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FOOD INFLATION IN INDIA: CAUSES, CONSEQUENCES AND REMEDIES

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Abstract:

The rate of food inflation became a serious concern in India. The scenario of food inflation had turned in quite different way after 2008.In most of the months of 2008, rate of inflation remained close to or above 10% since mid 2008. This is causing a serious concern since expenditure on food accounts for more than 50% of total household expenditures in rural and 43% in urban areas. Household in lower income categories spend much higher percentage of their budget on food compared to the higher income groups. This indicates that food inflation hurts more than any other commodity group and low income consumers are affected much more than high-income consumers

The reasons for food inflation can be grouped into two different categories: those which are related to domestic economy and which follow from changes in global market. Since early 1990s, with the increase in liberalization of trade in agriculture, domestic food prices have been strongly influenced by international prices. Several other reasons also lie behind for high rate of food inflation. This paper seeks for those reasons the ways to manage food inflation, which can be checked in different possible ways.

Key Words: Food, Inflation, CPI, WPI, India

Introduction:

The panic of increase in food price threatened common people's life heavily during the last part of first decade of twenty first century and thereafter. After rising from bed, people found that prices of everyday articles have increased, especially, edible oils, pulses and sugar. That was a burdensome hindrance for the people who live by hand to mouth. However, Inflation refers to percentage change in the price of goods and services over a period. It represents change in the overall price level in the economy, say for a week or a month. If one says that inflation is coming down it does not mean that prices are coming down. It means that the rate of increase in prices was less. Inflation is

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basically of two types cost-push and demand-pull inflation. i) Demand- pull inflation refers to increase in the price level due to demand being in excess of supply in the short run, ii) Cost push inflation is due to autonomous increase in the cost components, including labour and material costs. There have been used different primary measures of inflation in India such as wholesale price index (WPI) and consumer price wholesale price index (CPI). Wholesale price index is defined as weighted price index of a good of baskets consisting of 435 commodities, which categories under three groups: i) Primary articles (98 commodities) ii) Fuel power, light and lubricants(19commodities) iii) Manufactured products (318 commodities). These three again divided into smaller sub-groups. Whereas, WPI is compiled on weekly basis.

Objectives of the Study:

1. To analyse causes of food Inflation in India.
2. To find out possible ways of controlling food Inflation in India.

Data and Methodology:

Here, we have taken secondary data, published by CSO, RBI and Ministry of Agriculture of India. In this article, we have applied WPI, CPI, Simple arithmetic logics & Graphs to analyse and interpretation of the data. Where:

$$\text{WPI} = (\text{Current Price}/\text{Base Period Price}) \times 100 \qquad (1)$$

On the other hand, consumer price index (CPI), that can be defined as price on baskets in current year to price of basket of base year. i.e

$$CPI = \left\{ {(CPI_t - CPI_{t-1})}/{CPI_{t-1}} \right\} \times 100 \qquad (2)$$

here CPI_t refers consumer price index of the current year, CPI_{t-1} refers consumer price index of the previous year and consumer price index reflects retail prices of goods.

Inflationary tendency of food inflation in India:

India is the only major country that uses a wholesale index to measure inflation, where most countries use the CPI as a measure of inflation, that ultimately the consumer have to pay for. However, as per classical economic theory a small dose of inflation is good for a growing economy as it has multiplier effect on economic growth. Therefore, in

