

The National Food Security Bill (NFSB)

Incremental Financial and Distributional Implications:

2013-14 to 2015-16

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The National Food Security Bill (NFSB) is an important effort to ensure the majority of population in India has access to adequate quantity of food at affordable prices. This note examines the financial consequences of the revised NFSB, which was approved by the Cabinet and has been circulated in the Parliament in March 2013. Although the revised bill is likely to simplify the identification of beneficiaries, the financial implications are still going to be huge. Our analysis suggests that NFSB even after the proposed amendments needs to be carefully evaluated to take into account not only the cost of food subsidy, but also the additional costs of setting up/running of new institutions and bureaucracies, and the additional costs that are likely to arise if there are political pressures to protect the existing beneficiaries, many of whom are not grandfathered even in the revised bill. When these are taken into account, the amended NFSB may also entail significantly higher burdens than currently envisaged.

We estimate the fiscal cost of the current version of the bill, which proposes to cover 75% of the rural population, and 50% of the urban population with an entitlement of 5 kg per person per month of food grains at issue prices of Rs. 2 and 3 per kg for wheat and rice respectively. This proposal has only two categories: covered and uncovered, rather than three (priority, general and uncovered) in the previous version of the bill. The AAY (Antyodaya Anna Yojana) households will receive an additional 10 kgs of food grains per household to protect their existing allocations. The state-wise inclusion ratios are determined by the Planning Commission based on a national-level cut-off for per capita consumption to cover 75% and 67% of rural and urban populations respectively.

The food subsidy cost of implementing the amended NFSB is estimated at Rs. 124,502 crores for 2013-14. The food subsidy is calculated as [economic cost-issue price]*food-grain requirement. The

“economic” cost computed by the FCI includes in addition to the MSP, handling, storage and distribution costs. The calculation assumes a total coverage of 75% of rural and 50% of the urban population. The individuals identified as “covered” or “included” are entitled to 5 kg/person/month of food grains (wheat and rice combined); with an issue price of Rs. 2 and Rs. 3 per kg for included persons for wheat and rice respectively. The AAY households are entitled to an additional 10 kg of food grains per household. An additional allocation of food grains of 6.5 million tons for other welfare schemes (OWS) in the revised bill is also included. This includes provision of additional 5 kgs of grain per month to pregnant women and new mothers, and free mid-day meals in schools for children in the age group of 2-16 years. The total food grain requirement of the revised NFSB is estimated at 61.2 million tons, this includes an additional 2.9 million tons to protect the allocation to states under the existing TPDS. These estimates are in line with those of Food Ministry (MOFPD).

The cost is estimated to increase to Rs. 140,192 and Rs. 157,701 crores in 2014-15 and 2015-16 respectively. This is assuming a 10% increase in MSP and economic costs and a 1.7% annual increase in total population (2.8% increase in urban, and 1.16% increase in rural based on the average annual increase over 2001-2011), with the other parameters remaining unchanged.

The “incremental” food subsidy over and above the existing TPDS is estimated at Rs. 23,951 crores. This is equivalent to 0.2 percent of GDP. The incremental subsidy is the difference between the estimated cost of the NFSB in paragraph 3 above, and the cost of existing TPDS at Rs. 100,551 crores (based on 2000 population and 1993/94 poverty definition).

A commonly ignored fact is that even the revised NFSB entails significant new financial implications in addition to the food subsidy. This includes e.g. the setting up/running of State Food Commissions and District Grievance Redressal Offices (DGROs); expenditures on intra-state transportation of food grains; and cash benefits to pregnant and lactating women. Most of these expenditures would be incremental and is estimated with inputs from the MOF & PD at roughly Rs. 20,760 crores annually (see Table 1 for details). Rs. 8,760 crores would be incurred by the state, and the remaining cost would be shared between the center and state (based on a sharing arrangement to be determined). A one-time assistance may also be provided by the center to the states to enable them set up the State Food Commissions and DGROs. The setting up of national food commission is done away with in the revised bill; and states are allowed to rejig existing infrastructure to run state food commissions and DGROs but it is reasonable to assume that even if states decide not to create new infrastructure, they would still need to incur additional expenditures to beef up the existing facilities to implement the NFSB.

These costs may still be an underestimate since they do not include many other expenditures stated in the bill e.g. costs to be incurred for a new system for identification of beneficiaries, for strengthening the capacity of Food and Civil Supplies Corporations, establishment of institutionalized licensing for Fair Price Shops (FPS), setting up of vigilance committees to monitor the implementation, periodic audits of FPS, food security allowance to be paid in case of non-supply to entitled persons, funds to state governments to be provided by the central government in case of short supply of food-grains etc. Whether/how much of these additional expenditures would be incremental needs to be carefully assessed.

