

Managing Food Security to Sustain Political Transition¹

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One may debate on whether Bangladesh's politics is in transition – but all would agree that there has been a major departure from past trend in politics since January 2007 (often referred to as 1/11). Whether some of the current actions against the 'untouchables' in the upper echelon in the society are 'eye-wash' actions or genuine – one may only speculate. However, the commoners cannot recall even such 'eye-wash' actions during the past. And that's where the hopes are rooted, the basis of all our patience, which may however erode if the politics is not right. Since bad economics often lead to bad politics with subsequent adverse affects on the economy, this paper highlights on some recent economic issues of concern, attempts to provide consistent explanations of these, and proposes few suggestions to make the costs of transition bearable.

The central issue of concern is the unanticipated increase in food prices – a threat to human livelihood in a country where more than 40% of the people had already been living in poverty. Increased vulnerability in food security is a threat to a smooth transition to political stability as well. Nominal prices of most commodities normally increase, and the average rate of such increase (called the inflation rate) had been hovering in the range of 6 to 7 percents over several years in the past. This is both believed and experienced to have increased, and there is no doubt about it amongst buyers of staple food in both urban and rural Bangladesh. Current estimates show that the rice price had risen by more than 35 percent over a period of last five months (which corresponds with the trend in the international rice prices, see Figure 1). Retail price of coarse (HYV) rice in the neighboring northern districts of Dhaka was Tk. 16 per kg in December 2005, as well as in May 2006 and December 2006. The reference months are those immediately following harvests; and the prices hardly rose by a Taka per kg during January-April 2006. The pattern in price variation suddenly changed during the first five months of 2007 - it jumped to Tk. 18 to 19 per kg by February, and is currently at around Tk. 22 per kg or more. Along with several other factors (discussed later), increase in rice price may have triggered increases in prices of other food items; and the increase in oil prices certainly contributed to increase in general price levels. And, in markets on which agents lack confidence, initial price increases may lead to expectations of further increases, inducing prices to be raised by another fold!

¹ The paper is a reflection on current situation, and draws upon information compiled by various agencies. The author acknowledges supports received from Raisa Afsana at ERG and from various other people in the government and non-government agencies. Views expressed in this paper are exclusively of the author, and do not necessarily reflect the views of other members of Economic Research Group. All comments and suggestions may be directed to sajjadzohir@yahoo.com.

Recent increase in inflation (rate at which nominal prices increase) is largely attributed to increases in food prices. One may identify several reasons for the price increase – and these are highlighted below.

- Increase in domestic fuel prices (effective since 2nd April 2007);
- Increase in rice price in the international market;
- Disruptions in the market, as a result of the political transition, leading to inadequate engagements by the marketing agents, which subsequently led to supply shortfalls; and
- Presence of syndicate/cartel, which is currently getting quite a bit of attention in the media.

