Spotlight: Econ Op-eds in Summary

Week ended 04th March '20

In Summary

The underneath contains summaries of the articles given above, including key extracts from these articles.

1. Ominously rising foodflation needs medium to long-term strategy to improve agricultural productivity
By: W.A. Wijewardena

- Rising food prices led to a recent increase in inflation levels in Sri Lanka. A prolonged drought and rising producer prices had negated expected price drops. While some higher food prices were blamed on the middlemen, research has suggested that middlemen margins are low for paddy and that higher margins on vegetables are to compensate for the costs including transport and waste.

- Importing food items might create an over-supply as the Maha season stocks come in the next month. At current productivity levels, rice farmers benefit with a low output. The long-term solution to food inflation will be to improve productivity in main agricultural crops in the country. The excess supply from improved yields could be used in producing industrial goods for exporting.

- Paddy cultivation also requires a large quantity of water. In Sri Lanka, while water is supplied almost free, droughts will affect the production. Water-efficient paddy cultivation methods developed worldwide should be adopted. All the stakeholders in the agriculture sector should come together to implement a comprehensive reform strategy targeting medium to long-term.

Foodflation raising its ugly head

As at end-January 2020, Sri Lanka's consumer price levels have shown a sudden upsurge mainly due to increases in food items, a situation known as 'foodflation'. The Colombo Consumers' Price Index or CCPI that covers only the consumers in the Colombo District accelerated 6.2% by end-February compared to the price levels that had prevailed a year ago. While non-food items had recorded an increase of only 2.9%, the food items had increased by 14.7%, up from 6.3% two months ago.

Following the same trend, Sri Lanka's National Consumers' Price Index or NCPI that covers the whole island too recorded an increase of 7.6% by end-January, compared to 1.2% a year ago. Of this, the non-food items rose only by 3%, while food items steeped by 13.7%, up from again 8.6% a month ago. According to NCPI, the main culprits have been vegetables, coconuts, red onions and fresh fish which had recorded a sharp increase compared to their levels in December 2019.

Against this foodflation, the consolation for consumers had been the slower rise in the non-food items that had been included in the indices. That component in NCPI constitutes 56% of a consumer's budget.

This time, it isn't a seasonal issue

Food prices are seasonal and therefore with the expected entry of the Maha crop to the market in about two months' time, they could be expected to reverse. However, in this year, in addition to the seasonal factors, they have been adversely affected by the prolonged drought and warm weather conditions in most of the food producing areas in the country. This is also shown by the reversal, by the end of the year, of the downward trend in the producer prices which had been the salient feature till mid-2019.

According to the Producer Price Index or PPI, the prices faced by the agricultural producers continued to fall till August 2019. Accordingly, the index value for this sub-category which stood at 160 in December 2018 fell to 138 by August 2019. But since, then, it took a sharp upward trend ending at 162 by December. This is a 17% increase in the agricultural producer prices in the last four months of the year.

Though we do not have the later data on producer prices, the increasing trend portends that agricultural prices will continue to be high for a few months more, despite the entry of the Maha crop to the market.

Suggestion to eliminate the middleman

The reaction of President, to this unwarranted increase in food prices happens to be based on his belief that prices are high because of monopolistic manipulation of prices by a few wholesalers. He is reported to have directed his officials to intervene in the market and put an end to the ongoing price increases.

He has drawn their attention to the structural issues in the vegetable market in the form of vegetables being transported to specially established wholesale markets from producing areas and then being re-transported to those areas for use by consumers. In this two-way transit, a large quantity of vegetables gets destroyed causing vegetable prices to remain high even when the supply conditions may have improved significantly.

He has also suggested that lands belonging to the state, should be used to cultivate vegetables thereby increasing their supply to the market. It can be considered as a medium to long-term remedy to the problem.

The charge against so-called oligopolistic paddy-millers

The general perception is that the middlemen are exploiting both the producers and consumers. Hence, the suggestion is either to eliminate the middlemen or handover the middlemen’s functions to a governmental authority. This charge is specifically levelled against the middlemen who are operating in the paddy/rice markets in the country.

The exploitation theory not supported by evidence

This popular claim is not borne out in empirical evidence. Two economics dons attached to the University of Colombo have worked backward from the retail price of rice in two markets in the Western Province in 2012.

In both cases, out of the price paid by consumers, paddy farmers have collected between 80 and 82% of the final price. The balance has been earned by wholesalers, retailers, millers, transport agents and collectors in the supply chain. The cost of processing by the miller has been about 7%, while his margin has been only 3% of the final price.

In the case of vegetables, the comparison of the farmgate price with the market price reveals that there is a price-gap of about 40%. However, this is due to the high transport costs and the high waste of vegetables, estimated to be around 40%, in transit. An improvement in post-harvest handling systems through improved technology will certainly reduce this high waste costs, thereby narrowing the price gap significantly. It would benefit both the producer and the consumer.

