

## Gist of EPW July Week 3, 2021

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#### 1. The Uncertain Trajectory of Food Inflation: Fresh Triggers amid the Pandemic

##### Context

The article highlights the Food Inflation Trends and its spillover effects in the economy.

##### Introduction

- The retail inflation measured by the [Consumer Price Index](#) portrayed a volatile swing as it became moderate between December 2020 and April 2021.
- The food items, commanding about 45% weight in the CPI basket, consistently surpassed headline inflation since September 2019 and declined sharply in December 2020.
- The CPI of the food basket at a disaggregated level reveals that the higher level of food inflation was mainly driven by a price surge in vegetables and proteins in the early months of the lockdown.
- The demand–supply conditions in certain vegetables like onion and protein-based food items turned out to be the major driver in the wake of the pandemic.
- The spike in food inflation is usually witnessed during the summer months, which are highly correlated to monsoon patterns.
- The other exogenous determinants of food inflation are global food prices, fuel price and the extent of [minimum support prices](#).
- Warehousing facilities, speculative pricing of traders and the food supply management of the government also influence food prices in the country.
- The pandemic-induced supply bottlenecks have taken a toll on items such as vegetables, cereals, milk, pulses, and edible oils that emerged, of late, as underlying pressure points. In general, expenditure on food items have seen a sharp increase, both in absolute and relative terms, since the severity of the pandemic has sunk in.
- The outbreak of the COVID-19 pandemic points to an unusual trajectory of [inflation](#), especially with respect to food items amid changing demand and supply conditions.

##### Demand-side Factors

- The demand for food is inelastic, consequently the consumption remains unaffected even during price rise, and this may be more applicable for staple food items.
- Perceiving supply shortfalls, consumers resorted to frantic purchase of essential food items, which pushed up the demand and prices.
- The door-to-door delivery of food items due to restrictions made food items even more expensive than normal times.

- The enhanced urban consumption of items like proteins, oil, and fats as well as spices seems to have contributed towards the higher level of food prices.
- Since the second half of the fiscal year 2020, edible oil prices firmed up in tandem with the high global food price index.
- The higher level of edible oil prices and subsequent demand caused an imported inflation, which is continuing even now.

### **Supply-side Factors**

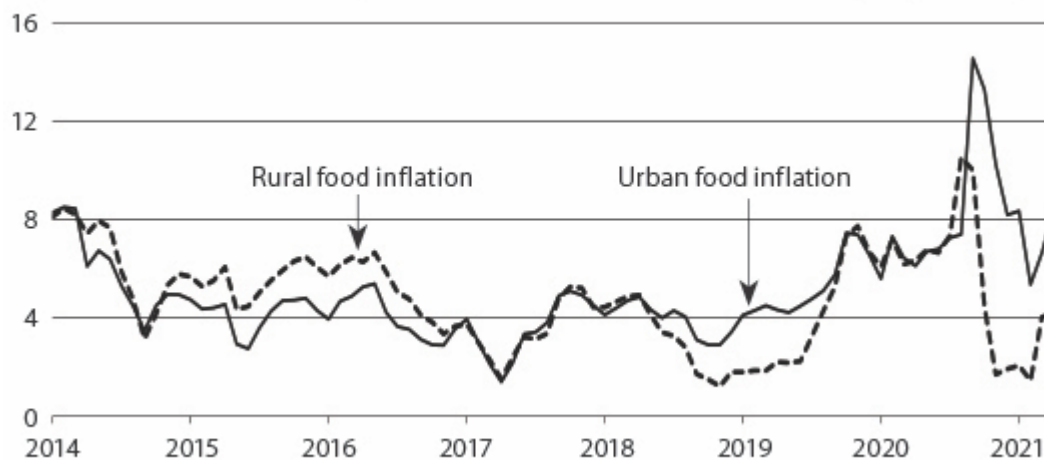
- The surging retail fuel price is one among them. The trajectory of fuel prices influences food inflation via transport and input costs like fertilisers, etc.
- There is a considerable positive correlation between food and fuel price indices. In a bid to make gains on the revenue front from the fall in global crude oil prices, the government increased excise duties on petrol and diesel, thus raising their pump prices.
- The oil-marketing companies revised the retail fuel price several rounds since June 2020 taking it to considerably higher levels.
- The elevated level of global food prices is another key factor influencing the near-term trajectory of food inflation in India. The influence of domestic factors and persisting supply gluts, with respect to the essential food items, seems to be the main drivers in the near term.