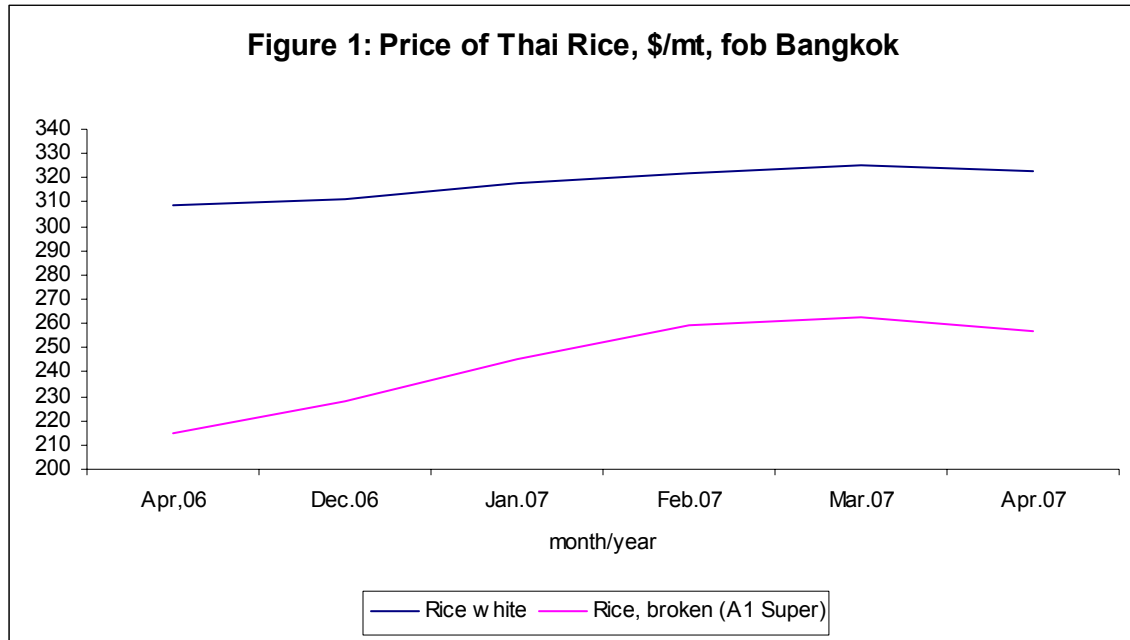
One may rightly posit the questions: would these factors be prevalent if there was no attempt made towards political transition, and, even if these factors were present under both scenarios, would these have contributed to price increase in the same way? Within such broader frame, possible significances of the above-mentioned factors are discussed. An understanding of these is critical – so that governance of the economy is guided by economic principles, and not otherwise. Anticipated situation in the near future calls for sharing the hard times ahead, only a part of which (as will be argued in the following) can be attributed to the political transition – though the cost may increase (along with the share) if there be failures in managing the economy.

A recent paper by two researchers at the Economic Research Group concluded that the increase in domestic fuel prices would lead to 10% or more inflation, which would be a one-shot jump (see, *www.ergonline.org*). The research however noted that the upward adjustment in prices was long over-due; and this had nothing to do with the political changes. If anything, bad politics around elections had pushed back the adjustment; and it had to come even if there was an election in January and an elected government took power. We need to come to term with a changed reality – the relative prices of energy resources vis-à-vis other commodities have increased worldwide by great margins and will remain at these high levels. Most other countries in the world have gone ahead with this adjustment, and the sooner we do the better.

On the trends in international rice market, a recent FAO brief on “Crop Prospect and Food Situation” (No. 3, May 2007) notes the following:

“The tightening of the global cereal balance in 2006/07 has pushed up prices of all cereals. In the case of wheat, the price index during the first 8 months of the current marketing year (July 2006 to April 2007), has averaged 25 percent above the average for 2005/06. For maize, the price surge has been even more significant with the index rising by nearly 44 percent. For rice, a modest 6 percent increase was registered in 2006 but prices continue their upward trend since the start of 2007. These increases have contributed to a significant rise in the cereal import bill of the LIFDCs (low-income food-deficit countries) which is forecast to jump 26 percent from 2005/06 to reach US\$23 billion in 2006/07. Given the prospect for strong international prices again in 2007/08, a more burdensome season may lie ahead for the LIFDCs, especially for those countries needing larger imports to cover domestic production shortfalls.”

The FAO brief shows that the rice stock with major exporters worldwide is already on decline, and it is projected to decline further in the coming year (2007-08); traded volume in the international market is projected to decline by 1.2%. For the LIFDCs, the situation is further grim. Interestingly, of the 7 LIFDC countries listed requiring external assistance, Bangladesh is left out. This partly reflects the lack of awareness on the part of the then government, which normally is the source of FAO information. This leads us to the third factor, identified as having a role in price increase.

