

Building efficient commodities markets: How can warehousing help?

NIPFP

February 25, 2014

Warehousing and Food Prices

Decision:
Land for
p1 vs. p2

June

October
(*Harvest*)

March
(*Peak price*)

Decision:
Storage for
p1 vs. p2

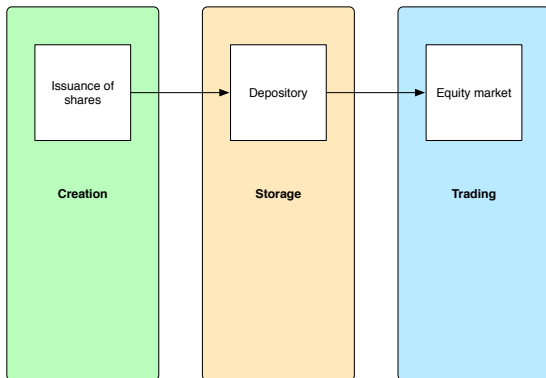
Warehousing and Food Prices

- High intra-year price fluctuations:
 - Max/Min ratio for average monthly wholesale price of onion in 2013: Onion - 4
 - Vegetable component of price index most volatile
- 70% agricultural land to produce wheat and rice (25% of value of food produce)
- High quality, abundant warehousing can help farmers
 - Store to sell at the optimal time
 - Access loans with commodities as collateral, for consumption during the holding period

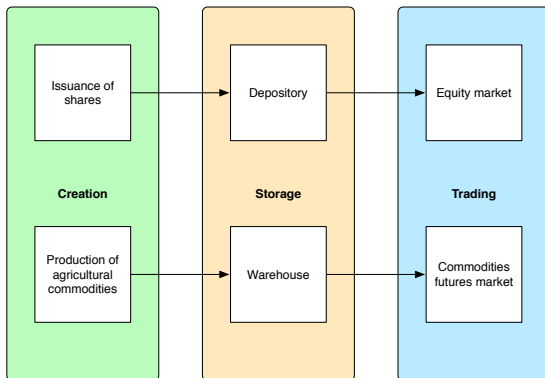
1. High quality, abundant warehousing could help

- *reduce intra-year price fluctuations for non-traded food commodities, and*
- *encourage more efficient allocation of farming resources.*

Compare: Equity Market



Compare: Warehouses as "Depositories"



Warehousing and Food Prices

2. High quality storage is essential to connect primary markets with secondary market in agriculture commodities.

- Unreliable storage leads to
 - high transaction costs for trading, especially over long distances
 - difficulties in settlement of trade
 - poor development of negotiable receipts
 - low trust in commodities markets -> low participation
- Uncertainty in storage reduces depth and liquidity of markets

Will a “depository-type” solution work?

- Commodities markets are different
 - Dispersed storage: not feasible to store commodities centrally in one place
 - Diversity: high level of diversity in characteristics of commodities coming from different places
- *Solutions have to be different.*

The objective

- The objective should not be to improve the quality of warehousing *at any cost*
 - Quality should be market-determined

The objective

- The objective should not be to improve the quality of warehousing *at any cost*
 - Quality should be market-determined
- Modest objective: *people should get what they pay for.*
 - Low uncertainty about what one will get when the commodities are received from the warehouse.

Warehousing market in India

- Weak systems of producing and making available information on quality of warehouses
- Thriving business of collateral management services
- Regulation
 - WDRA gives registration to warehousing, and regulates accreditation agencies
 - Weak penalties for poor performance

Solutions

- *Solutions should generate incentives for warehouses to fulfil contracts, instead of prescribing expensive standards*
- Market-driven
 - How can the information infrastructure around warehouses be improved?
 - Information repository on warehouse performance?
 - How can users know more about the quality of warehouses?
- Regulator-driven
 - Strengthening penalties for violations?