

# Indo-US Food Agreement

## And State Trading in Foodgrains

H Laxminarayan

[ SINCE the commencement of the programme of food aid to India in 1954 under Title I of the II, S. Government Agricultural Trade Development Assistance (Public Law 480), five agreements have been signed between the United States Government and the Government of India. The P. L. 480 agreements aim at supply of surplus agricultural commodities from the U.S.A. against payment of the rupee equivalent of the dollar cost of these commodities plus 50 per cent of the ocean freight cost. The proceeds realised by the sale of these commodities are credited to the account of the U. S. Technical Cooperation Mission in India and are to be spent on programmes approved by the Government of India. The total value of the commodities imported under P. L. 480 in the period August 1956 to November 1959 comes to approximately Rs. 452 crores. The quantity of foodgrains involved amounted to 10.5 million metric tons of wheat, 2 lakh metric tons of rice, 1.8 lakh metric tons of corn and some quantity of maize. Out of the total proceeds realised by sale of P. L. 480 commodities, a sum of Rs. 234 crores has been given as loan to the Indian Government, Rs. 93 crores as grant for economic development, and the balance for such purposes as the expenses of the U. S. Embassy and mutually agreeable loans.

These above are exclusive of the assistance which this country is going to receive under the fifth P. L. 480 Agreement which was signed on 4th May 1960. The new agreement is for an amount almost four times as large as in any agreement previously signed by U. S. A. with any country since the commencement of P. L. 480 programme. This would enable us to import from U. S. A. 16 million metric tons of wheat and 1 million metric tons of rice valued at Rs. 1700 crores over a period of 4 years.

An important aspect of the present agreement is that half the aid will be supplied gratis while the other half will be given on credit

repayable in rupees over a fairly long period of time. As in the previous P. L. 480 agreements, the proceeds realised from the internal sales of these commodities would be available\* for financing some of the developmental programmes during the last year of the Second Five Year Plan and first three years of the Third Five Year Plan.

Though the main features of the last P. L. 480 agreement do not differ from those of the previous ones, its implications are different at least in two respects. Firstly, the quantum of assistance assured is of a considerably larger magnitude. While our normal import of wheat would be of the order of 3 million metric tons per year, the present agreement envisages the import of about 4 million metric tons of wheat plus 2.5 lakh metric tons of rice per year. Thus the proposed import of 4 million tons per year would form as much as 40 per cent of our domestic production of wheat which stood at 10 million tons in 1958-59. After making allowance for the normal import of 3 million tons of wheat per annum which should be sufficient to meet our internal deficit, we would be left with a net surplus of one million tons every year. At this rate, we should be able to accumulate a buffer stock reserve of about 4 million tons of wheat and one million tons of rice over a four year period. A food reserve of 5 million tons should serve as a safe reserve for all emergencies.

The other distinguishing feature of the agreement is that unlike the previous agreements, it is a long term arrangement. The latter would provide a useful base for any anti-inflationary measure that we may have to take during the Third Five Year Plan period.

The experience gained during the first two plans suggests that building up of food reserves is one of the most crucial factors that determine the rate of growth of the economy. An adequate buffer stock of food would pave the way for a higher volume of deficit financing and increased savings and investment.

as any increase in demand for food grains resulting from increased income could easily be met. The first Five Year Plan could progress smoothly and most of the targets could be attained mainly because the food situation was easy. The food situation during 1953-54 and 1954-55 was so comfortable that the rate of investment could be easily stepped up from Rs 343 crores in 1953-54 to Rs 667 crores in 1955-56. The dissipation of savings of the community due to decline in food prices during 1953-54 and 1954-55 indicates that there was scope for further stepping up of the rate of investment without generating inflationary forces.