Foodflation increases the cost of living

Foodflation causes an increase in the cost of living of people. In the case of the present increases in food prices, the increase in the expenditure by a consumer on food items from end-August 2019 to end-January 2020 has been Rs. 2,010, according to NCPI. It records an increase of 11% on the food budget of a consumer over the budget as at end-August 2019. To relieve the consumers of the high cost of living two measures can be taken by the government. Immediately, it can increase the market supply by permitting imports to come into the country.

However, since there is a time lag of about one month for any imported food item to reach the market, the relief to consumers will be delivered not earlier than early April. But, by that time, the Maha crop will come to the market and if the market is inundated by both the locally produced food items and imported ones, the prices would fall worsening the conditions of the local farmers. Hence, the decision to import food items should have been taken some time in November last year and, therefore, it is too late to resort to that strategy now.

The other strategy is a medium to long term strategy to increase the productivity and the output in food items so that the market would be kept supplied by a bigger quantity of food items in line with the increase in the population. The improvement in the productivity in food items is essential to keep the costs of production in check and prevent them from percolating to the markets through an increase in the supply prices.

Rice paradox: produce more and become bankrupt

Rice is a part of Sri Lankans' DNA and therefore, early measures are needed to address the existing issues faced by the sector in the style of a 'rice paradox'. With low productivity, the paradox faced by Sri Lanka's paddy farmers is that when the harvest is bountiful, they become bankrupt due to prices falling below the production costs. Hence, it is to the benefit of farmers if the country's rice output is low.

However, this does not sit well with consumers who are great rice eaters compared to their counterparts in other major rice eating countries. On average, a Sri Lankan eats about 110 kg of rice a year, compared to a world average of just 54 kg. Hence, it is necessary to resolve the paradox in the rice sector if it is to sustain.

Diversify the use of rice

The permanent solution lies in improving the yields of rice farmers and creating a demand for rice as an industrial input. The former will help farmers to beat the rising costs of production. The latter will facilitate Sri Lanka to absorb a glut in the market, use it to produce industrial goods and export such goods since it cannot export its short grain rice as a food item. If there is no surplus of rice for industrial use, such surplus can still be generated if Sri Lankans learn to eat less rice and more meats and fats.

Even a reduction in average per head consumption by, say 20 kg, will generate a sufficient surplus of about 42 million kg of rice for this purpose. These are long term strategies based on proper awareness, changes in relative prices of rice as against meat and inventions made through the development of science and technology base of the country. The science part is the handiwork of a new subject area called 'biotechnology' which has now been added to the curricula of some state universities and private higher learning institutions.

Rice: the water guzzler

The problem with rice compared to maize or corn is that it is a 'water guzzler'. In farming, paddy fields are flooded by water and about a half of that is lost through seepage and percolation. It is the balance half which is used by the rice plant for its own purposes, known as evaporation and transpiration.

The researchers at the Manila based International Rice Research Institute or IRRI have computed, the amount of water used by rice plant to produce 1 kg of rice. Total flooding of the paddy fields from sowing to harvesting will use about 2500 litres of water to produce 1 kg of rice. About a half of this is lost through seepage and percolation; accordingly, the real use of water by the rice plant to produce 1 kg of rice is about 1432 litres.

Fortunately for Sri Lankan consumers, water is supplied to rice farmers almost free of charge either through rains or government sponsored irrigation schemes. But, shortage of water due to droughts will affect both the production and productivity of rice farmers. This is a serious problem in many rice producing nations like China, India and Sri Lanka.

The solution lies in improving farmer productivity

The long-term solution to foodflation is to improve productivity and yield levels in main agricultural crops in the country. All the stakeholders in the agriculture sector of the country to a common platform and get them to implement a comprehensive agriculture reform strategy targeting medium to long-term.

For the full article – Refer Daily FT

2. Debt in Times of Economic Crisis
By: Ahilan Kadirgamar

- Sri Lanka's economic woes were long in the making, with high debt and efforts to roll over debt with consecutive IMF agreements. These agreements often come with market friendly neo-liberal policies attached to them, which include measures that increase imports and the rapid flow of finance capital. This has only thrown the country further into debt.

- A debt ridden and stagnating economy raises the cost of capital and reduces demand for goods, in effect crippling SMEs, which are major employment creators in Sri Lanka. This in turn would reduce incomes of people, pushing them towards loans with high interest rates which leave them in higher debt.

- One such example was the IMF's recommendation that the recently implemented rate caps should be temporary. Thus, the alternative to this crisis should begin with barriers against the onslaught of market forces that not only entrap rural women in debt, but harm out small businesses and even paralyze states like Sri Lanka.

Debt relief is now a call at all levels of state and society in Sri Lanka. The Prime Minister recently requested a three-year moratorium on debt repayments to India, the Government earlier announced a debt repayment moratorium of one year for Small and Medium Enterprises (SME) with loans up to Rs. 300 mn, and women's groups called for the abolition of exploitative microfinance schemes during a protest held on February 27, in Colombo.

