Consumption and Consumer Policy

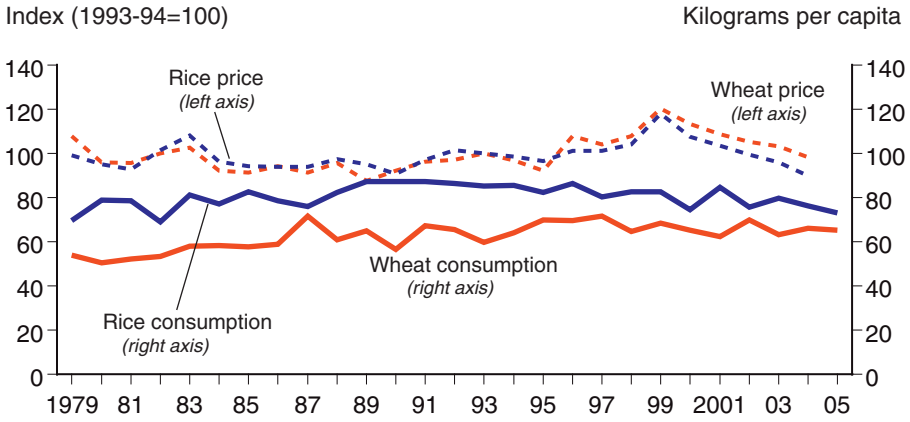
During the 1970s through the early 1990s, per capita consumption of wheat and rice rose, reflecting strong gains in production, income growth, and stable real prices. In the mid-1990s, however, per capita consumption of wheat leveled off and rice began to decline. Slowed growth in consumption occurred despite substantially faster growth in incomes, as the result of changing consumer preferences, changes in government price and distribution policies, and rising open-market cereal prices.

Recent studies of the relationship between income, prices, and consumption of wheat and rice indicate that, at least among some Indian consumers, wheat and rice demand is no longer rising with incomes. Although there is controversy on this issue, analyses based on India's National Sample Survey data (Kumar, 1998; Bhalla et al., 1999) suggest that, while low-income groups still show positive income elasticities of demand for cereals, income responsiveness for the population as a whole is declining and may now be near zero. As in other developing Asian countries, higher incomes and urbanization are diversifying consumer demand away from food staples, and gradually reducing the growth rate of wheat and rice production needed to meet domestic demand. However, wheat and rice remain the dominant source of calories and protein in the diets of most Indian consumers, and together still account for about 22 percent of household expenditure in rural areas and 13 percent in urban areas—more than any other item.

The demand studies have also generally shown that wheat and rice consumption respond to relative prices, with lower income consumers being the most price responsive. From the 1970s through the mid-1990s, the upward trend in per capita wheat and rice consumption corresponded with variable, but roughly constant, real prices (fig. 5). There was stronger evidence of the impact of prices on consumption between the mid-1990s and 2000, when slowed per capita consumption (particularly of rice) corresponded with rising real MSPs and market prices. Since 2000, however, declining market prices have yet to reverse the slowdown in consumption. Although the most recent behavior may suggest that wheat and rice

Figure 5

Wheat and rice consumption and real prices in India



Sources: Government of India, Ministry of Finance, Economic Survey; USDA Production, Supply, and Distribution database.

consumers are becoming less responsive to changes in relative prices, it is likely that the relatively low-income consumers served by India's food-distribution programs remain responsive to changes in relative prices.

Food Distribution Policies

Changes in government food procurement and distribution programs, which accounted for about 20 percent of total wheat and rice consumption during 1995-2005, have been a factor in the slowed growth in wheat and rice consumption since the mid-1990s. In 1997/98, the Indian Government revamped the public distribution system (PDS)—a system for distributing subsidized wheat, rice, and other essential commodities through a nation-wide network of more than 460,000 "fair price shops"—in an effort to reduce costs and improve targeting to low-income consumers. The revamped PDS was renamed the targeted public distribution system (TPDS). The previous practice of offering quotas of wheat and rice to all consumers at one subsidized rate through the PDS was replaced by a system with a separate, highly subsidized rate for consumers certified as below poverty line (BPL) and a higher rate for everyone else (termed above poverty line or APL). Prices for BPL sales of wheat and rice were initially set 33-38 percent below those charged under the PDS (figs. 6,7). The new rates covered only about a third of the total costs incurred by the Food Corporation of India (FCI). Prices for APL sales were set 12-30 percent higher than under the PDS, rates that covered about 60 percent of FCI costs in the case of wheat and 75 percent in the case of rice.

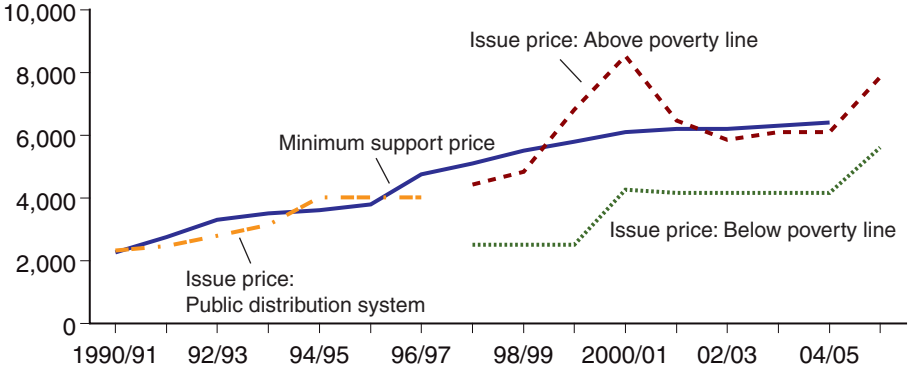
An additional change made with the goal of better reaching low-income consumers was the expansion and introduction of programs to distribute wheat and rice through school lunches, food-for-work programs, employment guarantee schemes, and more highly subsidized sales to the "poorest of the poor."