In contrast to the First Plan, the Second Plan did not pay adequate attention to the food problem, in fact it under-emphasised the importance of food supply in a developing economy. Though this was realised soon after and food targets were raised subsequently, no effort was made to match the higher target with an increased outlay on projects which could help to raise food output. While the total plan outlay was stepped up, it was not accompanied by an adequate increase in food output. While the total investment target (inclusive of investment in the private sector) was raised from Rs 3,360 crores during the First Plan to Rs 6750 crores in the Second, the target of food production was raised from 65.8 million tons in last year of the First Plan to 80.5 million tons in the last year of the Second Plan. Even though this target can by no means be considered as very ambitious the likely achievement might not exceed 75 million tons. The internal production stood at 73.5 million tons during 1958-59 which happens to be the third year of the Second Plan. With the 1959-60 output slightly lower than this, one can safely presume that we are not likely to attain the target.

Due to the high income elasticity of demand for foodgrains in a developing economy, stepping up the rate of investment without adequate measures to increase food supply

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led to dislocation of the price structure. While factors like increasing population and urbanisation were also responsible for increased demand for foodgrains, the main pressure came from higher plan investments and the resultant increase in income. The sharp increase in the demand for foodgrains led to an increase in food prices. As compared to 1955-56, which was the last year of the First Plan, food prices increased by 37.4 per cent during 1959-60 (fourth year of the Second Plan) as against an increase of 26.5 per cent in the general price level. Prices of industrial raw materials increased by 25 per cent and those of manufactured goods by 11.8 per cent. Thus price increases were much higher in the case of foodgrains. This diverted a substantial part of people's income from urban goods to food articles. The terms of trade between the industrial sector and the agricultural sector went against the former. Since a large proportion of rising income was frittered away in the form of higher prices paid for food, it was not possible to sustain the higher rate of investment and the Second Plan investment in the public sector was reduced from Rs 4800 crores to Rs 4600 crores. Our achievements in terms of physical targets may be even lower, due to the higher investment costs of many projects.

## II

The review of nine years of economic planning given above will pinpoint the strategic role of a sizeable buffer stock of foodgrains in a developing economy. Against this background, the latest Indo-U. S. Food Agreement must be considered as an important stabilizing factor in an otherwise\* deteriorating situation. Apart from the fact that the counterpart funds realised by the internal sale of P. L. 480 commodities would be available for economic development of the country, the Agreement may be expected to exert a stabilising influence in three different ways.

### BUFFER STOCK PLAN

First, the buffer stock plan is of such a magnitude that it is bound to have a healthy effect on food prices. It will be possible to arrest adverse price movements of one kind or another by undertaking large scale open market operations in scarcity

areas like Eastern U. P. and Northern Bihar and marginal areas like certain parts of Rajasthan. In these areas even marginal shortfalls in food production leads to sharp rise in prices due to hoarding of stocks and speculative activities. Unless timely action is taken to correct these trends, even marginal shortages in some parts of the country may lead to sharp rise in prices in other parts, particularly when crores of rupees are being invested in projects with long gestation period. These imbalances can be corrected and violent fluctuations prevented by buffer stock operations with the help of P. L. 480 foodgrains.

Second, almost throughout the four years of the Second Plan, the price structure has been distorted by the sharp increase in food prices as compared to the prices of other commodities. Apart from raising prices of industrial raw materials like sugarcane, high price of foodgrains has been a major factor responsible for a slackening of demand for manufactured goods. The P L 480 assistance will go a long way in correcting the discrepancy between the prices of food and non-food articles, paving thereby the way for increased industrial activity. This statement is based on the assumption that the entire income released as a result of decline in food prices is not spent in the form of increased consumption of food articles. In a country where people are used to a sub-standard of living' it is essential to take precautions against this danger. Any decline in food prices will also reduce the burden of cost of living allowance paid to workers in both private sector and public sector projects. To this extent our investment costs are bound to go down appreciably.

Third, apart from the fact that import of food under P L 480 does not involve any burden on our foreign exchange reserves, it will have the added advantage of reducing the strain on our balance of payment position. Any reasonable decline in food prices will be a welcome factor in the direction of improving our balance of payments.

