

# Right to Food and Foodgrain Policy

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Identification of the poor and the scale of operation are the most critical challenges of the proposed legislation on the right to food. This article suggests universal entitlement that excludes clearly identifiable rich. Food coupons could eliminate the need for the operations of public distribution system and eliminate diversion. Also cash transfers to the women of the household through Aadhaar cards could substantially reduce diversions and avoid the problem of distribution of food coupons.

The proposed legislation on the right to food poses a number of challenges. Identification of the poor and the scale of operation are the most critical ones. Apart from the large financial outlay involved, the disincentive impact can lead to a significant fall in production of foodgrains unless an effective mechanism is created either through the Food Corporation of India (FCI) or state agencies to procure foodgrains from every nook and corner of the country. These challenges can be better appreciated in the context of our food policy and experience so far. This article suggests a universal scheme excluding the clearly identifiable rich to effectively provide food security to the poor.

## Present Policy

The present foodgrain policy was initiated when foodgrains were the major item of consumption of people. It seeks to ensure adequate domestic production through assuring a minimum support price (MSP) to farmers, providing subsidised fertilisers and irrigation water as well as electricity for pumping.

At the same time, it seeks to provide foodgrains to consumers at a low price through the public distribution system (PDS) under which ration card holders get subsidised foodgrains (and some other items) up to their ration entitlements. Consumers are free to purchase additional quantities in the open market. The government bears the burden of difference

between the ration price and the cost of supply. PDS was initially operated only in urban areas and covered all residents. It was expanded to rural areas and has been tweaked in many ways over time. At present under the targeted PDS (TPDS), households are classified as those below the poverty line (BPL) and those above the poverty line (APL). The BPL households get foodgrains at a much lower price than the APL households.

The PDS is operated through the FCI which procures food from organised grain markets, stores and distributes to states for further distribution through ration shops under PDS. The FCI operations also serve the purpose of buffer stock management.

The MSP is set by the Commission for Agricultural Costs and Pricing (CACP). In recent years, the MSP has often become the maximum price when supply exceeds demand at MSP. The FCI then ends up buying foodgrains beyond its need for PDS or buffer stock operation and builds up stocks more than its desired level. Over the past few years wheat and rice stocks have been way above the desired stock levels.

To facilitate procurement by FCI in surplus states, foodgrains movement across states was restricted. Under the Essential Commodities Act (ECA) 1955, movement and storage by traders was restricted. In 2003, this was modified by an order that stated:

[A]ny dealer can freely buy, stock, sell, transport, distribute, dispose, acquire, use or consume any quantity of wheat, paddy/rice, coarse grains, sugar, edible oil seeds, edible oil, pulses, gur, wheat products and hydrogenated vegetable oil or vanaspati shall not require any licence or permit thereof.

The Agricultural Produce Market Committee (APMC) Act, a state-level Act, regulates agricultural marketing. Under this sale and purchase outside the market are

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prohibited and that agro-processors procure raw materials only from the notified markets. Thus, a few “licensed” or “registered” participants/agents/traders effectively controlled the markets and the Act became a deterrent to the development of competitive markets (Kumar et al 2007).

The APMC Act has been revised in a number of states but the process needs to be completed. The distortions in foodgrain markets put a large wedge between consumer price and producer price. Thus, producers get less than what they should and consumers pay more than what they need to. As Kumar et al (2007) note,

well-functioning private markets require completing the reform of the APMC Act, permitting direct purchase from farmers, abolishing restrictions on storage and movement, permitting warehouse receipts and opening import and export by private traders. Farmers and consumers can be protected from the excesses of markets through appropriate but minimal interventions by the government.

**Outcome of the Present Policy**

**For Producers:** The present policy has achieved the target of encouraging domestic production of foodgrains to meet domestic demand. India has been a net exporter of cereals since 1995. However, this has been achieved at high cost and one could ask the question if it could have been achieved at a much lower cost. The burden of subsidies for fertilisers, irrigation and power has been huge, 2.04% of gross domestic product in 2009-10.