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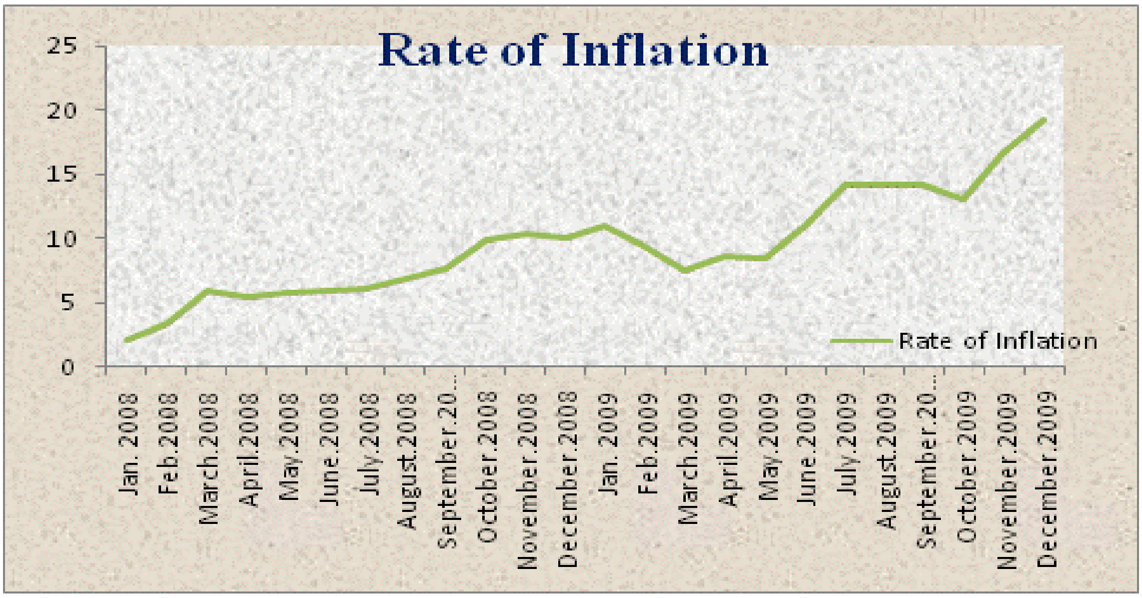
India, high inflation in 2009 and the year 2010 is mainly due to the fact that the country faced severe inflation. Inflation rate touched to an unprecedented level and food inflation touched nearly 20% in began to December 2009, after which it falls a little bit and started rises thereafter. Diagram 1 indicates the movement of food articles' inflationary tendency.

Diagram 1: Food articles' inflationary tendency in India



Source: CSO-Govt. of India (2010)

In a country like India, where more than two thirds of its population don't have adequate means to ensure minimum prescribed level of calorie intake, any further rise in the prices of food grains will have a disastrous impact on their living conditions. Households in lower income categories spend much higher percentage of their budget on food compared to the higher income groups. This indicates that food inflation hurts more than any other commodity group and low-income consumers are affected much more than high-income consumers.

Trend of food and non-food Inflation in India:

Dividing the commodities including in WPI in two major groups viz. food and non-food, shows that rate of price increase was higher in non food group compared to food group during January 2008 to October 2008.After this food and non-food prices follow

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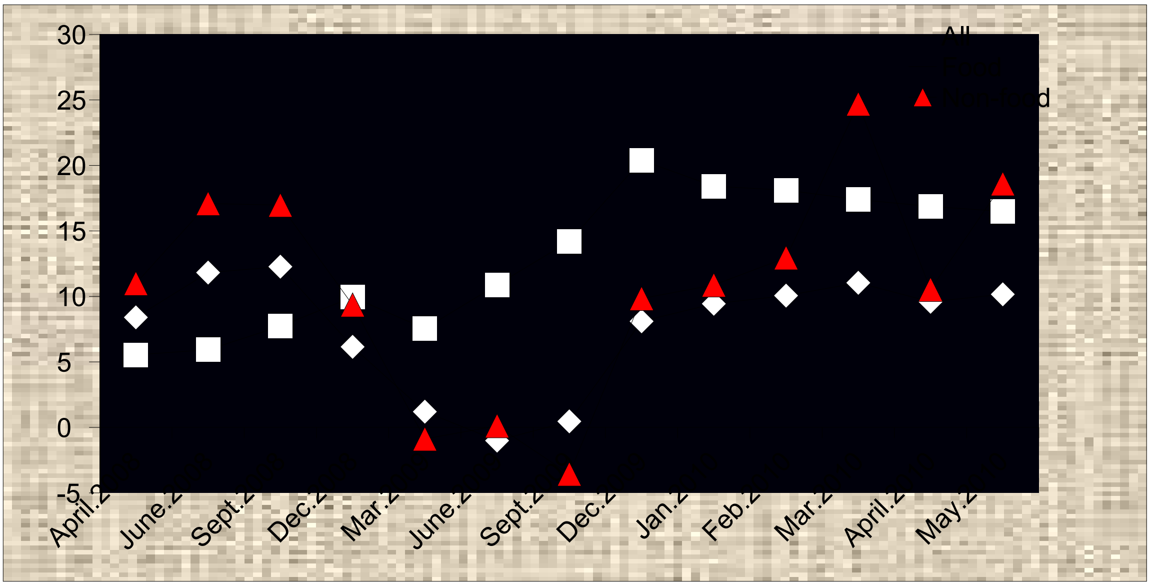
desperate trend. There was a sharp fall in inflation in non-food items where as food prices moved towards double rate of increase. For about nine months from March-November to 2009 WPI for non-food prices was lower than corresponding figures during 2008 which resulted in negative inflation in non food prices. After November 2009, prices of non food items also started rising which pulled up overall rate of inflation in the country to double digit level during February-March 2010.