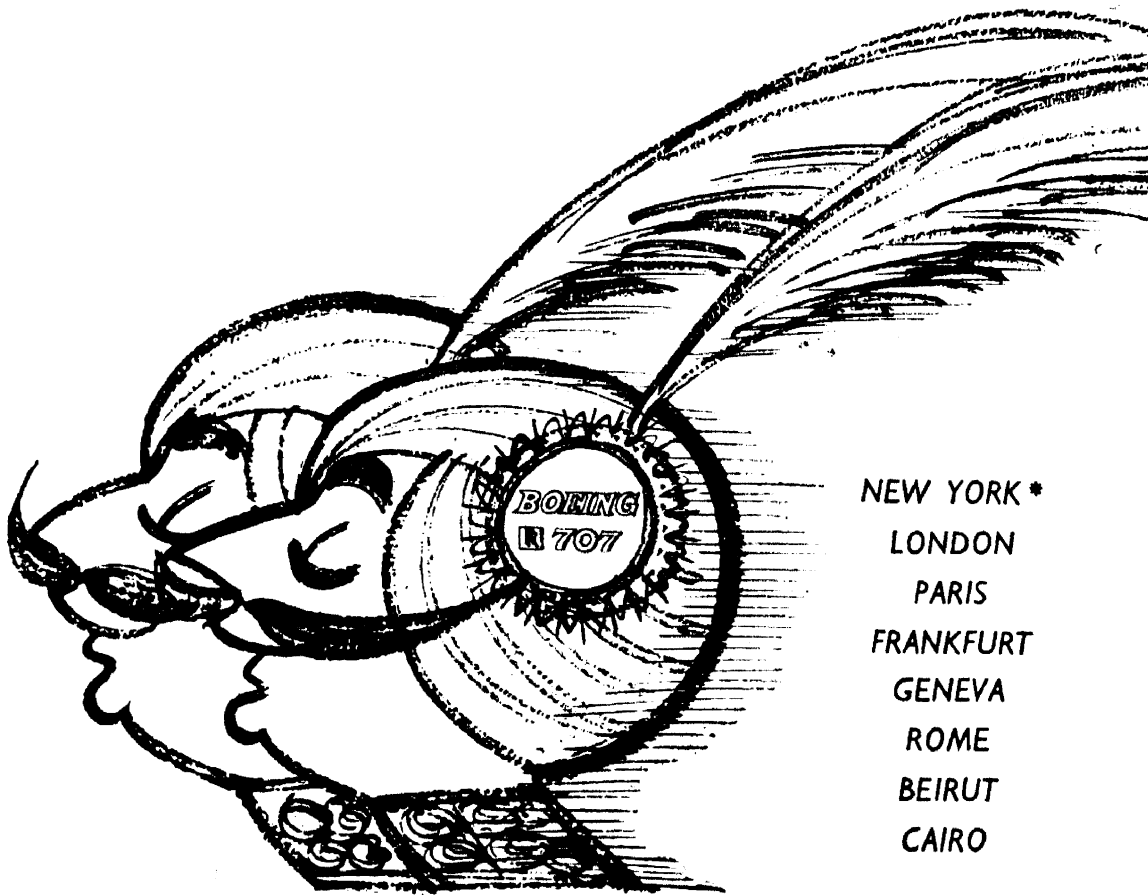
## III

While the P L 480 agreement would provide us a brief respite from food problem for a period of

4 years so that we can concentrate our energies on the task of building up the economy, the intervening period should be utilised for putting our food economy in order. The buffer stock is not of such a magnitude as to solve our food problem for all time to come. Two or three crop failures may entirely wipe it out. Even within the limited span of four years, the food aid might not provide a solution to many of our problems. The points to be considered are mainly four in number.