Also, to ensure that prices do not fall below MSPs, the FCI has to buy wheat and build up stocks. Basu (2011) has noted that from 1 April 2003 till 1 April 2010, the stock of wheat and rice, every quarter was above the buffer stock norm. The excess stock varied from a low of 70% to a high of 207% above the norm. Moreover, the FCI operations are concentrated in a few states. Thus, over 80% of rice is procured from only five states and over 90% of wheat from three to four states (see the Figure).

As a consequence farmers in other states are not always assured of MSP.

This has also distorted cropping patterns. Thus, Punjab grows rice using a lot of water, much of it from tube wells that depresses the groundwater table. Also cheap electricity leads to the overuse of water resulting in soil degradation due to waterlogging and salinity.

A study of hypothetical extension of wheat and rice procurement in Uttar Pradesh and Madhya Pradesh showed that if procurement is extended to all districts and if the additional foodgrains are distributed in the same district, it would improve the welfare of poor consumers as well as farmers, but at the cost of higher fiscal outlay by the government (Parikh and Singh 2007).

**For Consumers:** The main instrument for providing foodgrains at low prices to poor consumers has been the PDS and its current incarnation the TPDS. The effectiveness of PDS in reaching the poor consumers was first examined by Parikh (1994) based on household level National Sample Survey (NSS) data for the year 1986-87.

The paper found that (i) In most states more than half the poor did not get any cereals from PDS. Among those who got any cereals from PDS, the average among the poor was less than 3 kg per person per month. (ii) The value difference between PDS price and the price at which the households in the quintile group brought from the market came to around Rs 3

the bottom quintile obtained 17% of their foodgrains consumption from PDS for the country as a whole. The percentage varied from 2% for Bihar, 6% for UP to 50% for Tamil Nadu and 68% for Karnataka (Dev and Sharma 2010).

**Table: Percentage of Households in Each Quintile Purchasing Rice/Wheat from PDS**

MPCE Quintiles	1993-94	2004-05
Bottom 20	29.2	35.5
Next 20	27.8	28.1
Next 20	27.1	23.2
Next 20	25	18.5
Top 20	21.7	11.5
Total	26.2	23

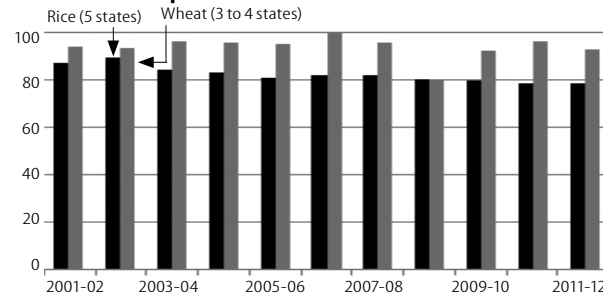
Source: Himanshu and Sen (2011).

Access to PDS has also been inadequate (Himanshu and Sen 2011). The small improvement for the bottom quintile seen in the table between 1993-94 and 2004-05 is the outcome of the TPDS. Yet even with the TPDS in 2004-05 only 35.5% of the households in the bottom quintile purchased rice/wheat from PDS. Himanshu and Sen also note that through leakage of rice and wheat implied by NSSO, estimated consumption and amounts released for PDS have come down from 55% in 2004-05 to 43% in 2007-08 and the leakages are still substantial. Khara (2011), who comes to similar estimates for 2004-05 and 2007-08, estimated 23.9% diversion of PDS grains in 1990-2000. With TPDS, the difference between market price and ration price increased and that may have provided greater incentives for diversion.

Jha and Ramaswamy (2011) have estimated that the income support provided to the poor in 2004-05 through PDS was Rs 2,100 crore, whereas the total subsidy was Rs 20,400 crore. Thus of these 20,400 crore, only 10% accrue to poor, 19% to non-poor, 28% is due to excess cost of operation and 43% is due to illegal diversion.

To sum up, (i) PDS has a large exclusion error and does not reach most of the poor. (ii) It provides only a fraction of foodgrain consumption of the poor households. (iii) The money value of income transfer through PDS grains is also modest. (iv) The poor get a bit more than 10% of the total subsidy expense of the government. (v) More than 40% of the PDS grains do not reach the consumers.