Why this sudden concern about debt, from the billions of US dollars in national debt, to the hundreds of millions of rupees in SME's debt and down to the tens of thousands of rupees in women's microfinance debt? Are these different levels of debt related, and what are their consequences?

Economic woes

The Sri Lankan economy is in crisis. A crisis generated by a fall in government revenues where

- the wealthy in this country are hardly taxed and
- a higher level of imports than what can be paid with the sum of exports,
- remittances and tourism-generated foreign income.

And to make matters worse the prospects don't look good, the global economy is stagnating this year and it has been aggravated by the Coronavirus. All this will have a disproportionate impact on the Sri Lankan economy with the tourism industry undermined by the reduction in tourist travel with the Coronavirus, and that too following the significant tourist slow down after the Easter Sunday Attacks.

These recent problems aside, Sri Lanka's economic problems were long in the making, with mounting national debt for decades, and efforts to roll over debt with consecutive IMF agreements. The IMF Standby Arrangement in 2009 and the IMF Extended Fund Facility in 2016, are the 15th and 16th IMF agreements reached by Sri Lanka. Such IMF agreements that come with stringent conditionalities have prescribed market friendly neo-liberal policies including to increase imports and the rapid flow of finance capital that have only thrown the country further into debt.

In this context, a debt ridden and stagnating economy raises the cost of capital and reduces demand of goods, in effect crippling SMEs, which are major employment creators. Next, when the economy slows down, rural incomes are also affected as the rural population increasingly depends on a mix of incomes combining rural livelihoods with incomes from urban, industrial and service sectors. Furthermore, rural women in particular get squeezed not just by falling household incomes but the extremely high interest charged by microfinance companies and money lenders.

IMF squeeze

The alternative to this crisis should begin with barriers against the onslaught of market forces that not only entrap rural women in debt, but wipe out small businesses and even paralyze states like Sri Lanka. But when the Government seeks away out through the IMF, mandated to relieve governments from short-term financial problems, the IMF imposes long-term prescriptions that are to further open market forces.

This was the subject of a recent public discussion organized by the Jaffna People's Forum for Coexistence with activist researchers from the international network of the Committee for the Abolition of Illegitimate Debt (CADTM). The analysis of CADTM was spot on showing how for example the tremendous corporate and banking debt is often bailed out by governments increasing the tax burden of citizens.

Furthermore, when government debt increases, there is a push towards austerity where social services and welfare are cut. Sadly, such cuts are coupled with microfinance schemes and the myth that people can both increase their incomes and pay for private services including healthcare and education with such small loans.

Exactly two years ago, with a major protest against predatory microfinance schemes, the Jaffna District Co-operative Council made the following demands:

"all microfinance companies that use unethical and illegal practices be banned, an interest rate cap with an effective annual interest rate not exceeding 25% be imposed, so that all predatory loan schemes are immediately stopped, cancel all existing predatory microfinance loans or provide a moratorium for two years necessary to restart sustainable economic activity and expand low interest government credit schemes that could generate sustainable rural livelihoods and rebuild the economy."

Eventually, a Central Bank interest rate cap of 35% was imposed in December 2018, but even that high rate has been effective in flushing out a number of the unscrupulous microfinance companies, as most of them were charging between 40% and 240% annualized interest rates. Indeed, the rural indebtedness situation in the North has been slowly improving with the co-operatives actively providing lower interest small loans.

Into this mix, the IMF after a recent staff visit to Sri Lanka, had the following to say in a statement on February 7, 2020:

"Caps on lending rates and the loan repayment moratorium for small and medium enterprises should be temporary, to avoid unintended distortions and inefficiencies in financial intermediation."

That is a worrying signal from the IMF, which is only concerned about so-called market distortions to the detriment of the economic lives of people, and it should be closely watched whether the Government will buckle under such pressure.

Struggle for the people

When Third World countries go to the IMF with a begging bowl for its blessing, so that global finance capital will flow in with an IMF guarantee, the vicious cycle of austerity and market forces can shred economies to bits. It is like the Tamil saying of the beggar who goes to a house and then cries, "pichchai vendaam naayaip pidi" (don't want your charity, hold the dog which is about to bite me). That has been experienced with the IMF from crisis to crisis around the world over the past many decades.

During the engaging discussion with CADTM in Jaffna, one local co-operative leader involved in the major low interest credit scheme underway in the North, and now reaching over ten percent of the population, put forward an insightful challenge.

He said there is a major struggle now between finance companies and co-operatives to engage the people, one to entrap them into predatory loans and the other to provide productive credit. He asked if we are ready for that struggle in our communities. Drawing from that there is also a major struggle to be fought against the IMF, which is about the freedom of the market to exploit people and the democratic freedoms of the people to collectively chart their economic lives.

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