

**Box 6.1**

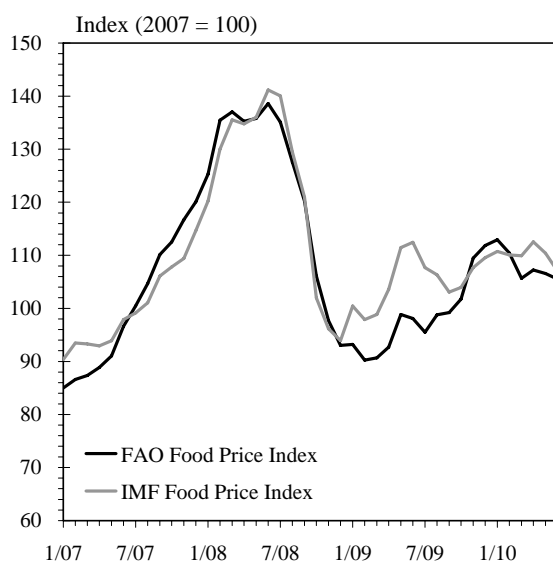
**Recent movements of global food and fuel prices**

With the global economy struck by the “Great Recession” in 2008-09 followed by the subsequent recovery, global food and fuel prices also showed much volatility over the period. Given that the movements of these prices bear implications on the relevant consumer prices in Hong Kong, a survey on their recent movements can be indicative of the likely price pressure in Hong Kong from these sources in the near term.

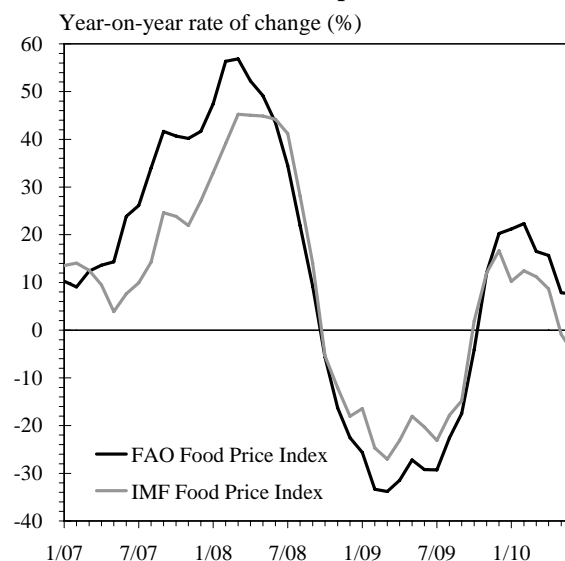
**Charts 1(a) and (b)** illustrate the movements of global food prices since January 2007, as indicated by the relevant indices compiled by the International Monetary Fund (IMF) and the Food and Agriculture Organization of the United Nations (FAO). Food prices rose sharply during 2007 and the first half of 2008 upon a spate of supply and demand factors (see **Box 6.1 of Half-yearly Quarter Economic Report 2008**), but retreated to levels comparable to that in early 2007 towards end-2008 as the global financial crisis struck. Then, as the free-fall in the global economy was arrested in early 2009, food prices began to bottom out. Since then, global food prices rebounded notably amid some fluctuations over the course of 2009, alongside the global recovery. However, global food prices turned more stable on entering 2010. As in June 2010, global food prices were still around 24% lower than the peak in mid-2008. According to the FAO<sup>(1)</sup>, the main contributory factor for the relatively stable global food prices in overall terms in recent months was from the supply side, as the earlier rally in prices spurred agricultural production, resulting in a recovery in inventories. Yet due to successive rise-back during 2009, in the first half of 2010 global food prices were on average around 15% higher than in the same period last year.

**Chart 1: After the rally of food prices, the international food market slowly returned to balance since late-2009**

**(a) FAO and IMF food price index**



**(b) Year-on-year rate of change of FAO and IMF food price index**



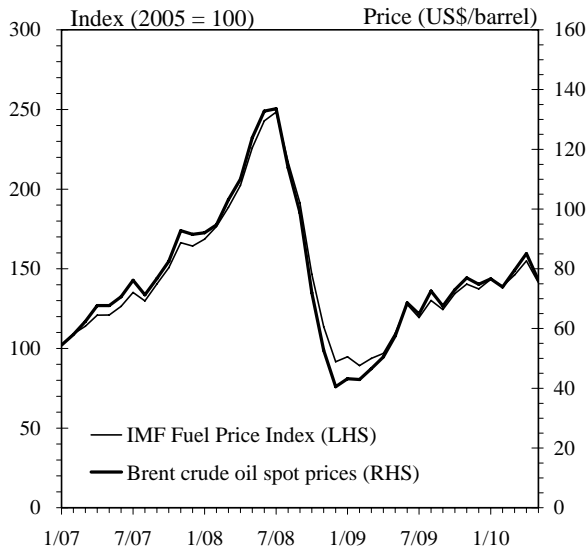
(1) Food Outlook, Global Market Analysis (June 2010 issue), FAO

