THE FOOD SITUATION AND THE COMMON MAN

BY

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FORUM OF FREE ENTERPRISE

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"People must come to accept private enterprise not as a necessary evil. bat as an affirmative good."

— Eugene Black
President. World Benk

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Free enterprise today is not a very popular word in some quarters in India. This is rather unfortunate because the biggest single problem before us to-day, on the mundane plane, is a speedy increase in our national income. The largest bulk of Indian national income — 92% — is contributed by the Private Sector. The Public Sector is no doubt growing, but the contribution made by it is about 3%. The rest — 5% — is accounted for by governmental administrative expenditure. Unless there was an economic earthquake. which we hope not, private enterprise is going to remain a dominant feature of Indian economy for some considerable time. It would not conduce to speed in growth to place handicaps and hindrances on the way of entrepreneurs. It will be worthwhile making a study of the hindrances placed on the way of private enterprise since Independence with a view to assessing their cost to the expansion of national income. It is a serious matter that 'restrictionism' is becoming a habit of mind with the administration for a solution of national economic problems. At the moment, we are passing through several crises, The iood situation is one of them. The foreign exchange problem is another. The stresses and strains on the economy resulting from the tax proposals of the last budget is the third.

Not being an official economist or one attached to an industrial or business firm, I shall examine the issues which the food problem raises on a wholly objective and technical plane. I shall consider the problem under five heads. First, what is the nature of the problem? Second, what are the possible causes? Third, what are the remedies proposed by the Government? Fourth, are the remedies adequate? Do they grapple with the root causes? Finally, what should be the remedies to meet the situation?

First, what is the nature of the problem? The outward manifestation of it is a rise in prices. The Economic Adviser's index of prices relates to four groups of commodities: foodgrains, industrial raw materials, semi-manufactured articles, and manufactured articles. Prices of all these have risen. The General Index of prices — the average of the four groups — has risen at an annual rate of 13% since May 1955, when the present price rise began. Now the rise in prices — the General Index — is accompanied by a bulge in the prices of foodgrains. Since May 1955, foodgrain prices had risen by 27%, or more than double the rise in the General Index. Among foodgrains, the most important, rice and wheat, had gone up at even a higher rate — 33% and 23%, respectively. That in broad outline is the price problem, a general rise in prices accompanied by a bulge in prices of foodgrains.

What are the causes of this price phenomenon? A price rise may result from a change either on the supply side or on the demand side, or both. Let us consider the two sides separately. National income figures show a fairly substantial increase during the First Plan period. National income rose during the period by 17½%. If we may take 1952-53 as the base year for purposes of comparison, the income in 1955-56, the last year of the First Plan, shows a rise to 110 per cent over 1952-53. Money supply, during the interval, rose to 124 per cent. Since 1955-56, the index of money supply has jumped to 133. Money supply having risen faster than output, the national income, quite naturally, prices have risen.

The expansion of money supply is related to the budgetary policy of the Government and, therefore, to the finance of investment under the Plan. During the first two years of the Second Plan, Plan outlay in the Public Sector is estimated at Rs. 1,600 crores. Not the whole of this expenditure was financed from savings. If investment is financed from savings, general prices need not rise. Governmental expenditure, then, would be in substitution of private expenditure. Money supply would not increase. The Government would be putting out, through Public Sector investment, the moneys it took away from the pockets of the public either by way of taxes, loans or other receipts. About a third of the Public Sector outlay of Rs. 1,600 crores represents inflationary deficit financing. That is how money supply has outpaced output.

This overall picture finds support when we examine the supply and demand position of foodgrains. The output of foodgrains in 1956-57 was nearly the same as the post-war peak attained in 1953-54. The production of foodgrains in India for that year is officially placed at 68.7 million tons. The figure for 1956-57, issued last week, is 68.6 million tons. To this must be added foodgrains imported from abroad, principally rice and partly wheat. During 1956, these imports totalled 1.4 million tons (as against 7 lakhs in the preceding year). This raises the supply to 70 million tons, or much larger than the peak production of 1953-54. Thus, it is not as if the rise in the prices of foodgrains may be explained by shortages of output. We come to the same conclusion when we examine individual cereals. The output of rice during 1956-57 has gone up by 4.8% (to 28.1 million tons) relatively to 1955-56 and of wheat by 5.8% (to 9.1 million tons). Even so the foodgrain prices have risen by 27%, of rice 33% and of wheat 23%. ***The explanation of the price rise is that money incomes of the people have risen faster than the available supply of foodgrains.***