First, import of so large a quantity of foodgrains as 4.25 million tons a year is bound to have a depressing effect on food prices. Since our normal food deficits would be of the order of 3 million tons, the pressure on prices will primarily come from the additional import of 1.25 million tons. The problem created by the imports will assume serious proportions as we move from one year of the Plan to the other, since there will gradually be a large increase in the size of our buffer stock. It is going to be a problem of some magnitude, considering that even marginal increases in food production have led to a decline in prices in the past. It is not so much the imbalance between supply and demand for foodgrains which is responsible for price changes as the behaviour of marketed surplus. Past experience shows that food prices have generally declined under the impact of increase in marketed surplus as both the producers and the traders, would be anxious to get rid of their stocks.


In view of this situation increased food imports are bound to lead to a depressing effect on food prices as they would produce the same effects as excessive internal production. The Indian farmer who has been used to high food prices during the last five years may not react favourably to a sudden decline in food prices. Apart from the political pressure which he may try to bring, his reaction might take the form of shifting over to production of commercial crops in which case the domestic production of foodgrains might decline. Though this shift in the pattern of production might temporarily benefit the industrial sector in the form of more and cheaper raw materials, from the long run point of view this development, is not desirable as it may drive us to depend more and more



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on external assistance for a vital commodity like food.

#### TO PREVENT PRICE DISTORTION

In order to prevent developments of this nature two remedial measures will have to be undertaken. First, the buffer stock operations will have to be carried out in a planned way so that no distortion of the price structure takes place. The Foodgrains Enquiry Committee rightly recommended that whenever food prices tend to fall, even if such a fall is not general but is confined to a particular locality, the buffer stock organisation should step in and start purchasing at reasonable prices and when prices tend to rise this organisation should sell at reasonable prices. Save during exigencies like crop failures, in order to assure a fair price to the producer, it would be best for the buffer stock organisation not to enter the market during the first few months following the harvest season as most of the marketable surplus arrives in the market during this period. During this period even a certain degree of price rise may be permitted so long as it is within reasonable limits. A certain degree of price increase during this period may even act as an incentive for increasing the marketed surplus.

As far as possible the P.L. 480 foodgrains should be released in the market only during the lean months when food prices show a tendency to rise sharply. However, the task of formulating a simple rule in this matter is not easy. Whichever period of the year the Government may choose for releasing the stocks, the guiding principle should be one of assuring a fair price to the producer without sacrificing the overall objective of price stability. Moreover, the internal food situation may turn so favourable that it might not be necessary for us to draw from stocks at all. The very fact that the Government is in command of huge reserves of foodgrains may itself act as a strong deterrent against all speculative activities on the part of both the trader and the producer. The effect which P.L.480 aid is going to have, on the psychology of all sections of the population is a very important part of the buffer stock strategy.

The second remedial measure is to guarantee a minimum price to the cultivator. The guaranteed minimum should be fixed in such a way that it takes into account the

cultivators income and production costs. While determining production costs, due consideration should be given to prices of means of production like fertilisers, iron and steel and cost of capital improvements needed on land, it is equally important to take into consideration the prices of urban goods like cloth and kerosene which form an integral part of the cultivator's consumption. Once the cultivator is assured of a minimum price, buffer stock operations can be planned in such a manner that the cultivator will not react adversely when prices fluctuate within reasonable limits.

#### DIVERSION OF DEMAND

The second point to be taken note of while utilising the P L 480 aid relates to building up of capacity for production of non-food articles. Since food prices are bound to decline to an appreciable extent, it is necessary to ensure that the extra purchasing power so released does not exert any undue pressure on non-agricultural goods. No doubt, it is true that in the case of industries like cotton textiles, there is some degree of excess capacity. In these cases, increased demand resulting from release of purchasing power may easily be met by a more intensive utilisation of the installed capacity. In the case of other industries like sugar, where there is no excess capacity, increased demand due to release of purchasing power is bound to have some adverse repercussions. In these cases prices will increase under the pressure of increased demand.

