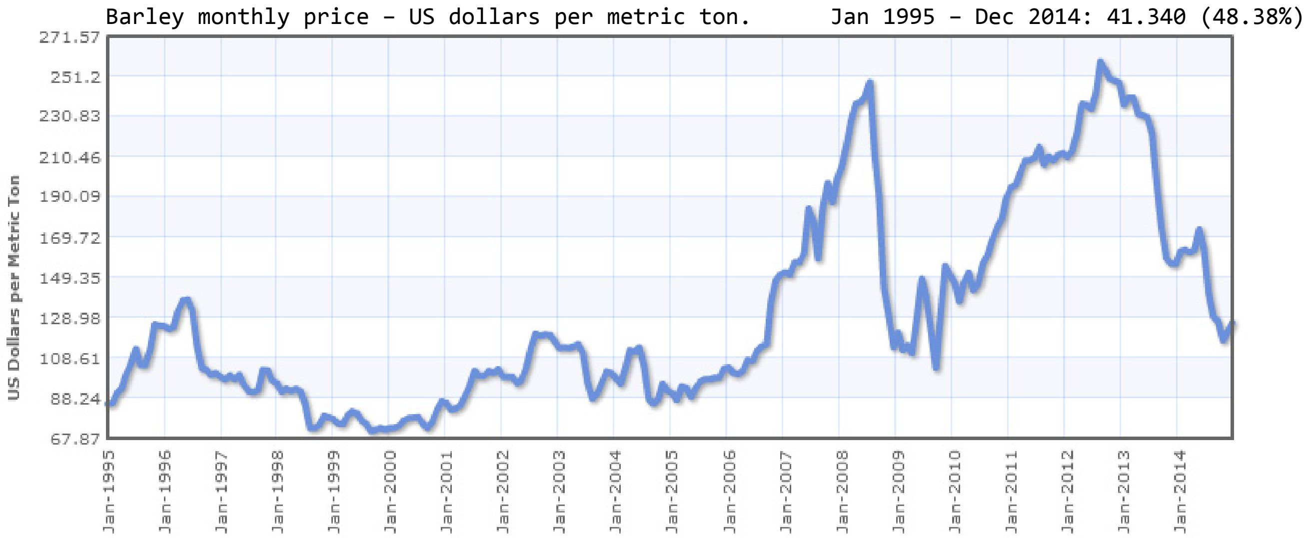
Price volatility

The aim here is to try to work out why the prices of agricultural and other primary goods are so volatile. Start by showing this chart and maybe a few others from the list on the left in the following link, looking over a 20–30 year period.

http://www.indexmundi.com/commodities/?commodity=barley&months=240

Divide the students into pairs and ask them to come up with possible reasons for this variation. They will probably come up with supply volatility, a few might also think about low PED and PES.



Now show the students the following clips. After each one, ask them to draw (in pairs) a supply and demand diagram trying to explain what they think might be going on.

Coffee

http://www.bbc.co.uk/news/world-latin-america-27600562

In this case, the drought is the big issue, so they will have drawn supply curves shifting to the left. With a bit of luck, some will have drawn steeper demand curves than others, making the change in price greater. Hold up the relevant ones and ask the students which they think describes the situation the best (they will generally go for the low PED one). Ask them why they think that demand will be price inelastic for coffee (a simple explanation is that it's a necessity/addictive; a more complex explanation is that big processors/coffee chains have to get it or they are out of business.) This establishes the idea that the pairing of volatile supply and inelastic demand makes prices volatile.

Orange juice

http://www.bloomberg.com/news/videos/b/0eb39938-40c1-4ef9-b623-d5ecc18a8903

Watch the first 60 seconds of this video. In this case the big factor is falling demand (although careful students will also pick up that supply has fallen, but demand has fallen by more). Once they have had a go, you can get them to focus on the impact of changes in demand. Again, students should observe that if demand shifts, the impact on price will be much greater if supply is price inelastic. You can then use this as a reminder of PES and the factors that affect it as you get them to agree with one another why supply will be likely to be price inelastic.

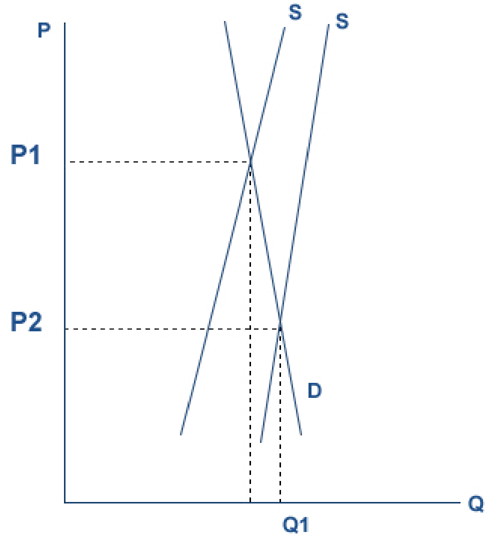
Chocfinger

http://news.bbc.co.uk/1/hi/programmes/newsnight/8836259.stm

Finally a neat video that highlights the role of speculators in commodity markets. In this case, the story is 'chocfinger' who is buying large quantities of cocoa in the hope of reselling when prices rise, although his own purchases are pushing prices higher. This reinforces the volatile demand idea from the orange juice clip.

The students should have two diagrams explaining primary product price variations:

1) Volatile supply and inelastic demand



2) Volatile demand and inelastic supply