FOOD INFLATION IN INDIA: PRESENT SCENARIO

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ABSTRACT

The rapid rise in food prices has been a burden on the poor in developing countries, including in India, who spend roughly half of their household incomes on food. In many countries and regions, food price inflation is higher than aggregate inflation and contributing to underlying inflationary pressures. Wholesale Price Index (WPI) which remained persistently high throughout 2011 due to increase in global commodity prices and high crude oil prices has started showing signs of moderation and it is expected to touch 6.5 to 7 percent during the financial year 2012. This paper examines the present inflationary scenario in the context of Indian economy and various factors responsible for it like weakening dollar, domestic infrastructure, and price stabilization policies. The paper also finds out the Lastly the paper argues that import of food items and execution of open market sale by the government will help to reduce inflation not only by bridging the supply gap, but also by reducing speculative buffering. It also suggests numerous options to contain inflation and to maintain overall price stability ahead. This paper spells out some plausible short-run steps that the government can take, without imposing much fiscal costs.

KEYWORDS: Consumer Price Index, Food Inflation, Private Consumption, Wholesale Price Index.

INTRODUCTION

Food inflation has become a major cause of concern for not only the common-man, but also for the policy makers. Of late, high inflationary, pressure particularly double digit food inflation since October 2008 is turning out to be a spoilsport in an otherwise robustly growing Indian economy. Food prices in India started increasing since mid-2008 onwards. The year 2010-11 witnessed overall inflation rate crossing 10% for the whole year. Inflation based on year-on-year wholesale price index (WPI) of primary food articles, still rules high at above 10% (in November 2011). Several factors like drought-induced shortages in food supply, rising international prices, various tiers in the value-chain are deemed to be the major reasons for food inflation in India. Greater government spending leading to increased money supply, structural changes in demand patterns, etc. are being cited as some other major reasons behind this high food inflation. Since November 2009, inflation has been moving northwards on the back of surging prices of fuel, commodity, fruits and vegetables. This consistently rising inflation has
resulted in a growing concern among policy makers, industry captains, bankers as well as the common man. During January, 2012, inflation shot through the roof of touch an 11 year high of 17.9%. The calendar year 2011 also saw inflation at a negative rate, ironically, food inflation roaring to its maximum level. The wholesale food prices in India touched a 10 year high with food inflation coming at 18.21% for the week ended March 25, 2012. This paper represents the inflationary scenario for overall food products during the year 2011-12 with the major causes, impact and measures taken by Indian government to contain food inflation.

WHOLESALE PRICE INDEX (WPI)
It was introduced in the year 1907, which is calculated on the basis of average rate of change in the wholesale market. A set of 435 commodities are used for wholesale price Index based inflation calculations. The base year for WPI calculation is 1993-94. It is available at the end of every week (generally Friday) for a period of one year.

The Government will adopt revised WPI besides considering actual prices. Instead of current 435 commodities, the revised WPI will have 980 commodities included in it. This will be rationalized by incorporating new items, removing unimportant items and amalgamating similar items. The base year will be revised to 2004-05 from the current base year of 1993-94. This new wholesale price index would give a more accurate figure for inflation.

CONSUMER PRICE INDEX (CPI)
The WPI based inflation rate, which is measured on point-to-point basis, is somewhat different from that of CPI based inflation. It is a statistical time series value based on the weighted average rate of change in prices of a set of goods and services purchased by consumer. CPI is more comprehensive and it catches the inflation value from the end consumer side rather than from wholesale side. CPI is based on monthly basis. India uses CPI, which most developed countries use CPI calculations for inflation rate.

Prices of set of 435 commodities especially Pulses, rice fruits and vegetable are used to calculate WPI in India. Economists say that India should adopt CPI for inflation calculation as it is the one that shows price rise that end consumers would experience. The finance minister counts it saying that in India there are four commodity price indices.

- CPI for Industrial workers
- CPI for urban non manual employees
- CPI for Agricultural laborers
- CPI for Rural laborers

In existence which makes switching over to CPI risky and complex and also CPI has too much time lag in reporting. CPI are the prices that people actually pay is fairly soft.

