoing concern over the geopolitical ripple effects of food scarcity and/or price increases.

The Black Sea Grain Initiative (the deal between Ukraine, Russia, brokered by Turkey to allow grain to exit through the Black Sea) was thankfully renewed November 17 for a further 120 days. However, the exports of existing grain play only a supporting role in the story of global food security. Looking to the horizon, it is the coming harvests that are of concern. The planted area of winter barley shrank by 35% and the UkrAgroConsult are already predicting a reduction in the corn area for the 2023 harvest. The extent of this reduction will be determined by the behavior of the domestic prices in the coming 2-3 months[23]. Other issues such as fuel and fertilizer shortages, supplier credit, war-torn farmlands with supplies of labor impacted by conscription, and compromised transit corridors are adding to the problem. Meanwhile, other global breadbaskets being affected by drought and flood is compounding the issue.

Furthermore, the disruption regarding the ability of farmers around the world to obtain Russian fertilizer and its components, such as ammonia, due to perceptions or interpretations of sanctions and/or banking struggles, will likely compound the food crisis well into the future. Peru has already seen protests from its farmers earlier this year while Brazil imports more than a quarter of its fertilizer from Russia, which is leading to difficulties in the region.

Today, particularly after the COVID-19 pandemic and the rise of populism in many countries, many governments have become increasingly protectionist about retaining certain commodities for their own consumption. This means some countries may not permit certain exports or, in extreme conditions, may seize stocks. Anti-Western sentiment could lead to damage of MNC facilities potentially viewed as contributing or profiting from a crisis. Countries plunged further into debt from increased food and fertilizer costs from subsidies may impose currency controls. Supply chains too may be affected, causing cancelled contacts and/or extra expense from having to substitute a commodity from another supplier.

How might geopolitical challenges impact MNCs?

We consider three hypothetical future scenarios. These are not intended to refer to any specific company or historical event but illustrate potential impact on MNCs of ongoing geopolitical challenges and where political risk insurance could help mitigate the financial losses:

Government disputes leads to significant financial damages for commodity trader

A Western multinational commodity trader has substantial stocks of grain, fertilizer, and sugar stored in third-party warehouses globally, with a focus on the Middle East and Africa. The protracted crisis in Ukraine together with the compounding effect of drought in other breadbasket countries that leaves them unable to soften the global impact, results in a continued surge in prices for grain and scarcity of product. An outpouring of negative public sentiment ensues in a particular country, with calls for the government to 'do something' about the food crisis before more citizens fall into poverty as a result. To curb growing resentment toward the government policy, or lack thereof, the government prohibits the export of any grain from its ports to the next intended destination. A dispute ensues during which time the commodity trader's grain stocks rot in their silos. The population becomes increasingly hostile towards the government for not managing the process better, so to stave off mounting pressure, the government then seizes a grain silo's contents 'for the people'. The financial damages sum incurred is more than $85M which includes the value of the rotted goods during the dispute due to the inability to export, as well as the value of the goods seized.

Currency controls create trapped cash for multinational food company

A Western multinational corporation packaged food company has a substantial and profitable subsidiary operating in several countries, with a particular Sub-Saharan African country being one of recent continued growth. Given the food price shocks felt in the country, unrest has broken out, with demands on the government to provide food subsidies. Facing mounting pressure, the government obliges but the unrest has caused capital flight and plunged the government into a foreign reserve crisis. It passes currency controls prohibiting any corporation from transferring any local or hard currency out of the country. The financial damages incurred are roughly $65 million in trapped cash made up of declared dividends, royalties, and intercompany loan repayments over a six-month period.

Coup compromises pre-export finance program

A Western commodity trading company has a very profitable and effective pre-export finance program with farmers in a West African country. It supplies financing to enable the farmer to purchase seeds, fertilizer, and the like, in exchange for the crop yield when it is harvested. However, due to a coup d'état and an ensuing civil war within the country, the crop cannot be received and in turn, the farmer is unable to prepay the loan advance as stipulated. The financial result is a $50 million loss.

Paramount in this risk and market environment is the importance of both framing the risk to underwriters and the strategic structuring of a program.

Insuring food and beverage risks in the political risk insurance market

Political risk insurance was born out of the post-WWII era as a tool for governments to promote a return to cross-border trade and investment by insuring the political and credit perils investors confronted. Today the market is robust and dynamic, able to support c.$3 billion of capacity per insured program through close to sixty private markets, multilaterals and many export credit agencies (ECAs).

Premiums are based on the rate-online multiplied by the limit per layer. Those rates generally range from 0.30%-3.00%. Policies are multi-year, with a key benefit of coverage being the policy is non-cancellable and rate-guaranteed by the insurance company, even in cases where the risk situation deteriorates within the multi-year policy period.

Many commodity traders and food and beverage companies already utilize this market for substantial political risk insurance programs and therefore have the capacity and terms 'grandfathered in' for the life of their multi-year policy.

Several have been supported with claims with respect to the Russia/Ukraine crisis in the form of seized assets, property damage to facilities, the need to abandon assets due to the security situation, and currency inconvertibility out of Russia.

For new potential insureds coming to market, there may be some challenges related to obtaining large amounts of capacity for very sensitive commodities in key import-dependent and low-income countries. They may also face increasing challenges around raising support for multi-country programs. However, for most risks, the market generally remains open and affordable, with plentiful capacity at the time of writing. That said, these market conditions could change as geopolitical tensions in the sector potentially escalate. We therefore advise global companies take a proactive approach in their political risk management and consider political risk insurance with urgency as these risks will likely continue to increase. This means market capacity will likely continue to shrink and rates trend upwards.

Paramount in this risk and market environment is the importance of both framing the risk to underwriters and the strategic structuring of a program. Working with a strong specialist broker in political risk insurance can help ensure the nuances of the investment or mobile stocks and bespoke coverage needs will be captured in the terms and conditions of an optimized insurance program or other risk management vehicle.

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