The total incremental fiscal cost of implementing the NFSB over and above the existing TPDS (including the quantifiable expenditures in addition to the food subsidy) is thus estimated for 2013-14 at Rs. 44,711 crores. The estimated total incremental fiscal cost for 2014-15 and 2015-16 are estimated at Rs. 47,392 and Rs. 50,591 crores respectively.

These estimates should be considered to be lower bounds for the actual expenditures to implement the bill. As discussed above there are various additional expenditure items stated in the bill, the incremental costs of which cannot easily be quantified ex ante. Further, the open-ended procurement policies of the government have implied that procurement has typically been much higher than the required quantity of food grains. For example, on average over the last 10 years between 2002-03 and 2011-12, procurement has been 40% higher than the offtake. If we add costs of 40% additional procurement to the incremental food grain requirement in the baseline NFSB, the estimated fiscal cost in 2013-14 can increase by Rs. 4,925 crores. In addition, the estimated incremental food subsidy costs under NFSB in the next two years could also be higher if the procurement of the additional grains requires an increase in MSP of more than 10% assumed in the baseline calculations. For example, if we assume a 20% increase in MSP (and economic cost) over 2013-14, the estimated incremental fiscal cost would increase substantially from the baseline by Rs. 14,111 crores and Rs. 15,720 crores in 2014-15, and 2015-16 respectively.

In addition to the aggregate fiscal costs of implementing the bill, there will be distributional implications as well; where some individuals may gain, some may lose, and others may have their food expenditures unchanged. Although the procedure for identification of beneficiaries will be left to the states and is not specified in the bill, if we assume a natural ordering, we can conduct some

simple simulation exercises to see how the current TPDS in a typical state will map into the new regime (see Table 2).²

- All AAYs can be relabeled as “covered”. They will be **as well off** as under the current TPDS; their entitlement will be unchanged at 7 kg per person per month, and they will pay the same issue price: Rs. 2 and Rs. 3 per kg for wheat and rice respectively.
- The remaining BPL individuals (62%) will obtain 5 kg of food grains at a lower issue price than under the TPDS but their entitlement will also reduce by 2 kg. Assuming current prices of wheat and rice (in the north zone at Rs. 19 and Rs. 27 per kg for wheat and rice respectively) and assuming they will demand at least as much as under TPDS, they will be **strictly worse off** (the loss on the 2 kg entitlement will outweigh the gain on the 5 kg).
- 71% of APLs will move into “covered” category. They will obtain 2 kgs of additional food grains and a lower issue price relative to TPDS; they will **be strictly better off**.
- The remaining APLs will move into “uncovered” and will **be strictly worse off**.

² We recognize that there is considerable variation across states in the implementation of TPDS (with near universal PDS in many states). The exercise here simulates the distributional implications of moving into NFSB assuming allocations and issue prices for BPL and APL as assumed by the central government. This exercise can be repeated in principle for different states taking into account the differences in implementation. The political necessity to protect existing beneficiaries is likely to have different implications for different states.

- Overall, out of the current population covered under the existing TPDS, 46% will be strictly better off, 14% will be equally better off and 40% will be strictly worse off.

If the implementation of the NFSB includes “grand-fathering” of existing beneficiaries, the estimated fiscal cost could be higher than under the baseline scenario. As discussed above, the existing APL beneficiaries who move out of coverage would be worse off; and the BPL individuals whose entitlement is reduced by 2 kg would also lose. If there is political necessity to ensure no existing beneficiary is made worse off, the estimated incremental food subsidy cost could increase by Rs. 20,074 crores from Rs. 23,951 crores to Rs. 44,425 crores in 2013-14 (Table 3). In that case, the overall coverage of NFSB to include the left-out APLs would increase from 67% to 82% of the total population.

Similarly, if implementation of the NFSB requires merging the current classification under the TPDS with new and more careful identification schemes, we should also consider the consequences of misclassification. Suppose everyone classified as BPL under the current scheme is automatically given “covered” status. However, everyone who currently holds a BPL card may not be truly poor. Even if a more rigorous identification scheme unearths the poorest 75% and 50% in rural and urban areas respectively, there may still be political pressure to expand the size of those classified as covered to include those misclassified under the current BPL system. Assuming BPL classification misclassified 25% of individuals when they truly are well off, and if the misclassified are new entrants into the NFSB (they were not a part of the TPDS offtake, but the NFSB entitlement at much lower issue prices is attractive enough for them), then the cost of subsidizing them can be substantial and is estimated at Rs. 11,301 crores (Table 4). The overall coverage of NFSB would increase in the

misclassification scenario to 74% of total population (from 67% in the bill). The total incremental food subsidy cost in the baseline would increase from Rs. 23,951 crores to Rs. 35,252 crores.