FOOD INFLATION IN INDIA: RECENT TRENDS
The table below gives the retail prices for some of the key agricultural commodities in four Indian metros. This is just to give an idea of how the prices have moved in the last one year.

Clearly, the prices of all key agricultural commodities have risen sharply. Significant price increase has been observed in commodities like, Onion, Vegetables and Fruits.
The key reason cited for the spiraling food price inflation is the bad monsoon in India. Monsoons have a major impact on the price levels in the country. The primary articles inflation originates in commodities whose production is affected by the monsoon like food or cash crops. June is a critical month for all, Government leaders, bureaucrats, economists, policy makers, industrialists, farmers and besides, millions of ordinary Indians. During this month, the south west monsoons usually set across the country bringing the much needed rains. Last year, monsoons set in on time, but its progress was halting by the time the season ended around September, the country had experienced one of the worst monsoons over the 35 years. Crops withered across the country and agricultural production suffered a setback with a loss of over 15 million tons of food grains. The Indian farmers are largely dependent on the four-month monsoon season during which 80% of the year's total rainfall takes place. The reason is that 60% of the country's total cropped area is not irrigated. The Government has again been talking about inclusive growth and stress on rural India. These facts don't point to any meaningful efforts to help farmers in a country where over 10,000 farmers have committed suicide over the last decade.

Table 1.1: Food Inflation for Select Commodities in 2011-12:

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Commodities</th>
<th>Inflation (Percentage)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Onions</td>
<td>74.15</td>
</tr>
<tr>
<td>2</td>
<td>Vegetables</td>
<td>65.39</td>
</tr>
<tr>
<td>3</td>
<td>Fruits</td>
<td>15.19</td>
</tr>
<tr>
<td>4</td>
<td>Milk</td>
<td>12.16</td>
</tr>
<tr>
<td>5</td>
<td>Eggs, Meat and Fish</td>
<td>12.04</td>
</tr>
<tr>
<td>6</td>
<td>Rice</td>
<td>02.86</td>
</tr>
<tr>
<td>7</td>
<td>Cereals</td>
<td>0.23</td>
</tr>
<tr>
<td>8</td>
<td>Potatoes</td>
<td>(-) 2.94</td>
</tr>
<tr>
<td>9</td>
<td>Wheat</td>
<td>(-) 6.11</td>
</tr>
</tbody>
</table>

Source: Self Compiled
Figure 1.1: Contribution to WPI Inflation by Major Groups:

Looking at the weighted contribution of major product groups to WPI inflation (figure 1.1), it can be noticed that the largest contribution is made by manufactured products i.e. 49 per cent while primary articles and fuel has contributed to Wholesale Price Index only by 28 per cent and 23 percent simultaneously during the year 2011-12.
The food price index consists of mainly two subcomponents, namely primary food articles and manufactured food products. The overall weight of the composite food index in the WPI is 24.31 per cent, (primary food articles: 14.34 per cent and manufactured food products: 9.97 per cent). The primary food article inflation has been a cause of serious concern for the economy during 2009-11. It remained at an average level of 16.75 per cent in 2010-11 and 15.27 per cent in 2009-10 (April-January) mainly due to surge in the prices of fruits & vegetables prices and protein-rich items such as milk, eggs, fish, and meat. However, in the current economic year average inflation in food articles has significantly declined to 7.15 per cent. This was mainly due to sizeable drop in fruits and vegetables prices, as a result of which inflation in these commodities has now turned negative in December 2011 and January 2012 (Table 1.2).
Figure 1.2: Weighted contribution of food Items to headline inflation:

Source: Economic Survey 2011-12

It is clear from the above figure 1.2 that the weighted contribution of food articles in headline inflation has shown a fluctuating trend continuously from January 2010 to January 2012. It was 10 percent in January 2010, declined up to 2 percent in May 2011 and again increased up to 10 percent in January 2012. Contribution of Eggs, meat and Fish is almost constant but the overall contribution of milk has declined and crossed zero and became negative during Dec’ 2011 to Jan’ 2012. The weighted contribution of food grains to headline inflation has decreased significantly from 10 percent in January 2010 to 3 percent in January 2012.

