VI THE PRICE SITUATION

134. The pressure on prices which had begun developing in November 1969, continued throughout the latter half of 1969-70. The seasonal factors came into operation thereafter, and the wholesale price index showed a steady rise until the seasonal peak was reached in September. This was followed by a decline, but at a much slower rate than is normally expected, so that in December 1970 the price level was 6.5 per cent higher than in the corresponding month of 1969. During the remaining three months of the year, the situation showed a relative improvement and prices in March 1971 were only 3.3 per cent above those of March 1970. End-March prices were, in fact, only 2.8 per cent higher than those a year ago. For the year as a whole, the average level of wholesale prices during 1970-71 was 5.6 per cent higher than what obtained in 1969-70.

TABLE XI

Index Numbers of Wholesale Prices

(1961-62 = 100)

Percentage Variations

	Weight	Over the preceding year				March, 1971 over March, 1970
		1967-68	1968-69	1969-70	1970-71	
All Commodities	(100·00)	+11·6	—1·1	+3·7	+5·6	+3·3
Food Articles .	(41·30)	+21·4	—5·2	—0·1	+2·2	+0·8
Foodgrains .	(14·78)	+24·9	—12·0	+3·6	—0·7	—6·9
Liquor and Tobacco	(2·50)	+13·3	+26·6	+1·3	—5·2	—2·7
Fuel, Power, Light and Lubricants .	(6·10)	+5·6	+4·6	+4·4	+4·3	+1·8
Industrial Raw Materials .	(12·10)	—1·3	+0·6	+14·5	+9·6	+3·5
Raw cotton .	(2·24)	+11·8	+8·6	+10·5	+22·4	+30·9
Raw Jute and Mesta	(1·16)	—27·7	+53·8	—11·5	+1·3	+3·5
Oilseeds .	(5·24)	—4·3	—11·4	+26·2	+10·4	—4·2
Chemicals .	(0·70)	+9·2	+7·4	+8·7	+2·2	—3·2
Machinery and Transport Equipment .	(7·90)	+4·3	+0·5	+2·8	+8·6	+8·0
Manufactures .	(29·40)	+2·8	+2·5	+6·8	+7·9	+7·9
Intermediate products	(5·70)	+4·8	—0·9	+10·1	+11·6	+6·5
Finished products	(23·70)	+2·3	+3·5	+5·8	+7·0	+8·2

135. The somewhat disquieting developments on the price front can be mainly attributed to the shortage of a number of important materials aggravated, in part, by the larger creation of credit in the economy over the year. The shortages of raw materials such as cotton and oilseeds and of metals such as steel and non-ferrous categories have affected production, and therefore, prices over a wide number of industries. Changes in the price level of industrial raw materials affect the wholesale price index directly *via* the price index for raw materials and subsequently through the price index for manufactures. In a situation of over-all shortage of particular commodities, the fact that there has been over the year a general expansion of money supply has further clouded the picture. Irrespective of selective credit and administrative controls, where supplies are constricted, a general increase in credit is bound to leave some influence on prices. Besides, in a situation marked by excess demand, the exercise of group or monopoly power, of which speculative activity is a manifestation, cannot but gain a certain ascendancy. Although wage and income adjustments during the year have conceivably had a marginal effect on prices, this is up to a point an inevitable consequence of the bargaining for compensatory adjustments in money incomes, a common enough occurrence in a period of inflation.

136. On the other hand, the improvement in the supply of food due to higher domestic production and an adequate public distribution system enabled certain sectional adjustments between supply and demand to take place. The rise in the price index for food articles was only 0.8 per cent, while the price index for foodgrains has in fact registered a decline of 6·9 per cent over the year. The price indices of both cereals and pulses have come down, the former by 6·2 per cent and the latter by 9·1 per cent. In the absence of the Government's comprehensive price support-*cum*-procurement policy, foodgrain prices would have fallen further.

137. Consistent with the fall in foodgrain prices over the year, consumer prices, as measured by the All-India Working Class Consumer Price Index, have risen at a rate lower than the rate of rise for the wholesale price index. The phenomenon is explained by the fact that a significant proportion of the expenditure of the working class families is accounted for by foodgrains. The average Consumer Price Index for the 11-month period ending in February 1971 was 5·1 per cent higher than the average during the corresponding period of 1969-70; this order of rise bears comparison with the rise in the wholesale price index, which, over the year, on the same 11-month basis, works out to 5·7 per cent. In fact, from December 1970 onwards, the Consumer Price Index started to decline; by February, it had fallen by as much as 2·6 per cent from the level attained in November. There is therefore ground for suggesting that, in case the supply of industrial raw materials was not affected, the general price level during the year would have been pronouncedly quieter.