There remains to answer the question, why is there a bulge in the prices of foodgrains? This is attributable to the abject poverty of the people, which is the key-note of the Indian economy. In a poor economy, such as ours, consumption of food by the masses of the people is below nutritional standards. In such a context when money incomes rise, the tendency will be for the increase in money incomes to be devoted first to the purchase of foodgrains:. That is what has happened in India. The demand for foodgrains has risen with the increase in money incomes and this increase has taken place faster than the increase in the output of foodgrains.

What is the remedy to this problem? The remedies proposed or adopted by the Government are five-fold. First, they imposed a ban on the exports of foodgrains and foodgrain products in January/February 1956; second, they released stocks of wheat and rice with the Government at first on the open market and later through a network of 20,000 fair price shops scattered around the country; third, arrangements for larger imports of foodgrains (rice and wheat) from Burma and U.S.A.; fourth, measures to prevent hoarding of foodgrains; and, fifth, a credit squeeze on foodgrains.

Now most of these measures are palliatives. We may call them "first-aid" measures. The ban on exports would prevent a deterioration of the position. It would not, in itself, remedy the problem. For a remedy, the shortages should be made good either by increased production or increased imports. As production takes time, the immediate remedy lies in increased imports sufficient to cover the gap. Coming to the second remedial measure of the Government, the release of stocks in the open market and of their distribution through fair price shops, are a mere matter of machinery. In one market there cannot be two prices for the same commodity at one and the same time.

So long as a price difference existed between open market prices and prices at the fair price shops, the market will gobble up the supplies issued through the latter and complaints of too small and too slow releases will remain. Distribution through fair price shops will have an effect upon prices only to the extent the quantities released may reduce the gap in supplies; the price effect would not be any larger than if the stocks were released directly on the open market. What, then, is the difference between releasing stocks on the market and distributing them through fair price shops? The difference is in the subsidy. In the case of distribution through fair price shops, there is a food subsidy. In the case of releases on the market, there is no subsidy. This subsidy, moreover, is haphazard, and a part of it leaked into the hands of black-marketeers. With our budgets already in deficit, we can ill-afford to distribute large sums in ill-conceived subsidies.

Now let us take the third of the remedies, larger imports of foodgrains. We have seen that, notwithstanding very near peak production in 1956-57 and large imports, foodgrain prices have kept soaring. Imports will have an effect upon prices only if we can keep a check on the expansion of the money incomes of the public. If money incomes kept expanding, the demand for foodgrains will keep rising and the gap in supplies will keep growing so that we will need larger and larger imports to cover the gap. It is not intended to suggest that poor people must not be allowed to have a little more foodgrains. We began by saying that the biggest single problem in India is a speedy increase in our national income. That will enable the masses of the people to feed themselves a little better than they are able to do to-day. ***But we cannot solve this problem — the problem of low standard of living of the masses of the people — by an inflationary expansion of money incomes. To do so would be to defeat our purpose,*** *as inflation, through dissipating savings into consumption, would detract from the pace of capital formation and economic development.*

Coming to the fourth remedy, the reasoning which links up hoarding with the prevailing rise in prices is rather superficial. Hoarding is not so much the cause as the consequence of the inflationary price rise, though it fanned the flames of the price rise. Why does hoarding take place? It takes place because of the expectation of a continued price rise. So long as this expectation remains, hoarding will continue. Hoarders are no doubt engaged in an anti-social activity as they are hoarding foodgrains in a background of food scarcity and they merit severe punishment. But it is bad policy to put a premium on hoarding with one hand and punish the hoarders with the other. If we stopped inflationary finance (over-investment), hoarding would soon cease as it would be, then, no longer worthwhile. We do everything we can to drive prices up through inflationary finance in the name of the Plan. At the same time we insist that prices do not rise in the name of the cost of living of the common man. If prices do rise, we get angry, we look around for the anti-social elements responsible for it, and threaten to hang the foodgrain hoarders and speculators and, lately, also the General Managers of scheduled banks, who, notwithstanding the directives of the Reserve Bank, have not succeeded in restricting bank credit sufficiently.