MAIN DRIVERS OF FOOD INFLATION

The major drivers of food inflation during the current financial year were milk, eggs/ meat/ fish, and edible oils. In comparison with last year when cereals, vegetables, and sugar were the main contributors to food inflation, 2011-12 witnessed higher contribution from manufactured food products especially edible oils due to higher global prices of soybean oil, palm oil, etc.

1. Capital Stock Deficiency: Capital stock deficiency tends to lead to bottlenecks, under which resource constraints, including limited infrastructure and lack of manufacturing capacity delay overall production or service generating processes which leads to higher inflation through shortages in supply. India’s capital stock-to-GDP ratio was 1.79 in 2010, among the lowest in Asia which is following the same trend in the year 2012 also.

2. Demand Side Drivers: Demand-side inflation drivers, especially those arising from a sharp rise in personal disposable income and an expansionary fiscal policy, have also played an important role in keeping inflation persistently high. As the credit policies are now liberalized
more money is injected into the economy which is increasing the purchasing power of the people the key reason to induce demand.

3. **Food Price Pressures**: Food price inflation has been a major driver of inflation during the year 2011-2012, because lack of rainfall during the monsoon season often hits India's food production. In addition, the structural change in food intake has significantly contributed to food price inflation in 2011-12.

4. **Import Price Pressures**: Import price pressures have also been an important factor for overall inflation as India has become a more open economy over the past 10 years. In fact, the imported goods-to-GDP ratio doubled from just above 11 percent in the financial year 2000-01 to 21.9 percent in Financial Year 2010-11 with bulk imports, such as crude oil, metals, rubber and food articles account for 42.7 percent of total imports.

5. **Inflation Expectations**: In the RBI's latest inflation expectations survey of households, respondents' inflation expectations for three months ahead inched up to 12.2 percent in the third quarter of 2011 from 11.8 percent in the second quarter. Overall, inflation expectations have been largely driven by food price inflation in India as food constitutes more than 50 percent of the average Indian household's consumption basket. WPI food inflation dropped from 20.2% in February 2010 to 1.6% in January 2012, calibrated steps initiated to rein-in inflation on top priority.

6. **Other Factors**: The food subsidy in India is poorly targeted. Many of the poor receive insignificant amounts of subsidy and depend on the market to access supplies. In spite of this, a reduction in the food subsidy is not in their interest as the reduction in subsidy increases the market price of food. The inefficient storage and mal-functioning of Public Distribution System has also led to inflation of food commodities.

### OPTIONS TO ENSURE PRICE STABILITY IN FOOD ITEMS

The per-hectare agricultural yield in India is half that of China. This again points of inefficiency and the failure to help the farmers adopt latest technology in order to increase the crop output. These things have not been taken care of in the past and even when discussed nothing substantial has been done in order to overcome these challenges. Steps are to be taken in the near future to ensure minimal food wastage, high crop productivity and increase in irrigated land. If the INR 58,000 crore of food crops is not wasted on an annual basis, India's deficits could be wiped out in less than a decade without any other measures being taken. However, looking into the very near term, some ways to ease food prices would be:

- Another major related issue is the strengthening of the supply chain so as to avoid wastage of perishable products. One suggestive measure in this regard could be the expeditious completion of the Agriculture Produce Marketing Committee (APMC) Acts reforms in different states so that enough flexibility is imparted to farmers to sell their produce. Further, it is important to develop a robust agricultural marketing system through adequate investment - domestic and/or foreign - so as to strengthen the back end infrastructure and reduce wastages.
- For promoting interstate trade, a commodity for which market fee has been paid once must not be subjected to subsequent market fee in other markets including that for transaction in other
Only user charges linked to services provided may be levied for subsequent transactions.

- Perishable food items could be taken out of ambit of the APMC Act. The Government regulatory markets sometimes prevent retailers from integrating their enterprises with those of farmers. In view of this perishable may have to be exempted from this regulation.

- To arrest the adverse impact of food inflation on the common man, the policy of the government should emphasis on the PDS, foreign trade policy, and distribution of essential commodities at below market prices through state public-sector units (PSUs), anti-hoarding operations, and strengthening of supply chain efficiency.