138. While the influence of the speculative factors need not be under-stressed, the pressure on the prices of industrial raw materials was principally due to a relative paucity of supply. The output of

cotton is virtually stagnant, while that of jute has been subject to such wide fluctuations during the last few years that stocks have been generally in a precarious state, which have given a handle to the speculative elements. In oilseeds, demand seems to be keeping ahead of whatever improvements in output have been taking place, thereby aggravating the scope for speculative stockholding. Since the prices of hydrogenated vegetable oil are linked to those of its principal raw material, that is, groundnut oil, higher market prices for oil and oilseeds inevitably tend to get reflected in the prices of the former. Similarly, given the nominal penal provision, higher prices of raw cotton can be passed on to the consumer by reducing the output of controlled cloth and increasing that of the uncontrolled varieties.

139. The index for raw materials, which stood at 170·6 for November, 1969 rose continuously to reach 201·2 in June, 1970. There was a seasonal fall in October with the arrival of the new crops of cotton and oilseeds into the market. The decline was short-lived as raw cotton prices came under considerable pressure in November 1970. For the month of January 1971, the raw materials index stood at 206·5, a rise of 20 per cent in the course of a little over a year. Prices have since begun to decline and the index for March 1971 came down to 194·0, mostly attributable to a drop in oilseeds prices in the more recent months. Cotton prices too declined in February and March 1971, even though they are still 30 per cent above the level reached a year ago.

140. The price index for metals has been similarly responsible for the more or less continuous pressure on prices during 1970-71. In January 1970, prices of pig iron and steel had been raised by Rs. 37·50 and Rs. 77·50 per tonne respectively and the price index for pig iron and semis rose by over 10 per cent. Consequently, the price index for manufactures, as also that of machinery and transport equipment, is 8 per cent higher than the level of a year ago. Of the remaining commodity groups, the price indices for liquor and tobacco and chemicals have shown a decline, while those for fuel, power, light and lubricants have recorded a moderate increase.

Price Policy

141. The general price index had begun to move up from the middle of November 1969 principally due to an increase in the prices of oilseeds and pulses. In January 1970, the impact of delayed winter rains led to an upward pressure on the prices of foodgrains and raw cotton too. The Reserve Bank of India, therefore, stepped in with measures of selective credit control aimed at these commodities. The credit restrictions in regard to raw cotton (and cottonseed) were relaxed on the eve of the 1970-71 busy season to facilitate the marketing of the new crop, but this step had to be reversed a few weeks later. On reports that the crop would not be as good as earlier anticipated, and in view of the time lag in imports, mills indulged in hectic buying which pushed prices up to an extraordinary degree. Similar activities on the part of the trade had to be checked by suspending futures trading in *kapas* and by reducing the period of non-transferable contracts in cotton from six to three months (and

later to one month only); simultaneously, non-transferable specific delivery contracts for the sale of cotton in excess of one thousand bales were required to be registered. Despite these measures, the price index for raw cotton rose from 185·7 for October 1970 to 252·6 for January 1971. Larger supplies of imported cotton, as well as of staple fibre, were accordingly arranged. The announcement of this step, combined with the effect of the new credit control measures taken in January 1971, has resulted in a decline in prices during March 1971.

142. In the case of oilseeds, too, the price index has fallen from 233·0 in January 1971 to 211·8 in March 1971. The process was assisted by a tightening of control over bank advances against oilseeds, vegetable oils and vanaspati towards the end of January. Imports of soyabean oil for the hydrogenated oil industry have been continued at a level of approximately 100,000 tonnes per annum, supplies of rapeseed from Canada further helped to augment the availability of oil for edible purposes. The overall shortage of oils and fats has also been sought to be taken care of through imports of mutton tallow for the soap industry.

143. An import policy has been framed with the object of ensuring that actual users do not suffer for lack of essential steel. While exports are being regulated, actual users have been granted an increase in their import quotas. Bulk imports of scarce varieties of steel, such as plates and sheets, have been arranged. The projected import of steel for 1970-71 was of the order of 600,000 tonnes as against an import of 425,000 tonnes in 1969-70.