During the initial years of implementation of the new TPDS and other welfare schemes (1997/98-2000/01), total distribution of wheat and rice declined and remained well below the amounts procured in price-support

Figure 6

Wheat policy prices in India

Rupees per ton

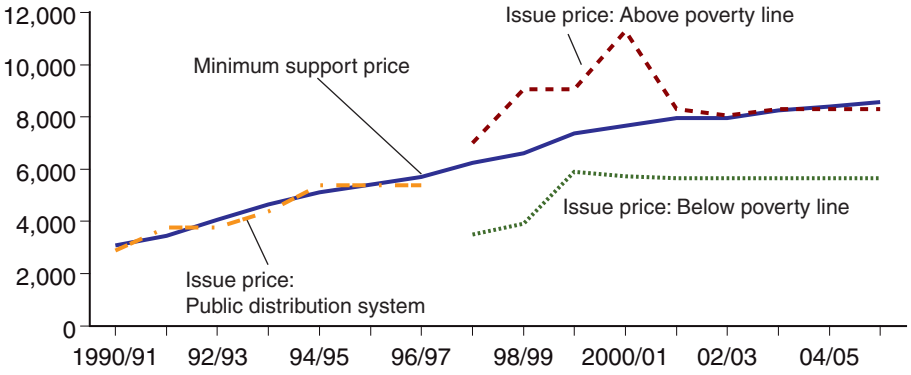


Source: Government of India, Ministry of Finance, Economic Survey.

Figure 7

Rice policy prices in India

Rupees per ton



Source: Government of India, Ministry of Finance, Economic Survey.

operations. Under the TPDS, BPL distribution initially remained low, largely due to administrative difficulties in certifying poor households, and there was very limited distribution through the APL channel because APL prices were typically above market prices. The new welfare programs also began slowly due to implementation delays. The net impact of government operations during this period was to reduce market supplies of wheat and rice available for consumption, with the FCI either adding grain to public stocks or making it available for export.

In recent years, there has been expansion in wheat and rice distribution through the BPL program and various welfare schemes, and reduced APL prices have also boosted sales through that channel. Welfare programs have shown the most growth, rising from about 11 percent of total distribution in 1997/98 to nearly 40 percent in recent years. The TPDS and welfare programs continue to face criticism because of difficulty in accurately identifying and reaching targeted groups and because of problems with "leakages" of subsidized grain into the open market (Government of India, Ministry of Consumer Affairs, Food, and Public Distribution, 2002).

India's government food distribution programs, including both the old PDS and the current TPDS, have been criticized for their limited impact on the poor, and for inefficiency. Although large amounts of grain appear to have been distributed through the PDS and TPDS, poor households still rely primarily on the market for their supplies of wheat and rice. According to the 1999/00 National Sample Survey, only about 10 percent of poor rural households and 14 percent of poor urban households purchased grain from the TPDS (Ramaswami and Murugkar, 2005). A study of TPDS efficiency estimated that it cost Rs3.14 to transfer Rs1.00 of benefit to poor households through the TPDS in the State of Andhra Pradesh and Rs4.00 to transfer the same benefit in the State of Maharashtra. Out of the total expenditure on food subsidies in these States, 26.5 to 31 percent was lost in transfers to nonpoor households; 16 to 26.5 percent was lost because of the abnormally high costs of grain transport, handling, and storage; and 15 to 28 percent was lost because of "leakages" to the open market and other forms of fraud. The share of subsidy expenditure actually reaching poor households

was about 25 percent in Maharashtra and 32 percent in Andhra Pradesh (Ramaswami, 2002).

Because a high proportion of India's food subsidy costs stem from the Government's involvement in owning, transporting, and storing grain, a shift to a program based on food stamps, such as that used in the United States, would have the potential to significantly reduce government costs. With a food stamp program, physical handling and distribution of grain would lie with the private sector, thereby reducing or eliminating a large share of current government costs. The corruption-related "leakages" of grain during government handling and storage could also be avoided. Setting up a U.S.-style food stamp program would involve many of the same problems in identifying and targeting poor households as the TPDS has, but might have advantages in reaching remote areas where TPDS shops are not viable, and in subsidizing foods, particularly coarse grains, that are important for poor households in some areas but are not handled by the TPDS.

A key precondition for implementing a food stamp program in India is development of an administratively workable system of issuing and redeeming coupons that will prevent food stamps and program benefits from being used fraudulently. Another issue is concern about loss of government control of physical grain markets and private traders in the current system. The potential benefits of shifting to a food stamp program are discussed in India's 10th Five Year Plan (Government of India, Planning Commission, 2002). To date, there has been a small State-level food-coupon scheme in Andhra Pradesh, with plans for a food stamp pilot project in Maharashtra that is intended to evaluate the feasibility of implementing the program on a larger scale (Ramaswami, 2002; Ramaswami and Murugkar, 2005).