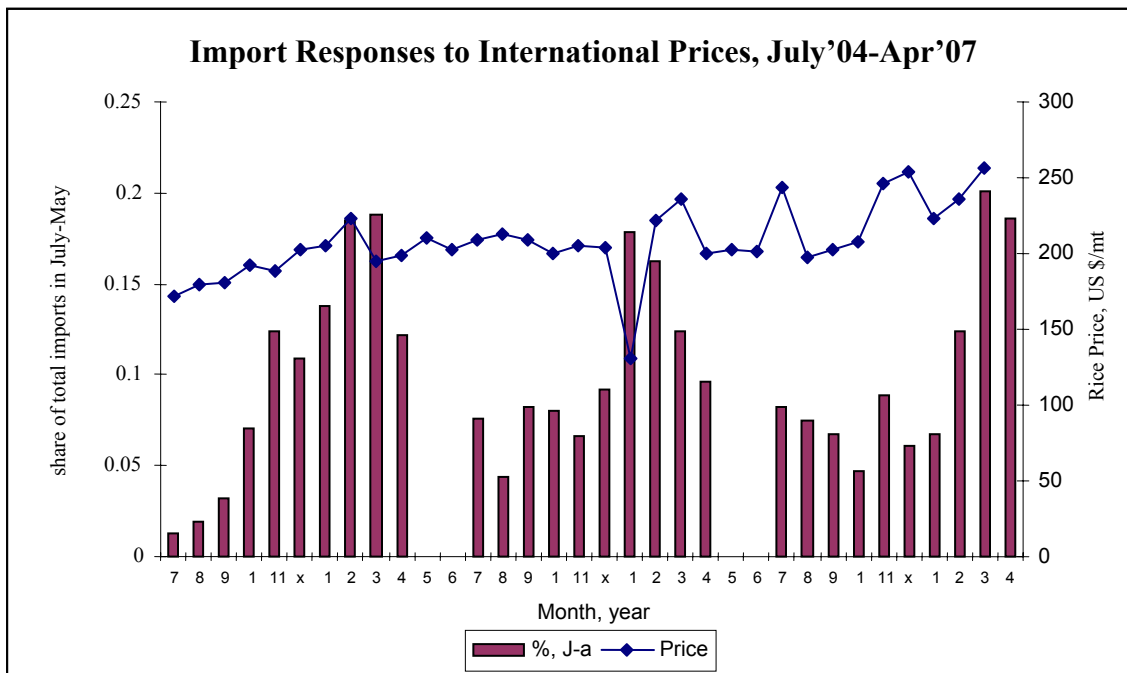


While tightening of the international rice market is real and nothing within our capacity could avert such a situation, could anything be done to reduce the cost arising out of it? One has to note that the demand and supply situation in Bangladesh's rice market is such that we have been in import parity price regime in most years over the last ten years. That is, the cost of making imported rice available in the domestic market (which includes the international price plus all the costs of transfers to domestic market plus the profit in various chains in the market) had dictated the rice price. Occasionally, good harvest allowed the domestic price to go below the import parity price, even though some varieties of (quality) rice continued to be imported. In addition, excess food reserve in India during earlier years had helped the local price to remain stable, which unfortunately has dried out. When markets are allowed to function with healthy governance, one expects the traders to ensure commodity flows responding to price differences between domestic and international markets. Importers' responses are normally reflected in opening and settling of LCs (Letter of Credit); and one may note that the ratio of LC settled to LC opened in (January and) February 2007 had been significantly lower than previous years (see Figure 3). One would presume that the traders had the information on international price situation and on the size of harvest to arrive during the *Boro* harvest;

and yet they did not or could not act for some reasons external to their usual profit motive. The political situation in the country during October 2006 till January 2007 is one big factor to induce lack of confidence amongst traders; and this was aggravated by stern anti-graft measures taken by the current Caretaker Government following the 1/11 changes. Thus, the opportunity of buying rice early when the prices were relatively low and buying rice on time (January 2007, see Figure 2) were partially lost.