Price Controls

144. A Bureau of Industrial Costs and Prices was set up during the year for review and examination of the cost structure of industries referred to it for study, and to recommend prices; a number of references have been made during the year to the Bureau. Administrative control over prices has been continued to be exercised in respect of a number of commodities. The commodities which remained subject to statutory price control during the year included certain varieties of mill-cloth, agricultural tractors, motor cars and scooters, cement, synthetic rubber, vanaspati, certain fertilizers, kerosene, sugar and industrial alcohol. Two additional cate gories, were brought under statutory price control in 1970-71, namely, aluminium and its products, and electric wires and cables. While the prices of the latter are yet to be determined, the prices of aluminium and its products were frozen at the levels prevailing on February 28, 1970 as an interim measure pending the report of a special study group. During the year, prices of drugs and medicines too were brought under a system of comprehensive regulation and control with the coming into effect of the Drugs (Price Control) Order in May 1970. The cost structure of the units manufacturing drugs and medicines was examined by the Tariff Commission and norms for the fixation of fair selling prices were suggested. Prices of seventeen essential bulk drugs have been announced, and of other

bulk drugs have been frozen pending a detailed study. A Drug Prices Review Board has been set up to assist the Government in the fixation of drug prices at reasonable levels.

145. The Tariff Commission has also submitted its report in respect of fair prices of rayon tyre yarn, cord and fabric, and a reduction in the prices thereof has been announced. As a consequential measure, tyre manufacturers have been prevailed upon to reduce the price of truck tyres. On the basis of the study made by the Oil Prices Committee, the retail selling prices of all petroleum products (other than furnace oil, motor spirit and naphtha) were reduced with effect from June 1, 1970. Informal control over prices has been continued to be exercised in respect of soap, rubber tyres and tubes, bicycles, matches and iron and steel; producers are not expected to increase the prices of these commodities without the Government's prior approval. During the year, the necessity was felt of extending this kind of control to the paper industry, the prices of whose products have risen significantly since decontrol in 1968.

146. Price increases have, however, been allowed during the year in respect of some commodities subject to control. Higher prices for cement had to be permitted consequent on the exhaustion of the funds in the freight equalisation account, while bicycle prices had to be raised on account of higher prices for steel. A small increase was also allowed in respect of soap as the prices of indigenous oils had risen. The question of minimum prices for rubber had been referred to the Tariff Commission; pursuant to the Commission's recommendation, the Government agreed to increase the minimum price from Rs. 415 to Rs. 520 per quintal in September 1970. The Government also agreed to an increase of 5 per cent in the minimum support prices for different varieties of raw cotton for the 1970-71 marketing season. In the case of sugarcane, the minimum prices fixed for the previous season were maintained to the extent applicable to the minimum recovery percentage of 9·4; the premium for higher recovery was, however, enhanced from 5·36 paise to 6·6 paise per quintal for every increase of 0·1 per cent in recovery.

Distribution Control

147. As mentioned earlier, during the year the movement of wheat and wheat products was made free throughout the country, except in statutorily rationed areas. Restrictions on the movement of gur were also removed. Partial control over sugar was continued during the 1970-71 season, but the free sales quota has been increased from 30 to 40 per cent. In view of the general shortage of iron and steel which developed during the year, and with a view to ensuring adequacy of supplies and equitable distribution, the Government decided to abolish the distinction between scarce and non-scarce categories and to extend distribution control to practically all the products of the main producers of iron and steel.

Issues and problems

148. As the resume above would indicate, the three main factors underlying the instability of prices during the year have been: (a) inadequate supply of essential goods, (b) a certain excess supply of money, and (c) exercise of monopoly power, of which speculative hoarding is but one example. While, given the several imperfections of the system, the last factor does indeed play a part, it is on the central question of adequate supplies and prudent fiscal and monetary policies that efforts at maintaining a stable price level will hinge. Among the shortages that have bedevilled the economy during the year, the most persistent and insidious from the point of view of the price level for essential commodities are those relating particularly to cotton and oilseeds. Even in regard to foodgrains while the general situation has been good, supplies have been short for pulses, and, even for rice, the position is only marginally satisfactory. In the case of most of these bulk commodities, it would be futile to hope that chronic internal shortages can be made good by imports. Even in 1970-71, the import bill for cotton, rice, tallow and soyabean oil has been considerable. There can be no enduring solution to the problem of prices as long as the country is not able to have adequate production of foodgrains, cotton, pulses and oilseeds and such other food articles as milk and vegetables. Among industrial products too, apart from iron and steel—where output has been hampered by organisational problems—there are areas such as paper and non-ferrous metals where price stability will depend upon substantial increases in productive capacity.

149. There is similarly need for enforcement of due restraint on the demand side. While credit for the hitherto neglected sectors must continue to be allocated in adequate magnitudes, the search should be continuously on to enforce credit and fiscal discipline elsewhere in the economy, both in Government and outside. Once success is achieved on this front, the speculative elements will discover that their ability to distort has been effectively limited.