**Box 6.1 (Cont'd)**

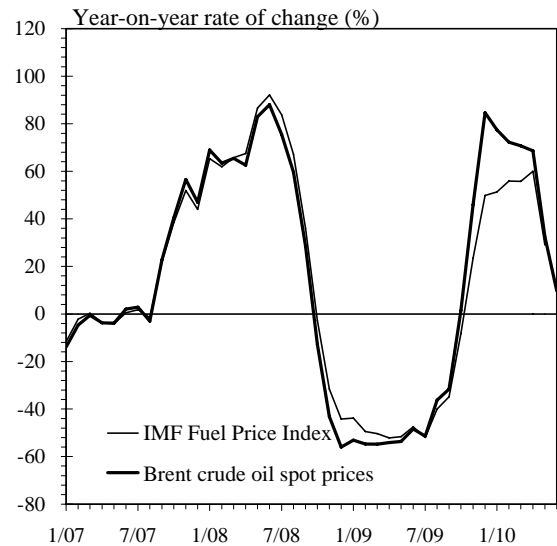
The movements of fuel prices in the international markets showed a similar pattern in recent years, as shown in **Charts 2(a) and (b)**. For example, Brent crude oil price, after reaching the historical peak in July 2008, averaging at around US\$134 per barrel in that month, it experienced a sharp decline of over 70% towards the end of 2008 amid the global financial crisis. After languishing at around US\$40 per barrel in late 2008 and early 2009, it rose back and moved within a narrow range of around US\$70-80 per barrel in the past several months. The gradual recovery in industrial production activities and the general improvement in financial market sentiments since the second quarter of 2009 were the factors driving the bounce-back in crude oil prices.

**Chart 2: Fuel prices bottomed out since early 2009, mainly the result of recovery of industrial production and improved market sentiments**

**(a) IMF fuel price index and Brent crude oil spot prices**



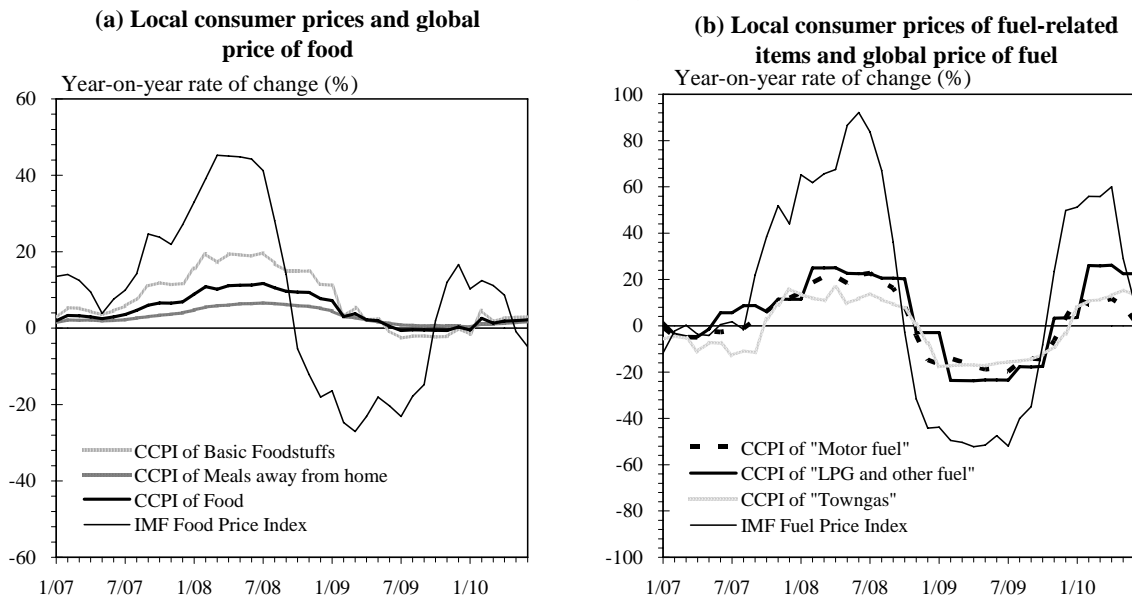
**(b) Year-on-year rate of change of IMF fuel price index and Brent crude oil spot prices**



**Box 6.1 (Cont'd)**

As shown in **Charts 3(a) and (b)**, local retail prices of both food and fuel-related items generally moved broadly in line with their counterparts in the global markets, though with a notably smaller degree of volatility. This is because local retail prices also depend on such factors as local wage, rental and other business cost movements.

**Chart 3: The movements of local retail prices of food and oil-related products generally followed the movements of global food and oil prices, yet with a much lower degree of volatility**



Generally speaking, because food items account for a large share of household spending, large fluctuations in food prices can have a rather noticeable impact on local consumer price inflation, as in 2007 and 2008. By contrast, oil-related items account for only a small share of household spending. This, together with the fact that Hong Kong is not an oil-dependent economy, suggests that local consumer price inflation is less susceptible to oil price fluctuations. Although global food and oil prices have held relative stable in overall terms in recent months, they can turn more volatile in the period ahead, considering the high degree of uncertainty surrounding the global economic outlook and the volatile nature of these prices. In case of food prices, the adverse weather conditions and exchange rate movements in the key supplier economies can also cause upward price pressures. Therefore the upside risk to local consumer price inflation from these sources need to be monitored closely.