**Figure: Percentage of Total Procured Rice from Top Five States and Wheat from Top Three to Four States**



Source: Author by using data source of FCI.

per person per month. (iii) For reaching Re 1 of income support to the poor, the government spent more than Rs 5 for PDS operations.

This story has not changed much. As per the 2004-05 NSS round, households in

To take care of some of the ineffectiveness of the present PDS, use of food coupons was discussed by the *Economic Survey 2009-10* (GOI 2010). A person can go to any shop and buy food items at market price paying part of the cost through food coupons. The trader can exchange the coupons for money at any bank. These coupons would eliminate the diversion of PDS grains by the traders. In fact, it will eliminate the PDS itself. It would, however, involve the problem of printing and distributing the coupons to the poor, who will have to be identified.

### Effectively Reaching the Poor

The messy problem of printing and periodically issuing coupons can be eliminated with the use of Unique Identification Number under the Aadhaar Scheme. But even with the Aadhaar cards, the task of identifying the poor remains. The large exclusion and inclusion errors of the present system of issuing BPL cards will still persist.

One way to deal with the exclusion error is to go for a universal right to food under which everyone is entitled to get subsidised foodgrains from the PDS. This was proposed by the National Advisory Council. The proposed Food Security Bill was adopted with some modifications by the empowered group of ministers (EGOM) on 11 July 2011. The draft, which after cabinet approval was placed in Parliament, provides rice at Rs 3 per kg, wheat at Rs 2 per kg and coarse grains at Re 1 per kg to priority households. Forty-six per cent of rural and 28% of urban households are to be priority households. The scheme will cover 68% of the population and government's subsidy outlay will increase to around Rs 75,000 crore, though I estimate that it will be Rs 95,000 crore.

The scheme will face two problems. First, how to identify the priority households to eliminate exclusion errors and minimise inclusion errors? Second, how to control diversion, the incentives for which are now much larger, and how to make a much more enlarged PDS cost efficient?

Instead of identifying the poor, it would be a lot easier to identify the rich to exclude them. A better way to provide

food security to the poor is to make it universal, but exclude the clearly and easily identifiable rich. So, that all poor will be covered even at the cost of some undeserving rich getting covered. If all those who pay income tax, those who own motorised vehicles and all those in organised sector, including government, with monthly emoluments of more than Rs 15,000 are excluded, the inclusion errors could be reduced. There are some 350 lakh PAN cards and 1,000 lakh registered motorised vehicles. Since rich households will have more than one PAN card and vehicles and also many of these belong to commercial establishments, it is not easy to say how many households will be disqualified on these grounds. A rough estimate can be around 300 to 400 lakh households. Further, reduction can be achieved through self-selection if, as observed by Kotwal et al (2011), households are themselves required to purchase rations with an Aadhaar card as many relatively well-off would not find it worthwhile to claim their rations. In any case the present PDS has an inclusion error. Undeserving rich belonging to the top 3 quintiles having BPL cards constituted 40% of all BPL card holders in 2004-05 (based on the Table 2 of Himanshu and Sen 2011).

The second problem of diversion can be taken care of by providing food coupons or Aadhaar card-linked entitlements that can be purchased at any shop. This will eliminate the problems of having to procure and distribute more than 500 lakh tonnes of foodgrains every year as also the problem of diversion. The costs of the PDS system would be greatly reduced. Of course, the problem of traders charging high market price in remote areas can be a real one. In such selected areas cooperative societies and even fair price shops may be encouraged which stick to prices announced every week by the government. International experience indicates that this can work, as in the case of the 22,000 cooperative DICONSAs stores in remote areas of Mexico who sell food and other necessities, and provide competition to private traders in thin markets of remote areas.<sup>1</sup>

Should entitlements be linked to purchase of foodgrains, or should one do

cash transfer? Linking transfer to purchase of foodgrains increases the transaction cost for the consumer which will encourage self-selection and better-off consumers will stay away. Another argument may be that it would encourage more consumption of foodgrains and increase nutrition. This, however, does not follow. Deaton and Dreze (2009) have observed declining consumption of cereal calories by rural households belonging to the poorest decile and the poorest quartile of expenditure levels. This suggests the poor may not want to consume more cereals and would prefer to consume other foods. Providing foodgrains may also not improve nutrition outcomes. As noted by Headey et al (2011), it is unlikely that insufficient calories are a binding constraint for much of Indian population. They also point out that Sharma (2006) observed a very weak correlation between calorie intake and nutrition outcomes at state and sub-state levels.

