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Increasing Food prices in India after COVID-19 Era - A Food Security Approach

Mr. Milind Patil[1] & Dr. Gulnawaz Usmani[2]

[1]*Research Scholar, Dept of Economics AKI's Poona College, Camp, Pune.*

[2]Asst. Prof, *Dept of Economics AKI's Poona College, Camp, Pune*

Corresponding Author: Mr. Milind Patil

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Abstract:

Food inflation in India has remained stubborn in recent years. Several proximate factors such as Increasing demand particularly arising from higher rural wages, rising agricultural cost of production, changing consumption patterns favouring protein items, increases in minimum support prices (MSPs) and droughts in certain years are believed to have led to higher food inflation. This paper examines the relevance of these factors and finds that increasing real rural wages have played the most dominant role in the determination of overall food inflation in India in the long run. In the long run, while money supply leads to a rise in the prices of both food and manufactured prices, a hike in the call rate has a negative effect only on manufactured prices. The impact of the money supply is, however, more on food prices than on manufactured prices. The present paper discusses on the impact of monetary tools on curbing food price Inflation in India. Recovering from pandemic-induced contraction, the Russian-Ukraine conflict and inflation, the Indian economy is staging a broad-based recovery across sectors, positioning itself to ascend to the pre-pandemic growth path in FY23.

Keywords: Food Inflation, Minimum Support Price (MSP), Money Supply, Call Rate, Pandemic

Introduction:

In India, the three major objectives of economic policy are growth, social justice (equitable distribution of income and wealth), and price stability. Of these, price stability is perhaps the one that can be pursued most effectively by the monetary authorities of the country. The monetary policy of an economy operates through three important instruments, viz., the regulation of money supply, control over aggregate credit, and the interest rate policy. In the proreform period, given the largely underdeveloped state of the financial system, the regulated nature of financial markets, and plan priorities, the RBI often resorted to the direct instruments of monetary policy like CRR, SLR, and interest rate for allocating credit and regulating money supply in the economy. Gradual liberalization and globalization of the economy, strengthening and development of the financial system, restrictions on the automatic monetization of fiscal deficit, and various other changes in the economy had made it possible for the RBI operates with the indirect instruments of monetary policy such as bank rate, repo rate, and OMOS (open market operations). Accordingly, there has been a distinct shift in the monetary policy framework and operating procedures from direct instruments of monetary control to market-based indirect instruments in recent years. The monetary authorities are striving hard to curb inflation by adopting several monetary policy measures, the important amongst which are changes in CRR, repo, and reverse repo rate, which directly influences the money supply in the market with immediate effect without creating any distortions in the economy. That is the reason, they are perceived to be the most appropriate by the monetary authorities to curb the existing inflation, and hence changed 16 times during the year 2020 to 2022.

Beginning 2021-22: Q2 till 2021-22: Q4, with the exception of few quarters during 2012-13 and 2013-14, food inflation in terms of a wholesale price index (WPI) remained above overall inflation. The quarterly food inflation grew at an average rate of 10.16 percent during this period compared with 6.76 percent for overall inflation. In contrast, during the preceding period of five years between 2019-2020 till 2021-22, the overall inflation was generally observed to be higher than food inflation. This was the period when inflation in general was low, and the average quarterly food inflation of 2.63 percent during the period was much lower than the overall inflation rate of 4.90 percent.

Objectives of the Study:

1. To study the nature and causes of food prices inflation in India
2. To examine the effectiveness of monetary policy in ensuring price stability in India
3. To study the changing role and importance of selected monetary instruments in India
4. To study the impact of food price rise as an obstacle to economic growth.

Comparison of Various Financial Values:

The disproportionate response of agricultural and industrial prices to monetary changes, both in the short-run and long-run have been empirically validated by several studies for different countries, for the US, Onlen and Fackler (1989) using a VAR and impulse response function show that an increase in money supply raises agricultural prices relative to the general price level for more than a year implying monetary changes lead to a change in real agricultural prices in both the short- and long-run Saghai Reed and Merchant (2002) extended Frankel's closed economy model to an open commodities for the US economy. They found that monetary changes have both short- and long-run economy framework by including exchange rates to account for international trading of agricultural effects on agricultural prices