Diagram 2: Trend of food and non-food Inflation in India



Source: RBI (2010)

There is some slowdown in food inflation after 2009; but food inflation still rules 16% in 2010, is shown in diagram 2.

Aanalysing different causes of food Inflation in India:

Food prices in international markets and in India have not behaved in the same way after the year 2006. Global food price increased by 26% (twenty six percent) during the year 2007 and reached historical peak by the middle of 2008. As per Govt. data, in contrast to these statistics, food prices in India (i.e WPI of food and food products with base 1993-94) increased by 8% during 2007-08. Further, monthly food prices in global markets increased by 20% between January and June 2008 while India experienced by only 12% increase. This difference in behaviour of the domestic and international prices has

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evoked serious concern because of persistently high rate of food inflation in the country and raised several questions.

i)Are Indian prices lower than international prices and closing the gap between the two necessitates higher inflation in India?

ii)Has trade ceased to be an important instrument for a country like India in taming food inflation?

In a country like India, which is largely food sufficient at aggregate level and where trade to output ratio is not very high, domestic factors matter much more than global factors in determining medium and long-term trend in prices. These factors relate to domestic demand, supply, food administration and so on. Further, factors like demand and supply depend on many variables like growth in income distribution of income, money supply, credit, technology and weather-related variables.

Taking a closer look at food inflation base on WPI over the last two years, it becomes apparent that manufactured food products have been contributing in a higher proportion than primary food articles towards rise in prices. Among the primary articles like cereals, milk and meat have higher share but rapid increase in prices of pulses, fruits and vegetables are also ignited inflation, for example, price of rice increased 12% during January in 2008 to may 2008. 1n 2010 price of wheat increased by 7%, among pulses, price of pea rose extremely high. Price of food product increased steeply with an average rate of inflation of 40% between January 2009 and May 2010.The fact that these articles are essential and irreplaceable components of the daily diet of an average Indian consumer adds gravity to the situation.

Supply side constraints and structural deficiencies:

The steady increase in food prices can be interpreted with the help of different short term and long-term factors. Among them most important is demand supply imbalance in essential food commodities. With the steady growth in income of the people and increasing urbanization, the demand for food is rising consistently year by year. The programme like NREGS contributed positively in demand for food. On the other hand, various supply side constraints like stagnating area under cultivation and constraints of

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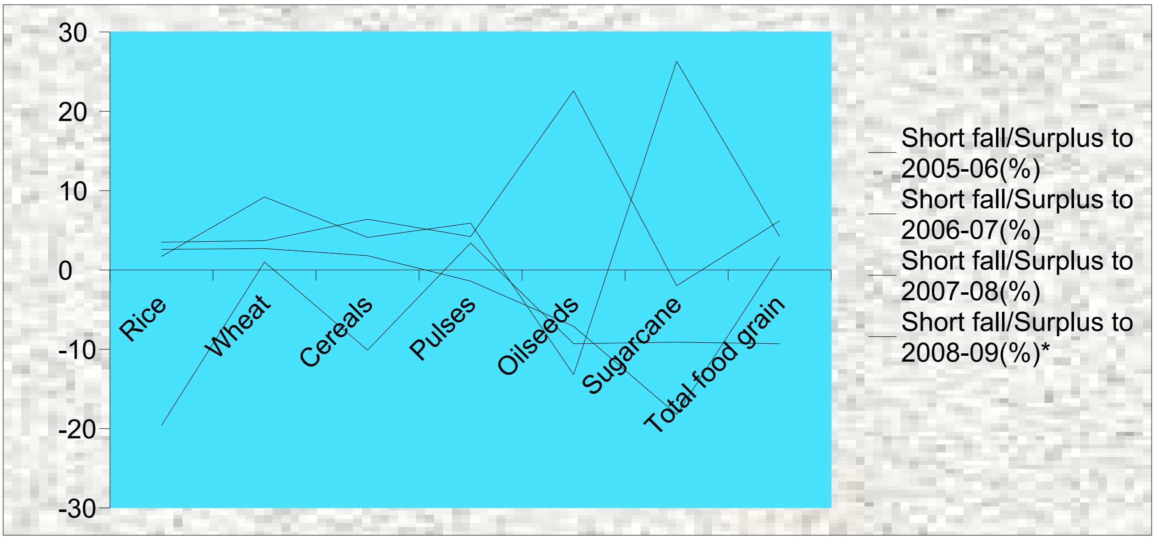
crop yields posing limits to production. Besides, drought in the last year and deficiency of monsoon is an immediate cause of supply shortfall during 2009 and which was extended to 2010.The country received around 25% less production in 2009 in relation to long term average. Production of major food commodities also got affected leading to overall shortfall in food grain production and other major crops like oil seeds and sugar cane. The shortfall of rice was around 20% with respect to the previous year, wheat production was less than targeted, production of oilseeds and sugarcane suffered a perceptible reduction shown in the diagram3.

