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Bharat Ramamurti

The state and the market

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Over the past two months, confusion has dogged the issue of wheat imports. There is little agreement on this, as experts, journalists, activists and various "concerned" groups have dispensed opinions on whether we need imports, whether the asking prices are too high, whether the import tenders need to be marked at the right time, whether the prices specified in tenders should be relaxed to allow US wheat, whether India should hedge its requirements in derivatives markets, and similar other whether this or that questions.

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At the end of it, the government decided to cancel the wheat tender because it thought the prices were "too high". A journalist who agreed with the view on prices nevertheless thought "it is a matter of shame that the entire tender process—from floating till scrapping—was handled in an utterly bizarre manner". This newspaper published a Reuters report that the government would import its decision because the prices, if anything, would be higher in the future. Clearly, these issues will be revisited whenever the government decides to access world wheat markets.

Whether the import process has been bizarre or not, the dirt of controversy is entirely expected. It has been this way every time the government imports grain. Last year, too, there were many observers critical of the choice of supplier and the price of contracted supplies. It is another matter that many of those critics should now favourably contrast the response to those tenders with the "high price" response this time around. Similarly, the wheat imports in the last half of the 1990s evoked opposition for the "high prices" and there were allegations of corruption as well in the deal with the Australian Wheat Board.

Why cannot the government get it right? Why is it not a simple matter to determine how much should be imported and at what price? There are several reasons why the government can never be sure that it is not overpaying for imports. Honest, intelligent and competent action is not enough.

Two features of the wheat market deserve attention. First, there is no such thing as a world market price. There is no global mandi where consumers bid for supplies. The closest thing in terms of a global market price is the wheat futures price at the Chicago Board of Trade. But the wheat that is traded in Chicago is not the one that is consumed in this country. So, while the Chicago market is a useful barometer of the wheat market, it is not of much help in figuring out what is a reasonable import price. The only way to discover the price is to be in the market all the time.

Second, the world market is highly volatile—wheat is harvested at different times in India, China, Canada, the US, Europe, South America and Australia. So, the world price at any point in time depends on expectations of the future. If we add the volatility of ocean freight rates, it is clear that if anybody talks of the world price of wheat to be, say, delivered in November in Indian ports, then that is just a forecast.

Even if we knew the wheat price in global markets, there is an added layer of difficulty. Our estimate of what wheat costs domestically is imperfect as well. The Food Corp. of India, which buys, stores and transports wheat to different parts of the country, reports to the government only the overall costs of its entire operation. So, while we know the cost of supplying a tonne of domestically procured wheat averaged across all procurement over all months, this is not the correct benchmark. To decide whether it makes sense to import wheat in, say, Andhra Pradesh in November, the government must know the "cost to" buying "a tonne of wheat in the wheat producing areas, transporting it to Andhra Pradesh and storing it till November.

The point is that no matter how hard government officials work, neither they nor their critics can be really sure that import decisions are correctly made. Trades will necessarily have to be based on forecasted prices. People will differ on forecasts and there will also be no shortage of it told you so when trades go wrong.

The key lies in looking at how we manage our other imports. For instance, India imports close to five million tonne of edible oils annually. Yet, how much newsprint do you see expended on whether we are paying too much, or whether we are imported at the wrong time? The truth is that, like in the case of edible oils, the government should not be in the import business at all, because it is not set up to be a trader.

If the government needs additional supplies, it should invite bids irrespective of where the grain is sourced—whether from overseas or domestically. The job of price discovery and hedging risks is a valuable market should be left to the traders who are better placed to do it. If home wheat were cheaper, no trader would sacrifice profits to buy from world markets. The only thing that the government must take care of is to announce its purchase intentions as early in the season as possible, so that farmers can benefit from the price movements. This is no different from the best practice of corporate governance where corporates offer earnings guidance for the benefit of small investors.

Bharat Ramamurti is a professor at the Indian Statistical Institute, Delhi. Comments are welcome at theirview@livemint.com

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