Figure 2 captures the monthly distribution of total rice imported during July-April period, and projects them onto the figure on trend in international price (Figure 2). Without getting into a technical exercise, one may observe that the importers were quick to respond (by increasing imports) during previous two years (2004-05 and 2005-06) when the prices in the international market declined temporarily. The opportunity this year came during January 2007, which was not availed.²

Figure 2



There were also instances of unintended mismanagement in the input market. It is alleged that the natural functioning of the fertilizer market was partly disrupted due to ‘excessive’ control on mobility of fertilizer. On the last point, one may note that the actions were based on the assumption that spatial allocations were made with perfect information that matched with regional demands for fertilizer. On the contrary, the reality may have been a biased allotment or misallocations (in terms of regional allocations – a source of ‘rent’), and the markets corrected these deviations through inter-market (location) transfers by

² LC openings and the percentages of these settled were also looked into. No clear inference could however be drawn.

private traders. Under the latter assumption, any zealotry attempt to check those movements is likely to have adversely affected market functioning and optimal allocation of inputs. It is hard to come up with estimates on possible loss in production – but the direction of the impact is consistent with the shortfall in *Boro* harvest from that anticipated earlier.

There is a third dimension to market disruption – when some of the actors in the market are on the run, the regular commodity flows these actors had once facilitated would be disrupted, even if it be for only a short while (since appropriate management of the transition can ensure new actors substituting those roles).

All the above three aspects, considered unintended fallouts of long-desired political transition, are deemed to have contributed towards increasing the prices. As noted before, the first two factors – increase in fuel prices and in the prices of food grain in the international market – are the major contributors to the recently observed increase in prices. But those are beyond our reach and we may only focus on ways to minimize the cost rather than adding fuel to it.

Within the broad perspective laid out above, there is little room for ‘syndicates and cartels’ to provide satisfactory explanation of additional price increase. On the contrary, putting such factors on the central stage may misguide politics, further aggravating the problems of transition. Let me briefly note the basics to argue for the position.

- Was the cartel absent before and did it surface over the recent past to cause price increase? There is no *a priori* reason to believe that cartels would be absent during regimes of uncontrolled corruption and would surface when vigorous drives were pursued against corruption.
- Could it be possible that there were cartels before and they consolidated to nullify all reform attempts? Earlier studies on rice market in Bangladesh had rigorously established that the market was competitive and spatially well integrated. It is also well-known that the old coarse rice is hardly available in the local market, and has been largely replaced by improved quality of milled rice, and the efficient millers in the country are to be credited for their innovation to suit the tastes of the urban consumers. It is rather an irony that the media had failed to appreciate the contributions and find the millers an easy scapegoat for evils associated with price increase! As for wheat, experiences during the post-trade liberalization period in the 1990’s revealed that the individual flour mills would prefer to rally behind a big importer to ensure procurement of wheat from external sources – bulk import reduces unit costs, which applies to most food imports by sea. With limited market size, there had been few major importers who derived premium by virtue of their position in an oligopolistic market. If there has at all been a change in price setting behavior in such a market – one may only trace it to a reduction in the number of players, and that too may be attributed to the market disruptions during political transition alluded to earlier.
- Finally, one does not require the presence of cartels in explaining why there is price difference between urban wholesale market and the retail markets. One may

rather take solace from the fact that the margins the consumers pay go to support the livelihood of many poor rickshaw-pullers and retail traders!

Imagine a situation where cartel is not the reason for price increase, and oligopoly (finite number of suppliers) exists naturally because of certain compulsions in the market (such as, bulk procurements through fewer importers help in reducing shipping cost and overall transaction costs associated with external procurements). What happens if the government acts on the presumption that cartels are the cause of price increase? While the readers may ponder over how bad economics may lead to bad politics, and subsequently creating a bad economy, we move into the final part of the paper – what needs to be done and how. The focus is confined to food issues only.