Now, we can have a look into the variations in the values of these variables over the period for finding out the reasons behind them. Whether the monetary policy is effective in implementing price and financial stability or not, will be clear from such a comparative analysis. The values of all three items have increased over the years, i.e., net bank credit, broad money, and the price level. We can see the maximum values in the financial year (in 2022-23), i.e., Rs. 16,67,096 crores, Rs. 55,79,567 crore and 242.9 respectively. The values have increased continuously during the period, showing a positive and direct correlation between the three; even though the rate of growth does not seem proportionate. Percentage changes in these values also show a positive picture, but with frequent ups and downs in variations. Credit availability has exhibited its maximum percentage variation as 42 percent during 2018-19 and the minimum rate of change was 0.9 percent in 2020-21. WPI has marked its minimum of 3.3 in 2021-2022.

Whenever there were price hikes during the years, monetary authorities successfully have made use of all the weapons effectively and prudently, to rein the inflationary pressures and to maintain financially stability in the economy. However, the RBI reduced the CRR continuously many times during the inflationary pressures, and to absorb excess liquidity, the RBI has raised the CRR, SLR, Repo and Reverse Repo rates altogether.

Headline Inflation Declined from its Peak:

FY22 witnessed lower CPI-Combined (CPI-C) based retail inflation as compared to FY21. Even so, inflation remained on the higher side when compared to the moderation seen during the years prior to the pandemic. During FY22, some sub-groups such as 'oils & fats', 'fuel & light' and 'transport & communication' reported high inflation. This was mainly driven by supply disruptions caused by pandemic-induced lockdowns. The subsequent year (FY23) began with the Russia-Ukraine crisis that led to high headline inflation rate in April 2022.

In FY23, retail inflation was mainly driven by higher food inflation, while core inflation stayed at a moderate level. Food inflation ranged between 4.2 per cent to 8.6 per cent between April and December 2022, while the core inflation rate stayed at around 6 per cent except in April 2022.

Table V.1: Average Annual Retail Inflation Based on CPI-C (per cent) (base: 2012=100)

Groups/Sub-groups	**Weight**	**FY20**	**FY21**	**FY22**	**FY23***
Food & beverages	**45.9**	**6.0**	**7.3**	**4.2**	**7.0**
Cereals and products	9.7	2.8	3.8	0.5	9.3
Meat and fish	3.6	9.3	15.4	7.9	4.7
Egg	0.4	4.5	12.9	7.6	-1.0
Milk and products	6.6	2.9	5.4	2.8	6.8
Oils and fats	3.6	2.9	16.0	27.4	5.4
Fruits	2.9	0.7	2.6	6.2	4.4
Vegetables	6.0	21.3	5.8	-7.2	7.6
Pulses and products	2.4	9.9	16.4	6.0	1.8
Sugar and confectionery	1.4	0.8	2.5	2.3	2.7
Spices	2.5	4.4	10.9	5.3	14.9
Pan, tobacco & intoxicants	2.4	4.2	9.9	4.5	2.0
Clothing & footwear	6.5	1.6	3.4	7.2	9.7
Housing	10.1	4.5	3.3	3.7	4.1
Fuel and light	6.8	1.3	2.7	11.3	10.5
Miscellaneous	28.3	4.4	6.6	6.7	6.3
Household goods and services	3.8	3.1	3.0	5.8	7.5
Health	5.9	6.2	5.1	7.5	5.8