### **Scope for Stagflation In Present Scenario**

- The wedge between rural and urban food inflation since July 2018 stood as a matter of concern underscoring rural distress.
- The gap was more pronounced with respect to cereal, fruit, and vegetable prices. The slide in rural income and subdued demand in rural areas could be ascribed to this divergence.
- The lower level of income in rural areas prompted people to substitute with inferior food items. On the other hand, urban households continued to spend substantial amounts on food items.
- This wedge has closed ever since the pandemic started and with the consequent lockdowns.
- The rural–urban gap seems to have resurfaced in the latter half of 2020, pointing at the lesser resilience of the rural economy to the pandemic.

**Figure 1: Rural–Urban Gap in Food Inflation**

(YoY, percentage)



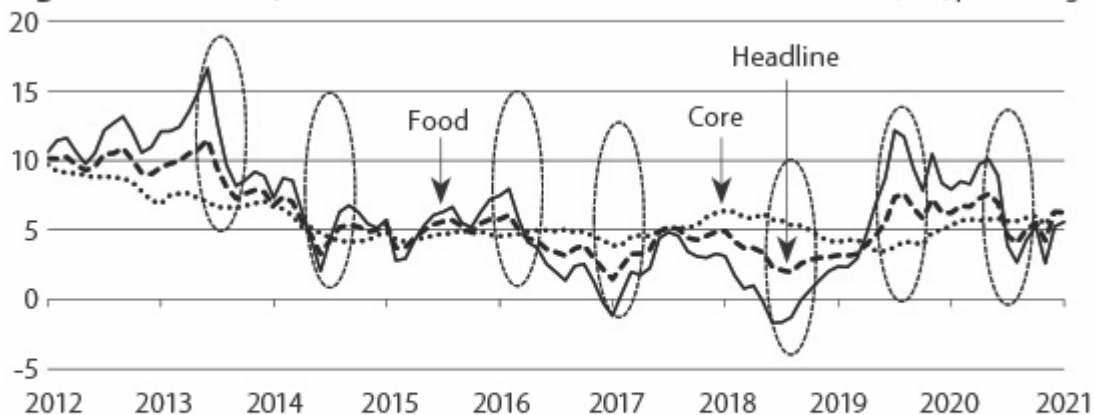
Source: MOSPI (2021b).

Image source: EPW

### Food Price Volatility

- Food price trajectory in India has a history of volatility due to various domestic and global factors.
- The 2013 food price spike, led by a surge in vegetable prices, was mostly driven by drought-induced shortages in food supply, rising international agriculture produce prices and sharp MSP increases.
- In 2014, the vegetable prices eased considerably leading to a free fall in food inflation. In 2015 and 2016, it once again surpassed the headline inflation mainly on account of higher prices in pulses as consumption demand continued to increase while production fell due to non-lucrative farm returns.
- The major part of 2017 and 2018, inflation due to lower prices of vegetables and pulses, and the food inflation broadly remained lower than the headline figures.
- The path of softening food prices saw a reversal and started surpassing the headline inflation prints. Food prices saw an uptick even during the winter months of fiscal year 2020, which is otherwise a period when they are seen to be subdued.

**Figure 2: Headline, Food and Core Inflation Trends** (YoY, percentage)



Headline is the inflation measured by CPI. Core inflation excludes food and fuel inflation. The dotted circles highlight volatility in food prices.

Source: MOSPI (2021b).

Image source: EPW

### Food Inflation And Food Security

- The other broader implication of food inflation is related to food security as the spillover of inflationary effects is likely to be felt in other sectors as well.
- A sharp rise in inflation without corresponding increase in incomes or wages leads to a decline in real income and consumption expenditure.
- While food in general is a necessary commodity, and hence the demand for it is inelastic, high inflation rates may lead to switching within the food basket to inferior products, thus impacting the nutrient value of the overall consumption basket.
- The elevated levels of food prices during the event of lower income levels and subdued demand leads to a further decline in purchasing power and weaker substitution effect. With evidence of a widening gap between rural and urban food inflation, rural distress seems to be evident, affecting the nutritious food intake of this population.

### Conclusions

- The pandemic unfolded changing demand and supply-side factors influencing the food inflation trajectory in the country.
- The upside risk to food prices is determined largely by factors like heightened international price of edible oil and pulses, causing an imported inflation.
- The reduced supply in the main producing and exporting markets pushed up the prices.
- Also, the high petrol and diesel prices have a cascading effect on the food price through the channel of increased input cost price.
- The present situation demands a more focused food supply management to tame the elevated food price in the coming months and thereby mitigating its impact on rural income and inflation.