Discussion so far suggest that rice and other food prices will remain on the high side, at the least till next *Aman* harvest and till the winter vegetables start to enter the market in large scale. It is quite possible that the rice price will eventually settle at a high level (say, Tk. 22 per kg for coarse rice) because all indications in the international market suggest of ‘rice getting commercial’, with major upward adjustment in its relative price. If all of us were parties to the old non-accountable corrupt system and the ‘illegally earned’ money circulated widely within the economy, people would only have to adjust their consumption basket in accordance to changes in relative prices. And sooner or later, the wages would adjust and so would the bribe money and the rest – eventually the economy settling to new set of prices, consumptions, production and distribution. But such convergence of ‘unholy’ actions is not expected in the changed environment where the drive is towards a less corrupt society. Unfortunately, the economic implications of such moves have drawn little attention so far – and we do not get into the topic here. Broadly, one may observe that there has been dislocation of informal sectors, having far-reaching implications for the livelihood of the poor and for internal remittance flows. The problems have been aggravated by dislocation of the traditional actors in some of the markets, and by sudden stoppage of the ‘corrupt’ money that had once lubricated parts of the economy. Since some of the steps are essential for the political transition, and because such steps are bound to incur cost (slow down economic activities), it is all the more important that errors in economic management be minimal and steps be taken to ensure that the cost be shared across society so that the goal of realizing political transition remains shared.

The paper alluded to costs of political transition from a corrupt to a less corrupt economy and society, but the task of identifying its many facets within the scope of a single paper is not possible. The focus therefore confined to issues of immediate concern – that of increases in food prices with dislocations in employment (and possible shrinkages in the size of employment), both affecting adversely the poor segment of the society. Given a scenario of little hope for immediate changes, the country needs to face the situation in a collective way. In its role as prime mover, the government ought to reactivate institutions under an environment of clean business, reactivate the economy with fresh investments, and address the dire situation that the poor will be facing in the coming months. If needed, the budget has to be recast accordingly, focusing on the recovery of the economy – if needed with additional (fiscal) deficit, spent in transparent manner. With that

perspective, a set of recommendations, focusing on a limited immediate issues pertaining to the food sector, is given below.

- Recent initiative to facilitate food grain imports to make up for the aggregate shortfalls is praiseworthy; and the foreign exchange reserve permits such undertakings. At the same time, there is a need to translate our savings (currently in the form of impressive build-up of reserve) into investment. One needs to look into ways of linking subsidized food distribution with real investment – if needed, centering around urban areas.
- Rice procurements are meant to support farmers when the prices are expected to be depressed; and there is no good rationale in the present situation of rising prices. Internal government procurement of rice needs to be stopped immediately, except for certain pockets in the country. This will save the government of undue claims on allowances, and also of having to deal with rotten rice in future. Moreover, it will give breathing space to the private sector, which need to keep the economy moving. Government procurement can remain confined to external procurement only.
- Recent initiative from the government to engage with millers is praiseworthy – but an appeal for a ‘no-profit’ gesture is unlikely to be sustained. The millers may have the option to switch back (part of their rice) to mill coarser varieties, which may reduce their cost substantially. It is possible that introducing further price differentials between the (traditional type) coarse variety and the fine variety will have beneficial re-distributive effects.
- In a regime of high prices of food grain, input subsidy is the primary instrument to resort to for ensuring increased production during next *Aman* harvest; as well as to promote summer vegetables and *Rabi* crops. It is important that steps are taken immediately to have an action plan worked out well before the planting begins.
- The government should seriously consider closing the OMS operation by para-military forces; and review the actual cost of undertaking such operations that involves payments of allowances (over and above the subsidy embedded in lower prices), not often revealed. If OMS is to be continued, the responsibility should lie with the traditional players within the government – those in the Department of Food and of Relief & Disaster Management. If the institutions within the government ought to perform, this is the best opportunity to make them deliver, when the country’s military and para-military forces have opted to assist the government in making institutions (including civil administrations) deliver services these are established for.
- It is now beyond doubt that OMS operation failed to lower food prices prevalent in the markets. If the objective is to provide supports to the poor, distributing cooked food (say, once a day meal) through ‘kitchen centers’ close to clusters of poor and very poor is a better option – it will save the fuel energy and time loss of numerous poor households, who may then seek meaningful employment. Private initiatives to open such centers may also be facilitated and/or donations for such initiatives may be encouraged.

Figure 3: Percentage of LC Settled, (Rice+Wheat)