Thus we may be compelled to increase the production capacity of non-food articles. However due to the tight foreign exchange position, we may not have facilities to increase the production capacity of these industries to an appreciable extent. In that case we will have either to allow the foreign exchange position to deteriorate further or we may have to allow some price increases. In the latter case, trade unions might press for wage increases in order to neutralise the rise in cost of living either partially or wholly. A phenomenon similar to this has been happening in our economy during the last one year or so. The two good harvests (inclusive of the present one) did lead to an increase in the purchasing power of the rural masses and this resulted in increased demand for non-

food articles like cloth and sugar. The price increases led to considerable increase in the cost of living and the resultant demand for higher wages by the trade unions. While utilising the P L 480 aid we will have to take certain protective measures against the reoccurrence of a phenomenon like this.

#### STORAGE CAPACITY

Third, we will have to increase our storage capacity for keeping the additional imports of foodgrains. Out of the annual import of 4.25 million tons, 3 million tons represent normal imports. The main storage problem will be in the case of the remaining 1.25 million tons. This problem might assume serious proportions if we proceed on the assumption that at the end of the four year period we will have to find place for stocking a reserve of at least 5 million tons of foodgrains.

In view of this problem we will have to bring about a carefully planned increase in the storage capacity. Our existing storage capacity does not seem to exceed 2 million tons. Since we have speeded up storage construction during the last two years, at best we may hope to add a capacity of 1 million tons by the end of the Second Five Year Plan. However the problem of increasing the storage capacity might not prove insurmountable provided we use a part of the funds made available by the sale of P L 480 commodities for purposes of constructing godowns.

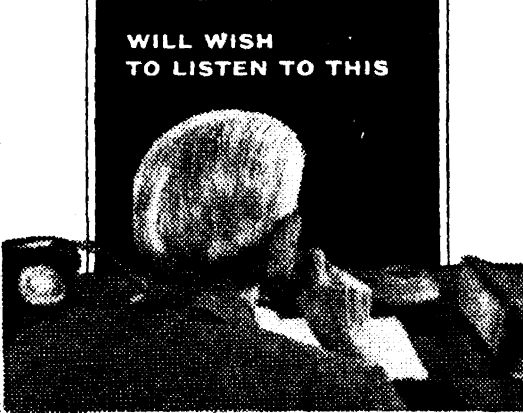
#### PROBLEM OF RICE

Fourth, our food problem is mainly one of shortage of rice since most of the P L 480 aid would be in the form of imports of wheat. In a predominantly rice eating country there is no short cut solution to this problem and we must increase production of rice. While wheat deficits can easily be met by importing wheat even from countries like Canada and Australia, it is not possible to increase rice imports by similar measures. By and large the world is deficit in rice supply. Assuming that we would be able to increase our rice imports from countries like Burma, Thailand and United Arab Republic, the surplus of all these countries together would no more than touch the fringe of the problem. Import of rice from some of these countries is by no means easy and in any case, none of these countries are in

ASP/LIC-E-17

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a position to give us rice on terms similar to the P L 480 aid. If we want to build up a substantial buffer stock of rice we can do so only by rigorous internal procurement.

Lastly, the P L 480 aid might give rise to an atmosphere of complacency, particularly in the official circles. Already it has created an impression that our food problem is virtually solved. Once this complacent attitude sets in, the organised efforts required for making this country self-sufficient in respect of food supply will not be forthcoming.

### Company Notes

#### **Escorts Issue**

ESCORTS will shortly announce a Rs 41 lakh public issue of share capital. This will comprise 17 lakhs of equity at a premium of 50 per cent on face value and Rs 21 lakhs of 6.3 per cent tax-free redeemable cumulative preferent shares. Almost the entire preference issue has been underwritten by the L j C. National and Grindlays. New India and National Employers Mutual, and by foreign collaborators like M A N, Westinghouse and Rheinmetall.

The company more than doubled its share capital to Rs 47 lakhs last year. The new issue will increase the share capital to Rs 88 lakhs. Net earning on net worth in 1959 was nearly 22 per cent and preference dividend was covered 10 times. Earnings per equity share was Rs 3.76 and dividend Rs 2.60 gross or Rs 1.482 net (see p 719, issue of May 14 1960).