At the moment, our attention seems to be riveted on a credit squeeze by the banks against speculative hoarding (fifth remedy) on the theory that, as stocks are held on bank credit, if the stockists are denied credit, they would be compelled to unload the stocks on the market and cause a fall in foodgrain prices. This ignores the root cause of the malady. If the expectation of a price rise remains, credit squeeze measures are likely to be dodged, as they

are being dodged, and hoarding will continue. The market will raise credit on the hypothecation of things other than commodities loans against which are restricted or banned. There may be borrowing and lending on a larger scale outside the scheduled banks. Credit squeeze measures may handicap the larger stockists. But this will only scatter the activity of hoarding. The place of the larger stockists will be taken by the lesser fry and the larger farmers. *Hoarding in a background of inflation with the attendant expectations of a continued rise in prices is an "en masse" operation of the entire body of traders, big and small, even non-traders, e.g., farsighted householders, joining their ranks.* It is significant that, notwithstanding a policy of selective credit restriction and, later, of selective credit squeeze (as may be expected in the wake of inflationary Plan finance), bank deposits rose during the two years ending 1956-57 at an annual rate of 12 per cent and bank credit at an annual rate of 22 per cent. Both continue to expand during 1957-58. *We cannot press the accelerator of expenditure in the Public Sector with one foot and jam the brake of bank credit with the other; such a policy just will not work. To attempt it suggests financial amateurism.*

What, then, should be the remedy? That a correct diagnosis is half the cure applies to economic ailments as well. If our diagnosis of the price phenomenon is right, we have embedded in it the natural remedy. Our analysis indicates that the shortages of foodgrains are artificially created market shortages. If we removed these artificial factors, we will be well on the way to a solution of the problem.

This suggests that the remedy is two-fold. *The first remedy, which I have been repeating again and again, is to prune the Plan according to the available resources. Post-war experience has shown more conclusively*

than ever before that most of our economic ills are traceable to a policy of over-investment. The second remedy was to accept the consequence of inflation of the immediate past, i.e., to recognise the fact that food shortages have arisen because of an artificial stimulant to consumption. That resulting gap in supplies can be covered only by adequate imports of foodgrains. I do not see any other way. This would trim the demand for foodgrains to the level consistent with the real national income. The artificial pressure on supplies will be removed.

What about internal procurement of foodgrains? Procurement of foodgrains might draw out supplies from one sector of the economy — the farmers — into the hands of the Government. But looking to the economy as a whole, shortages will continue. The same would apply to the cutting up of the national market for wheat into zones, one of the price corrective measures adopted by the Government. This may lead to prices in the surplus areas being artificially lowered. A fall in prices would react adversely on the production of wheat and this, in turn, will aggravate the wheat price problem.

In view of our experience of the working of price controls, the "remedy" of price controls does not appear to be under immediate consideration. A reimposition of price control measures would be most unfortunate. Firstly, price controls may not work in an inflationary background. A people in want cannot be induced or coerced not to spend the money put into their pockets. To the extent price controls may be effective, the flow of money to the controlled sector of the market would be less than might be the case otherwise and its flow into other sectors might be correspondingly larger, even as, if the flow of flood waters was checked in one direction it would flow with greater force in another direction. Lower prices of the controlled commodities would be balanced by higher prices

of the uncontrolled commodities. The average of the two — the general index of prices — would reflect the state of inflation. This indicates the fallacy of thinking that price control of foodgrains and cloth might control the cost of living. Control of the price of foodgrains may not control even the food bill of the people. ***A thali*** of food contains many more items than rice and ***atta.*** If the prices of vegetables, condiments, dal and firewood rose freely, the price of a ***thali*** of food would reflect the inflationary situation, notwithstanding foodgrain controls. This fact is not negatived by reducing the number, and diluting the quality, of the items in the ***thali,*** though it may deepen the delusion regarding the effectiveness of controls.

Secondly. under the stress of reduced profits the output of foodgrains, the prices of which were controlled, might suffer. It might cause honest farmers to shift to the production of uncontrolled commodities. This may widen the gap of the food deficit and the government may be compelled to import more foodgrains. The counterpart of this phenomenon was a diversion of resources to the socially less useful trades which offered higher profits.

