A controversial step

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THE recent decision of the Punjab government to ban the movement of wheat out of the province until it procures 3.5 million tons of the commodity, has evoked a sharp reaction from other provincial governments as problems of non-availability have caused the price of wheat/atta to soar.

Both the Pakistan and Punjab governments see their role in balancing conflicting interests, assuring farmers of a minimum remunerative price for their crops, while keeping the price of food products low for consumers. In this regard, wheat, which accounts for around 30 per cent of the value-added by major agricultural crops and that is produced largely by small growers, has strategic importance both economically and politically.

> Punjab government's decision to ban the inter-provincial movement of wheat is not only misplaced but also fails to achieve what are ostensibly well-intended objectives. The Punjabi farmer is losing out on a higher price that he would have earned if the market had been allowed to operate freely. The price of wheat in the deficit provinces will continue to be high unless they are allowed to import wheat from abroad.

Among the provinces, only Punjab produces surplus wheat. Until the policy decision in 2001 to allow free sales and movement of wheat across district and provincial boundaries, farmers were only theoretically at liberty to sell their wheat to anyone. In practice, provincial governments frequently resorted to the imposition of Section 144 to prohibit the inter-provincial/district mobility of wheat during harvest time. This has again been resorted to by the Punjab government, which has caused bitterness between it and other provincial governments.

The restrictions on the movement of wheat is forcing farmers to part with their wheat at depressed prices, below the market price of the crop, thereby defeating the purpose of establishing support prices, with the procurement price having effectively become the maximum/ceiling price. Punjab's claim that it has imposed this ban partly to check the smuggling of wheat is ill-founded.

There have to be market-oriented solutions to curtail smuggling. If the difference between the domestic price of flour and the price in neighbouring countries like Afghanistan is large, and the cost of smuggling and the chances of being caught low, the incentive to smuggle wheat will remain high.

Attempts to develop alternative means of checking smuggling will only meet with partial success. In such a case, the only effective solution to the problem of smuggling is the elimination of the subsidy, the alignment of domestic prices with prices on international borders and the removal of all restrictions on the inter-regional movement of wheat.

One supports the decision of the federal government to scale down public sector intervention in the market for wheat and allow an expanded private sector role. All other policy instruments will neither eliminate the rent-seeking opportunities for government officials nor facilitate the achievement of a more efficient allocation of resources.

However, in view of the private sector's experience of inconsistency in and the unpredictability of government policies, the private sector will adopt a wait-and-see approach before committing itself to any major investment in activities pertaining to the procurement, storage and marketing of wheat. The decision of the Punjab government to re-impose a ban on the inter-provincial movement of wheat will have put paid to any plans of the federal government of facilitating the private sector into becoming more active in the market for wheat.

Moreover, the federal and provincial governments have been incurring an annual subsidy of more than Rs. 8 billion on wheat. However, what is classified as the atta subsidy in budgetary allocations, is only very partially a consumption subsidy.

The bulk of the fiscal cost of the activities related to wheat operations comprises expenditures on incidentals — bagging, handling, storage and stock carrying costs — which go towards subsidizing the high cost of management, wastage, processing (financial charges and gunny bags), pilferage and corruption. Any relationship between the levels of poverty and the allocation for atta subsidy is at best tenuous. This is because of the definition of this subsidy and the manner in which the accounting entry for the subsidy is recorded, whereby the higher the stocks, the higher the subsidy.

It is not the consumer who is benefiting (in whose name the subsidy is being incurred) but the middlemen, the banks (lending the money) for procuring wheat, the officials of Passco, the food departments and the flour-mills. Less than 10 per cent of the total fiscal cost of the subsidy on wheat actually accrues to the consumer. The bulk of the expenditure in the name of subsidy for consumers is absorbed by the inefficiencies in and poor management of the government's wheat marketing operations. Also, since the subsidy is a general one and available in the same proportion to even the more privileged segments of society much of it accrues to unintended beneficiaries including those dining out in five-star hotels and restaurants.

Therefore, if the subsidy on atta is withdrawn completely the net adverse impact on the consumer will be marginal. However, since perceptions are more powerful than realities a better strategy would be to phase out the subsidy gradually, say over the next two years or so, to avoid a political or social backlash.

As regards the need for targeting this subsidy to meet genuine needs of assistance, a well-structured scheme, a rupee for rupee increase in the atta subsidy, would both reflect and ensure a pure transfer to the poor. A part of the existing allocations and levels of subsidy could be used for such transfers and could even be supplemented with allocations from the zakat fund.

To address equity concerns and minimize the adverse impacts on the poor of elimination of the general subsidy, the provinces should either use savings from the phased withdrawal of the subsidy to augment support to less affluent households under the Food Support Programme or formulate a food stamps scheme. Subsidized wheat should be sold through shops located in poor neighbourhoods or through government agencies selling flour from mobile shops located in trucks to slums and sold at subsidized rates.

The need for stock reserves of wheat for food security reasons, to avert situations of shortage in emergencies or to smoothen out large fluctuations in wheat prices either during the time lag between production and consumption or during periods of price volatility has been stressed.

In a world of declining international prices of food grains and access to information on price and the availability of tradable stocks, the demand for wheat reserves reflects poorly on domestic planning, information on crop size, marketable surpluses, domestic consumption patterns and requirements and international wheat smuggling. Therefore, buffer stock operations should constitute a step in the phased transition to the development of a free, unregulated, market for wheat through a gradual acceptance of greater flexibility in wheat prices, with phased shifting of buffer stocks operations entirely to the private sector over three to four years.

Moreover, the size of such a stock should be limited to two months of potential consumption requirement to account for the lead/lag times of transportation of wheat from world markets, although reserves earmarked for the NWFP and Balochistan may be maintained for three to four months in view of transportation issues.

If the underlying assumption determining the size of the strategic reserve is that it need only cover the requirements of the urban population for two months, then the initial size, assuming a consumption of 130-135 kgs per capita per annum, may not exceed 1 million tons and around 2.2 to 2.5 million tons if the non-agricultural population in the rural areas is also to be accounted for, compared to the Punjab government's desire to procure 3.5 million tons of the crop.

To conclude, the policy decision of the Punjab government to ban the inter-provincial movement of wheat is not only misplaced but also fails to achieve what are ostensibly well-intended objectives. The Punjabi farmer is losing out on a higher price that he would have earned if the market had been allowed to operate freely. The price of wheat in the deficit provinces will continue to be high unless they are allowed to import wheat from abroad and the principal unintended beneficiaries of the subsidy regime will continue to be the officials of the provincial food department, the middlemen and owners of flour mills.

The writer is a former finance minister of Punjab.