Funds raised from the public issue will be utilised for the establishment of three factories which will manufacture x-ray equipment (with Westinghouse), rail shock-absorbers (with Rheinmetall), and heating elements for electric appliances (with Eltra). The requisite licences under the Industries Development and Regulation Act have been obtained, land has been purchased and building plans are in progress. Licences for the import of capital equipment for these projects are expected to be issued shortly.

For over a decade, Escorts has represented world-famous firms like M A N, A E G, Massey-Ferguson and Westinghouse in India, it has exclusive representation in India of

In the long run, the solution to our food problem will have to come through our own efforts. This will depend as much on the initiative of the Government as on that of the people. In view of this danger involved in the P L 480 aid, every effort will have to be made to see that a sense of complacency does not overtake the people. We should not depend on the P L 480 aid for any thing more than the temporary respite which it provides for stepping up our food production and development of our agriculture. Development of agriculture is the

basis for industrial investment. Creation of a surplus in the agricultural sector is necessary for meeting the higher consumption of the non-agricultural sector and the absorption of surplus labour from the agricultural sector. Employment opportunities can expand as rapidly as the population only by increasing the per capita output in agriculture. It is therefore essential that the Indo-LS Food Agreement should not lead to slackening of internal efforts.

(To Be Concluded)

KOEL Diesel Engines over 100 H P made by Kirloskars under M A N licence, and cranes of all types manufactured by Hindustan Motors, also under M A N licence. Since early 1948, the company has arranged sales, erection and service of heavy and light machinery including agricultural equipment worth over Rs 80 crores. During the last three years, moreover, Escorts and its subsidiaries have successfully established their own manufacturing plants for pistons, piston rings, sleeves and razor blades in collaboration with Goetze, Burshied and Mahle, all of them well known German firms,

#### **India Reinsurance**

THE gross premium income of India Reinsurance in all departments in 1959 increased to Rs 3.55 crores from Rs 2.84 crores and net premium to Rs 1.82 crores from Rs 1.26 crores. A large part of the increase was in respect of Indian Fire business. Total departmental reserves went up to Rs 87 lakhs from Rs 55 lakhs. The year's operations resulted in a profit of Rs 5.23 lakhs, slightly higher than in the previous year. The directors have recommended a first dividend of Rs 25 per share of Rs 500, which absorbs almost the entire profit.

The company has achieved an impressive reduction in the ratio of claims, commission and management expenses to net premium. This reduction enabled it to raise the ratio of increase in reserves to net premium from 4.82 per cent to 10.75 per cent. The Fire results would have been even better but for the disastrous experience in the U K. The Marine department has shown a small loss, but its results are ex-

pected to improve substantially in the current year, the facultative business is expanding and the Reinsurance Exchange is working 'very satisfactorily'. As a result of the lead given by the Corporation, uniform procedures and rates are being evolved for guarantees in connection with hire purchase transactions in motor vehicles. In collaboration with the efforts of another leading insurer, the Corporation has succeeded in reducing the premium rates on insurance of Indian Hulls,

The principal sources of drain out of India occur on account of reinsurance of Aviation and Marine Hulls, and Fire. The drain on account of Fire business is expected to dwindle once 'normal experience' is restored abroad. The Chairman, Shri A D Shroff, has suggested that the drain could also be reduced by forming Pools of Indian business suitably protected, in which each insurer would contribute from its surplus upto a defined maximum liability per risk and redistribute the business in the ratio of business received from each participant. Business so pooled and processed could be retained in India. The Chairman hopes that once the adverse cycle on foreign business turns favourable, and normal experience on overseas business is realised, the arrangements made so far will enable the Corporation to achieve its objectives in a substantial measure. In this context, he has deplored the Government's decision to convert Indian Guarantee, a subsidiary of L I C, into a professional reinsurance company. The trend abroad in the insurance business is towards amalgamation of separate units in order to reduce the costs of handling.