

Food inflation is a structural problem



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The various explanations for high food inflation that unfolded and endured in the past year and a half, would suggest that the sudden decline in the rate of food inflation should be viewed merely as a respite. Although unfavourable weather conditions did play a role in food prices, structural factors were also significant.

The stubbornly high food prices have raised a number of questions about inefficient marketing systems, weak storage infrastructure and stagnant productivity. While solutions to these constraints were expected to take some time, something else seems to have led to the decline in food inflation rate. A relief in price scenario would not have come without either an increase in supplies or weakening of demand. We are perhaps looking at both these developments.

The arguments pointing to the rising demand for food to items be-

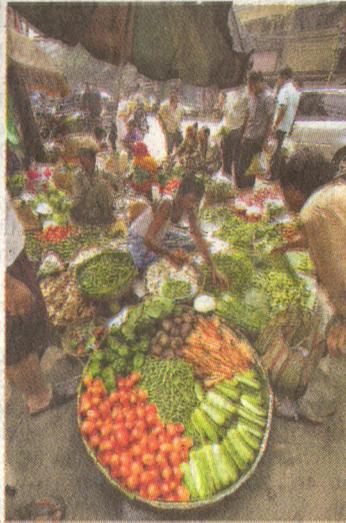
yond just the grains were particularly compelling; the high income elasticity of food and the rising income levels were a good explanation for the faster growth in demand than ever before. In this context, it comes as a pleasant surprise to consumers that supplies have caught up so soon.

If higher supplies have come from re-allocation of resources, particularly land, from other crops to those crops where price rise was sharper, then the supplies of the former will come under pressure. Therefore, unless unfavourable weather was the predominant cause of high food inflation, the watch on food prices will have to continue.

VIGIL ON PRICES

The relief in food inflation rate in the last few weeks has been significant. Seasonal factors, along with the prospects of better prices, may have led to increased supplies. In any case, high or remunerative prices would be needed for farmers to keep producing more. It is to be seen if farmers gained from high prices as well.

Marketing arrangements in the supply chain regained policy attention as farm prices rose. FDI in retail is only a pointer to the rising importance of marketing chains for perishables in agricultural policy. The



Supply-side bottlenecks need to be addressed.

issue is not just marketing efficiency, but also market infrastructure. Improvement in marketing infrastructure requires investments. It is necessary to get all these pieces of the food markets puzzle in place to deliver food to the consumers at an affordable price.

The policy dilemma in the context of food production and consumption is an old one. Farmers need higher prices to produce more, and con-

sumers cannot keep paying more for food. Government interventions to increase production do not necessarily mean lower prices to the consumer, although production does increase. Unless income also increases, the consumer would then have to be compensated in some other way for more expensive food.

STORAGE AND INSURANCE

What is significant about the high food inflation in 2010 and much of 2011 is that there were several commodities which contributed to high prices: pulses, sugar, milk, eggs, fruits and vegetables. An important feature of several of these commodities is their short shelf-life. The sensitivity of supply or demand fluctuations on prices under these conditions is obvious.

The need for reducing fluctuations in prices is important for both consumers and producers. There are incentives on the supply side to reduce output fluctuations, as also on the consumption side. These incentives are likely to drive other service providers, such as storage and insurance. Policies to encourage development of these services would help in reducing price fluctuations.

A number of initiatives are under way, including direct marketing of produce by the farmers to urban

centres. Continued support for improved infrastructure for transport and storage, including removing barriers that slow down movement, should form the core of government policies.

In order to balance the interests of producers and the consumers, the government should focus on measures that will have longer-term impact on supplies, and not merely the adjustments in export and import options or restrictions on stocks held by the traders.

The unfolding changes in the food economy also point to the scale of the problem. The price rise was not limited to one or two centres of consumption. The weak marketing infrastructure is not an issue that needs to be resolved only in major urban centres.

As income levels increase, the consumer may be willing to pay more for infrastructure that reduces supply uncertainties. But supply-side constraints will determine how much of which food would be produced.

The recent decline in food prices has not diminished the need for sustained supply-side measures.

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