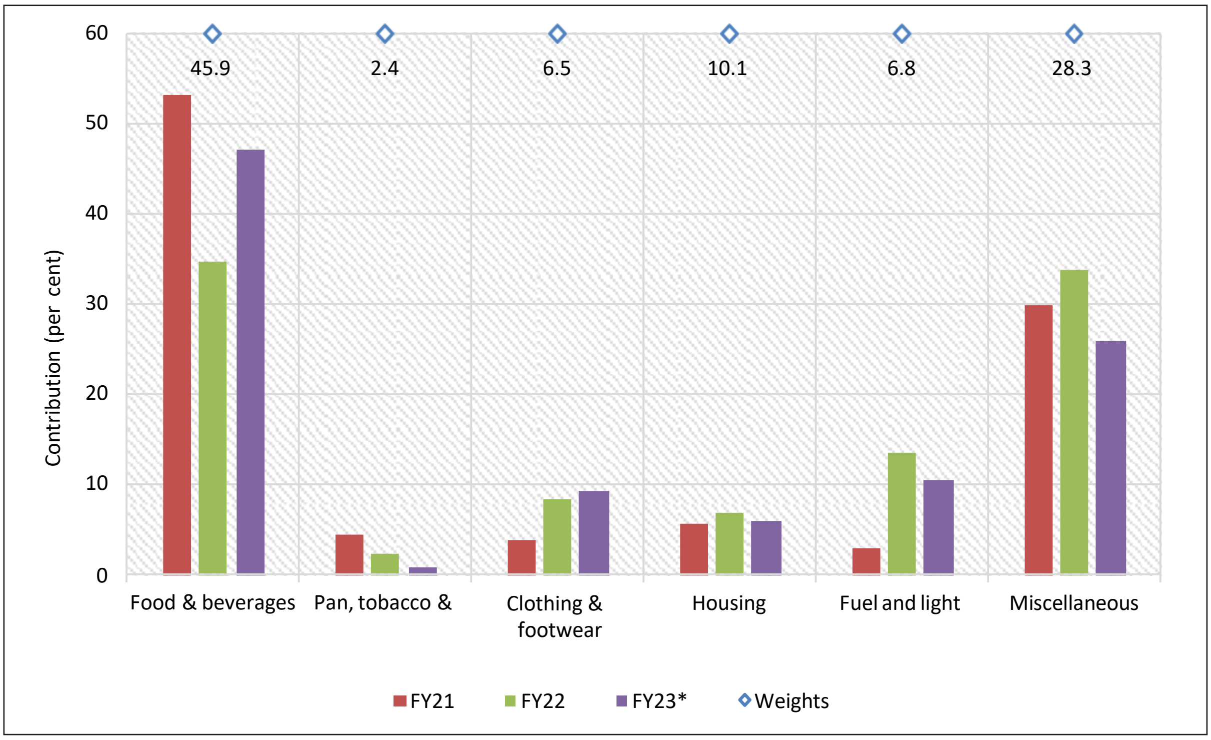
Transport and communication	8.6	2.4	9.9	10.1	6.4
Recreation and amusement	1.7	4.9	5.1	6.5	6.4
Education	4.5	5.5	2.8	2.9	5.2
Headline Inflation	100.0	4.8	6.2	5.5	6.8
Core Inflation	47.3	4.0	5.5	6.0	6.1
Food Inflation	39.1	6.7	7.7	3.8	7.0

Table 1 Source:: MoSPI, Source: MoSPI,
Note: *April-December, CPI data for December 2022 are provisional

Retail Inflation Driven by Food Commodities

Retail price inflation mainly stems from the agriculture and allied sector, housing, textiles, and pharmaceutical sectors. Further, the global spill overs, representing the imported inflation channel, driven by price pressures in energy, mining, chemicals, trade, basic and machinery,[2] reaches the retail segment mainly through the wholesale price inflation. During FY23, 'food & beverages', 'clothing & footwear', and 'fuel & light' were the major contributors to headline inflation– the first two contributing more this fiscal than in the previous one.

Figure V.4: Retail Inflation Driven by 'Food and Beverages' Group



Source: MoSPI
Note: *April-December

Within the 'miscellaneous' group, high inflation was observed in subgroups 'household goods and services' and 'personal care and effects' owing to the revival of consumer demand in the post-Covid-19 period. Moreover, retail inflation in the 'health' sub-group moderated in the current financial year as compared to FY22. However, inflation in the 'education' subgroup surged on account of schools reopening for in-person classes after the pandemic.

Food Inflation Caused by Vegetables and Cereals in FY23:

