Box 7.1

Recent movements of prices of food and oil in the international markets

International commodity prices are well-known to be volatile, as they are easily thrown off balance by such factors as the ebb and flow of world demand, abrupt disruptions to supply conditions, and global liquidity. Among the various commodity prices, those of food and, to a lesser extent, oil have the strongest direct bearing on Hong Kong’s inflation. Indeed, the fluctuations of food and oil prices in the international markets have been highly notable in recent years.

Recent trend of global food prices

According to the Food Price Index compiled by the Food and Agriculture Organization (FAO) of the United Nations, global food prices embarked on a general uptrend between early 2006 and mid-2008 (Chart 1). After peaking out in June 2008, global food prices tumbled and drifted 37% lower by February 2009, as the global economy underwent a drastic downturn subsequent to the outbreak of the global financial tsunami. Yet alongside the worldwide economic recovery and the occurrence of a number of supply-side shocks, global food prices bounced back briskly thereafter by 68% to a historic peak in February 2011, before retreating more visibly in the latter part of 2011. Yet, for 2011 as a whole, global food prices were still on average 23% higher compared with 2010.

Based on the analysis of the FAO, in spite of improved production prospects and a slowing demand, the overall demand/supply balance of the agricultural commodity market remained tight up till late 2011. Looking ahead, the movements of global food prices will continue to hinge on the relative shifts of factors that affect the demand and supply situation. Apart from a highly uncertain global economic outlook, gyrations in the financial and equity markets, and fluctuations in exchange rates and in the energy markets would also add to sharp price swings in the agriculture markets.
Box 7.1 (Cont’d)

Recent trend of international oil prices

The movements of oil prices in the international markets have exhibited a similar pattern in recent years (Chart 2). Taking the monthly average of the spot price of North Sea Brent Oil as an indicator, the oil price hit an all-time monthly record high at US$133.6 per barrel in July 2008, before plummeting by nearly 70% to US$40.3 per barrel in December 2008. Against the backdrops of global economic rebound and liquidity glut, as well as a series of supply shocks stemming from the wide-spread political unrest in the Middle East and North Africa (MENA) region, the Brent crude oil price kicked off a renewed rally, hitting a recent monthly peak of US$123.3 per barrel in April 2011, before easing somewhat to US$108.3 per barrel in December 2011.

According to the analysis of the International Energy Agency (IEA), the modest decline of crude oil prices recently could be partly attributed to the deepening eurozone sovereign debt crisis, rising output from Libya and recovery in North Sea supplies. However, the still-evolving political turmoil in the MENA region where many major oil exporting countries locate, if re-aggravated, could spur further price swings in the oil markets.

All in all, as the global economy is facing an unusually high level of uncertainty, and as the expected continuation of abundant global liquidity may add to financial and currency market gyrations, food and oil prices are more likely than not to observe pronounced fluctuations in the near future. As a small and open economy, Hong Kong is highly dependent on the imports from overseas, particularly foodstuffs and fuels, and is hence highly susceptible to the ups and downs of global food and oil prices. Indeed, the radical price swings of foodstuffs and oil products in the international markets have been one of the key ingredients in driving the rise and fall of inflation over the past few years in many economies across the globe, including the Mainland and many emerging Asian economies. Given all the uncertainties hanging over the food and oil markets, we will continue to closely monitor the movements of global food and oil prices, and their possible impacts on the inflation in Hong Kong.