Diagram: Shortfall of major crops in India (in Million tons)



Source: Ministry of Agriculture (2010)

Now to provide essential food grains through public distribution system (PDS) to the masses, especially to the poor people, govt. plays a very cautious role for food procurement. Then it becomes a matter of double loss to retain such high level of stocks, due to excessive expenditure incurred on storage in the one hand and it remains inaccessible to people on the other, which contributes to further rise in prices.

International link with food inflation in India:

After a sharp fall in global prices from the peak level during 2008, during 2009-10(June to May), global food prices again started showing up and increased by 17%. The sharpest jump was visible in sugar prices. Sugar price index shot up from 233.1 in June, 2009 to 375.5 in January 2010 due to supply shocks in Brazil. In the same period prices of dairy

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products went up by 86% and edible oils prices increased by 11%. All these price changes are transmitted in varying degrees from global markets to the domestic markets through various channels. For example, the unit value of pulse imports at 1993-94 prices in the year 2001-02 was Rs.8833 per ton, which increased to Rs.10781 per ton by 2008-09. Same trend was observed for wheat sugar and vegetable oils too. This has long-term implication in terms of taking the domestic prices to higher levels over a period of time and reflects the supply side constraints also. On the other hand, forward trading and speculation in food commodities especially essentials, is said to be another factor fuelling inflation.

Control of food Inflation in India:

Several initiatives have been taken by the govt. and the central bank to prevent general inflation. The Reserve Bank of India (RBI) has tightened its monetary policy through key policy rates but monetary policy has very limited effect to counter inflation in food commodities which is essentially caused by supply side constraints and the underlying deficiencies are chronic in nature. Food commodity driven inflation rate has become persistent phenomenon in India and the corrective measures involve concerted efforts over an extended period. We can refer some measures based on recent inflationary trend of food items which can be done under control. These are:

1. With public investments already hiked substantially in the recent years, there is a need to pay attention to improve efficiency of such investments.

2. As area available for agriculture and food production is going to shrink, focus must be given on enhancing the productivity of crops to keep pace with growing demand for food.

3. Filling up of food grains in the granary in India beyond the stipulated levels is an avoidable proposition. Resorting to open market sales is beneficial to control food price inflation as well as relieve the granary of excess stocks.

4. It is quite essential to widen the scope Of PDS by including more essential commodities like edible oils, pulses and sugar to provide some protection to poor against food inflation. It is again helpful to control food inflation by selling these items

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according to time need. However, this must be done cautiously giving certain number of subsidies and by proper care of leakages of our delivery system.

5. We need to develop a system for getting advance information on demand and supply imbalances timely and tune our trade policy accordingly without any political aim.

6. An important way for immediate remedy is to prevent speculation and hoarding in food commodities. The states should be active to forgo some taxes because of interstate transport of commodities at least for time being until the prices reach normal levels.

7. Down turn revision of state-specific customs and excise duties on diesel may also help bring down the prices of inputs used in agriculture, the possible way to control inflation.

Conclusion:

Monetary authorities and Govt.of India must be very much careful and swift enough to take proper stapes timely to contain food inflation without hurting growth momentum. Measures to control inflation in general and food inflation in particular, can be classified as immediate remedies, medium and long-term remedies. Immediate remedies is not enough which has require a long-term vision and planning where India's response is very slow and long running.

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