Also it is well-recognised that malnutrition relates to intake of the right kind of food during the first two years, the nutritional status of pregnant women and mothers during the period of lactation and also on access to clean water and sanitation facilities. Thus, there is no compelling reason to link foodgrain entitlements to actual purchase of foodgrains to improve nutrition.

An unlinked cash transfer will enable the family to spend the money as it wishes, say on milk or on sending the child to a better school. As is now well recognised, the transfer should be made in the name of the woman of the household to empower her. If this is done through Aadhaar cards, only she can use

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the money. A problem of linking entitlements to Aadhaar card is that the entitled woman or person may be unable to go to a shop due to sickness or some emergency. This can be taken care of by permitting two members of a household to avail of the entitlement.

Since transfer linked to Aadhaar can significantly reduce, if not eliminate, diversion, the total outlay even with near universal coverage can be much smaller than the present outlay. Thus, Rs 95,000 crore can provide Rs 4,700 per year to each of the 2,000 lakh households. If we assume that of the 2,400 lakh households in the country, 400 lakh relatively rich households can be excluded, the remaining 2,000 lakh households can be provided Rs 4,500 per year with the estimated outlay of Rs 95,000 crore keeping Rs 5,000 crore for administering cash transfers.

### To Summarise

- A universal entitlement that excludes clearly identifiable rich is preferable to one that seeks to identify the poor and restricts entitlements to only the poor.

- Foodgrains supply would have only a slight impact on the nutritional outcomes.

- Food coupons could eliminate the need for PDS operations and eliminate diversion. It would, however, involve printing and distribution of coupons, operations that may involve leakages.

- Cash transfers to the woman of the household through Aadhaar cards can substantially reduce, if not eliminate, diversions and avoid the problem of distribution of food coupons. It will also eliminate need for PDS operations.

### The Role of FCI

With nearly universal cash transfer through Aadhaar cards, the need for PDS operations would disappear. The FCI can then be charged with buffer stock operations. The level of buffer stock should be determined on the basis of minimising the expected cost of stabilising prices at desired levels and optimising the combined costs of domestic buffer stock and import/export operation taking into account the impacts on the world prices of India's trade (Parikh 1998).

The level at which price should be stabilised should be such that it balances domestic supply and demand on the average. The MSP should be a true minimum support price that should ensure that the price does not drop to a level where the farmers cannot cover all her costs and survive till the next season.

### NOTE

- 1 DICONSA is now piloting the provision of financial services by these stores with the support of the bill and Melinda Gates Foundation. <http://www.gatesfoundation.org/grantee-profiles/Pages/diconsa-financial-services-for-the-rural-poor.aspx>

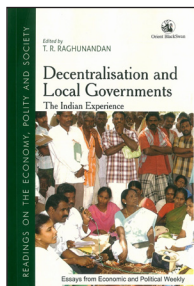
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## Decentralisation and Local Governments

Edited by

**T R RAGHUNANDAN**



The idea of devolving power to local governments was part of the larger political debate during the Indian national movement. With strong advocates for it, like Gandhi, it resulted in constitutional changes and policy decisions in the decades following Independence, to make governance more accountable to and accessible for the common man.

The introduction discusses the milestones in the evolution of local governments post-Independence, while providing an overview of the panchayat system, its evolution and its powers under the British, and the stand of various leaders of the Indian national movement on decentralisation.

This volume discusses the constitutional amendments that gave autonomy to institutions of local governance, both rural and urban, along with the various facets of establishing and strengthening these local self-governments.

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Pp xii + 432

ISBN 978-81-250-4883-1

2012

Rs 695

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