Combining the grandfathering and mis-classification scenarios could increase the incremental food subsidy cost of implementing the NFSB in 2013-14 to Rs. 55,726 crores. If we include the additional expenditures to be incurred in the setting up and running of new bureaucracies, the estimated incremental expenditure attributable to the NFSB under the baseline could escalate to Rs. 76,486 crores.

To summarize, the total incremental costs of implementing the NFSB over the above the TPDS could range from Rs. 44,711 to Rs. 76,486 crores in 2013/14. The smaller estimate is the baseline incremental costs, while the larger estimate includes the costs of grandfathering the existing beneficiaries and subsidizing the BPLs who are currently misclassified. If we add to it the cost of procuring additional grains according to historical norms, this would take the incremental costs of NFSB to Rs. 81,411 crores (0.7% of GDP). Table 5 provides a summary table, which incorporates all the costs discussed above.

Importantly, all these estimates should be seen as tentative and subject to revision because the precise costs of the current TPDS (and additional welfare) schemes are not easy to obtain. Given the experience is that off take increases when grain is offered at very low prices, and our estimates do not include various additional expenditures stated in the bill which are difficult to quantify, the rough estimates in this note are likely to be underestimates.

Table 1. Additional Annual Expenditures Under NFSB (Rs. Crores)

	State	Shared b/w center and state	Total
District Grievance Redressal Office (DGRO)	320		
State Food Commission	140		
Expenditure on intra-state transportation and handling of foodgrains	8300		
Maternity benefit		12000	
Total	8760	12000	20760

Source. MOF&PD

Table 2. Distributional Implications: Current TPDS vs NFSB

			difference in issue price (TPDS-NFSB) (rs./ton)		difference in quantity (NFSB- TPDS) (kg)
AAY 137495		→ Covered unchanged expenditure	wheat 0	rice 0	0
Other BPL persons in '000		→ Covered increased expenditure	difference in issue price (TPDS-NFSB) (rs./ton)		difference in quantity (NFSB- TPDS) (kg)
221,122	62%		wheat 2,150	rice 2,650	-2
APL persons 452,151	71%	→ Covered reduced expenditure	4,100	2,650	2
Remaining APL		→ No coverage increased expenditure			
181,312	29%				

Note. The estimates for TPDS are based on how it is currently operated (1993/94 poverty ratio and 2000 population)

The non-AAY BPL persons who move to covered: they were getting 7 kgs before at a higher issue price; they get 5 kg now at the lower issue price, but the gain on 5 kg outweighs the loss of entitlement of 2 kg, which they have to acquire now at the market price, accounting for a potential increase in the expenditures. APL persons moving out of coverage under NFSB have to obtain the grains through the market, and hence a potential increase in their expenditures.

Table 3. Cost of Grandfathering

Number of other BPLs moving into covered	221,122
Additional foodgrain per person (kg)	2
Total foodgrain (mn ton)	5.31
Wheat	2.41
Rice	2.89
Subsidy (Rs./ton)	
Wheat	15952
Rice	20786
Total subsidy bill (Rs. Crores)	
Wheat	3852
Rice	6012
Total	9864
Number of APLs moving out of coverage	181,312
Additional foodgrain per person (kg)	3
Total foodgrain (mn ton)	6.53
Wheat	2.97
Rice	3.56
Subsidy to be borne by govt. Rs. per ton	
Wheat	14,002
Rice	18,136
Total cost (Rs. Crores)	10,610
Total cost of grandfathering (Rs. Crores)	20,474
Incremental cost over TPDS (Rs. Crores)	23,951
Total including grandfathering -- Rs. Crores	44,425

Table 4. Misclassification in BPL: Fiscal Costs

	25% leakage
Additional individuals ('000)	89,654
Total foodgrain per person (kg)	5
Total foodgrain req (mn tons)	5
Wheat	2.4
Rice	2.9
Addition cost to govt (Rs. per ton)	
Wheat	18102
Rice	23436
Total subsidy bill (Rs. Crores)	
Wheat	4,431
Rice	6,871
Total	11,301
Baseline incremental cost of NFSB (Table 3) -- Rs. Crores	23,951
Baseline Incremental Cost + Mis-classification Cost (Rs. Crores)	35,252
Baseline Incremental Cost + Grandfathering+ Mis-classification Cost (Rs. Crores)	55,726
Baseline Incremental Cost + Grandfathering+ Mis-classification Cost+Additional Misc Expenditure (Rs. Crores)	76,486

**Table 5. Summary Table: Incremental Cost of NFSB and NFSB_2
Relative to TPDS: 2013-14 (Rs. Crores)**

	NFSB_2
1/ Baseline	23,951
Additional Costs Relative to Baseline	
2/ Grandfathering	20,474
3/ Misclassification	11,301
4/ Miscellaneous expenditures	20,760
1/+2/+3/+4/ % of GDP	76,486 0.67
5/ 40% additional procurement	4,925
1/+2+3/+4/+5/ % of GDP	81,411 0.72