- As a strategy, regular imports of agriculture commodities in relatively smaller quantities with an upper ceiling on total quantity could be considered. The upper ceiling can be decided annually, relatively well in advance, after assessing the likely domestic situation in terms of production and consumption requirements.

- Extension programmes and guidance to farmers regarding fertilizer and insecticide uses an alternate cropping pattern based on soil analysis could be undertaken and intensified.

- In view of the relatively high weight of food in the CPI, agricultural shocks not only increase short-run inflation, but also can generate a sustained increase in the inflation rate if it raises inflationary expectations. As a consequence, India should endeavor to liberalize agriculture to reduce the volatility of food prices and such an endeavor is Evergreen Revolution.

- Any strategy for strengthening agricultural marketing needs to have a three-pronged objective: first, of providing remunerative prices to farmers; second, strengthening efficiencies of supply chain; and third, ensuring that end consumers are charged fair and reasonable prices.

- Setting up special markets for special crops in states/regions/areas producing those crops would facilitate supply of superior commodities to the consumers.

- Improved Mandi governance is an area of concern. A greater number of traders must be allowed as agents in markets. Anyone who gets better prices and terms outside the Agricultural Produce Marketing Committee (APMC) or its farm gate should be allowed to do so.

- Considering significant investment gaps in post harvest infrastructure of agriculture produce, organized trade and agriculture should be encouraged and the FDI in multi brand retail once implemented could be effectively leveraged towards this end.

- The Government should step up creation of modern stories facilities for food grains.

- Crackdown on hoarders and black marketers could help prevent prices from rising further. This step might not significantly reduce prices but will ensure that prices don't escalate further.

- The Government should allow the private sector to import and store the primary agricultural commodities at zero import duty. This will help ease the prices to a large extent.

- The Government also needs to unload the wheat inventory it has in its storage locations. This will have an immediate impact on the prices.
CONCLUSION

Maintaining low inflation and pushing growth in the short run is, however, often a knife-edge problem. The price of a good in a free market should be determined by its relative scarcity, i.e. supply relative to demand. But in a high-inflation environment, relative price shifts may not reflect underlying demand-supply conditions of different goods and services. As a result, dispersion in relative price increases lead to distortion in price signals. High inflation has adverse impact on growth through a variety of channels. First, high inflation leads to uncertainty which impacts investment and growth. As it is, investment decisions are subject to a lot of uncertainties. High and volatile inflation adds to these uncertainties. Second, high inflation results in movement of savings from financial assets to physical and other unproductive activities. Therefore, low and stable inflation is desirable from a number of perspectives. In that context, for monetary policy to be effective it is vital for central banks and macroeconomic policymakers to have reasonable forward-looking short-term forecasts of inflation on which to base decisions. The government monitors the price situation regularly as price stability remains high on its agenda. Measures taken to contain prices of essential commodities include selective ban on exports and futures trading in food grains, zero import duty on select food items, permitting import of pulses and sugar by PSUs, distribution of imported pulses and edible oils through the PDS, and release of higher quota of non-levy sugar. In addition, state governments are empowered to act against hoarders of food items by holding in abeyance the removal of restrictions on licensing, stock limits, and movement of food articles under the Essential Commodities Act 1955. The hike in policy rates by the RBI was due to persistently high inflation. The high rates, however, have impacted growth in the short run. There is need to examine the linkages and tradeoffs between policy rate changes and growth in the Indian context. Such understanding is important for better calibration of monetary policy both with respect to size and timing of rate changes. This is especially important since monetary policy primarily addresses demand-side factors relevant for inflation management whereas supply-side factors also play a key role in contributing to sustained increase in prices. Renewed attention to structural ways of improving medium-term supply responses in agriculture and supply chains and infrastructure more broadly may be vital. Moreover, The Evergreen Revolution of boosting food-grain output in India to 400 million tons in next 15 years is need of the day. Its achieving is not very difficult. Rather it is achievable if mindset on introducing newer technology is changed. India has to wholeheartedly embrace the new technology. Private sector is better suited to deliver results than government managed schemes. Governments on the other hand can play a key role in expediting irrigation schemes and managing water resources.
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