Food inflation based on Consumer Food Price Index (CFPI) climbed to 7.0 per cent in FY23 from 3.8 per cent in FY22. Though the increase in food inflation is broad-based, the major contributors are vegetables, cereals, milk and spices. The RBI forecasts elevated domestic prices for cereals and spices in the near term, owing to supply shortages. Milk prices are also expectedto spike reflecting high feed costs. Since September 2022, double-digit inflation was observed incereals. To check the soaring prices of wheat and rice, the government has prohibited the export of wheat products under HS Code 1101 and imposed an export duty on rice. Further, in order to insulate vulnerable sections from the rise in prices, the Government has launched a new integrated food security scheme, 'Pradhan Mantri Garib Kalyan Ann Yojana' on 1 January 2023, to provide free foodgrains to more than 80 crore beneficiaries. High inflation in vegetables from April to September 2022 was mainly due to a spike in prices of tomatoes owing to crop damage and supply disruption due to the unseasonal heavy rains in the major producing states of Karnataka, Tamil Nadu, Andhra Pradesh, and Telangana. Inflation in pulses remained muted owing to higher production and measures taken by the government in terms of maintaining a buffer stock and reduction of import duties and cess on pulses. International prices of edible oils surged in FY22 owing to a shortfall in global production and an increase in export tax levies by various countries. India meets 60 per cent of its edible oils demand through imports, making it vulnerable to international movements in prices. For instance, sunflower oil, which makes up 15 per cent of our total edible oil imports, is procured mainly from Ukraine and Russia. Thus, FY22 saw edible oil inflation on account of international price pressures. However, inflation remained subdued in FY23 because of rationalisation of tariffs and the imposition of stock limits on edible oils and oil seeds.

Rural-Urban Inflation Differential Has Declined:

Rural inflation has remained above its urban counterpart throughout the current fiscal year, reversing the trend seen during the pandemic years. CPI-C based food inflation seemsto have cooled down after reaching a high of 8.3 per cent in April 2022 due to a subsequent moderation in global food prices and a reduction in farm input costs. However, the cooling was more pronounced for urban inflation, which softened to 2.8 per cent in December 2022. Rural fuel inflation remained lower than its urban counterpart throughout the current fiscal, due to subdued price pressures on traditional fuel items such as firewood and cow dung cakes as opposed to petrol and diesel.

While the current fiscal year saw rural and urban inflation closely tracking each other, FY22 had seen a wider differential between the two. The gap between rural and urban inflationreached its widest in March 2022 due to a difference in the experience of food inflation. Urban areas experienced a sharper increase in food prices of vegetables and oils during this time as compared to the hinterlands.

Findings and Conclusions:

The higher inflationary run is an unfamiliar development in a country that experienced an average inflation of less than 5% from 1996 to 2006; where government were once toppled over expensive onions and even 6% inflation seemed too much in 2004. India was model in the world for low inflation and low tolerance of inflation. But in the last few years, we have certainly entered a phase of more inflation accommodation than ever before. The factors contributing to rising incomes are expenditures under NREGA, hike in the Minimum Support prices, Sixth Pay Commission and demand of labor for PMGSY.

The Government has refused to panic even in these times and have gone for deregulation of petroleum products. Inflation can cut both ways even from growth perspective; it often poses a dilemma for policy makers. Undue tightening of monetary policy to contain inflation may choke off investment and therefore growth. At the same time excessive high inflation rates which result in high negative real interest rates may be detrimental to savings and hence growth. The Government performance with respect to food price inflation cannot escape criticism. Some factors responsible for food inflation are Crop failures, diversion of grain supplies to bio fuels, shifts in cultivation patterns from food crops to cash crops are beyond the control of government. Nevertheless, the government's mismanagement in Public Distribution System and Food Corporation of India where excessive stocks of food grains are washed away by rains, wasted by rats and pests. The Govt. should think certain strategies in order to shift away from dependency on monsoons and applications of technology in increasing agricultural productivity.

Inflationary expectations are decisive in charting the course of inflation. The RBI's anchoring of inflationary expectations through forward guidance and responsive monetary policy has helped guide the trajectory of inflation in the country. The one-year-ahead inflationary expectations by businesses have shown a decreasing trend in the current fiscal. As businesses are price-setters, their perceptions on inflation are significant in making sense of whether costs would be passed on, resulting in higher prices in the near future. Similarly, inflationary expectations by households-who are the price takers of the economy-determine their consumption choices in the near future. Much like businesses, household inflation expectations too have moderated.

Thus, along with monetary policy, government should try to work on increasing the supply of food crops so as to meet the increasing consumption demand. The demand of rising middle class towards fruits and dairy products cannot be tamed down with monetary policy nor logical.

Hence factors responsible for supply side of inflation should also be taken care of along with monetary policy. Apart from it there should be coordination between fiscal and monetary policy as both complement each other.

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