Thirdly, contorls once introduced would tend to breed more controls, and would cause corruption and black-marketing. The spread of controls would be induced by the urge to render controls effective. Black-marketing and corruption would be the natural outcome of the gap between controlled prices and competitive (black-market) prices, which would emerge in an inflationary background. The spread of controls (on the war-time U.K. model, which is often quoted in this respect) in a vast country like India would raise stupendous administrative problems and would involve a diversion of personnel, greatly needed for implementing development, into administering the machinery of controls. Economic development in India is not a matter of one or two five-year plans. It may take a generation or two before our level of living may rise to that of Western Europe. It is not practical to expect 385 million people meekly to submit to the rigour of price controls and rationing for prolonged periods. The analogy of the conduct, for a few years, of a disciplined island community in the face of the dangers of a total war would not apply to the needs of peace-time economic development. Moreover, the problem of imposing a system of controls in an economy, such as the British, where production and distribution were highly organised, cannot be compared with the almost insuperable task of controlling the operations of millions of small units of production and distribution, such as prevail in India. Even assuming that total controls were attempted and were successful, to the extent of their success they would leave behind them the legacy of latent inflation. *Controls would, thus, only postpone the evil, not remedy it.*

Finally, price controls and rationing did not create savings. Their prime function was egalitarian — to distribute equitably, at fair prices, the scarce supplies of goods and thus help maintain peace on the home front. They came into the picture, so to speak, after investment took place and the quantum of the available consumer goods had been determined. They did not influence either investments or the flow of consumer goods. *By themselves, price controls and rationing would not cause to grow two blades of grass where only one grew before.* It was, thus, a delusion to suppose that "the institution of controls on the lines of war-time controls" on the prices of wage goods would provide the "way out" of a shortage of resources. To meet the immediate requirements of a plan of development we need not controls but more savings. *Economic development is a function of invested savings and price controls are not a substitute to savings.*

CONCLUSIONS

1. The prevailing rise in prices is almost wholly a monetary phenomenon, being the outcome of over-investment under the Second Plan. Its roots lie in the last year of the First Plan, when over-investment began. The rise in foodgrain prices does not reflect shortages of foodgrain supplies; it reflects rather a stimulated demand for foodgrain born of incomes. The scarcity is, thus, an artificially created market scarcity.

2. The bulge in the prices of foodgrains reflects the natural tendency in a poor economy such as ours (where the foodgrain consumption of vast masses of people is below minimum nutritional standards) to expend expanding money incomes on foodgrains first. It is significant that the prices of rice and wheat have shot so high notwithstanding noteworthy increases in their output during 1956-57 and the considerable imports of the two grains during 1956 and after.

3. Imports of foodgrains and their distribution through fair price shops are in the nature of "first-aid". The price effect of these measures would depend upon the extent by which the imported grains would cover the prevailing foodgrain deficit. Whether Government grain is sold to the market or directly to the consumers through fair price shops is largely a matter of machinery. The former would involve no State subsidy, while the latter would. So long as price differential existed between the price in the fair price shops and the market prices, complaints of too small and too slow releases through fair price shops will remain. A part of the releases will also leak into the "black-market".

4. Selective credit squeeze measures and police action against hoarding are not a lasting solution to the price problem.

So long as over-investment continued and prices were expected to rise, hoarding will prevail, The action against hoarding will only determine who undertakes hoarding, and will, besides, introduce in the economy wholly purposeless stresses and strains and would add to economic instability.

5. Price controls of foodgrains in a background of inflation is a steep uphill task. It may not be effective. It may not control even the food bill of the people.

6. Control over the allocation of resources (which formed an integral part of the communist technique of planning) is incompatible with planning in a democratic economy. The functioning of it being governed by the market mechanism, there is little room in such an economy for allocation controls of the communist pattern.

7. No lasting remedy to the price problem is possible except through, firstly, a cessation of over-investment, and, secondly, imports of foodgrains in sufficient quantity to cover the gap in supplies which has resulted from inflation of the immediate past. If a restrictive investment policy is maintained, and sufficient imports are available, it is worthwhile considering the question of placing the imports on the market rather than distributing them through fair price shops. Sale to the market would save the Government large sums on subsidy. The distribution of the subsidy to-day is haphazard and a part of it leaks into the hands of black-marketeers. With a deficit budget we can ill-afford to devote large sums on ill-conceived subsidies.

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Free Enterprise was born with man and shall survive as long as man survives.

-A. D. Shroff

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