MicroSave India Focus Note #139

Fair Price Shop Sustainability in Automated TPDS: A Mirage or Possibility?

Arshi Adil, Lokesh Kumar Singh and Rridhee Malhotra

August 2016

Key Points:

1. *FPS automation addresses challenge of diversion but this also results in lower financial viability*
2. *It becomes imperative to cross subsidise FPS operations to make them sustainable*
3. *The government can either have community run organisation to run FPS operations or have FPS sell other commodities/ products as well as such as through public private partnerships like ABY*

Introduction

With a budget of INR 1,240 billion (US$ 19 billion) in 2015-16, Targeted Public Distribution System (TPDS) is the largest social security programme in the world. It distributes approximately 20% of India's wheat output and 15% of its rice output, and operates through a network of 478,000[1] fair price shops. PDS began as a measure to ensure self-sufficiency in staple food grains for the country and then became a major food safety net for the poor.[2]

However, according to the Shanta Kumar Committee set up by the government, more than 46% of grains supplied under PDS are being diverted. To address such large-scale diversions, governments (central and state) started digitisation of the PDS supply chain. The digitisation process was mandated by National Food Security Act 2013 (NFSA). Through de-duplication (removal of duplicate beneficiaries) and biometric authentication at the time of food grains uptake, Fair Price Shop (FPS) automation has addressed challenge of diversion, as it ensures that only intended beneficiaries (those who are listed and Aadhaar authenticated) access subsidised food grains.

On the other hand, a negative consequence of this development is the deteriorating financial viability of FPSs. A majority of FPS owners report that income under the digitised set-up has dropped drastically. Our study in three states where large-scale FPS automation has occurred, highlights the problem for the FPS owners.

On an average, an FPS owner's monthly profits are much lower than the prescribed minimum wages under MGNREGA. Considering the effort, risk, time and investment by FPS owners, these returns are inadequate. It is a matter of time before FPS owners shut their operations and look for alternative businesses offering better returns – a fact that came out very strongly in our discussions with FPS owners.

Table1: State Wise Financial Viability of FPS Owners[3]

State	AAY cards	PHH cards	Grain sold (Kg.)	Commission	Bag sale	Income	Expenses	Netprofit
	A	B	C=A*35+B*3*5	D=CX0.7	E=C/50*2*10	F=E+D	G	H=F-G
Chhattisgarh	137	403	10,840	7,588	4,336	11,924	9,305	2,619
Gujarat	49	364	7,175	5,023	2,870	7,893	6,000	1,893
Madhya Pradesh	76	458	9,530	6,671	3,812	10,483	7,056	3,427

Ways to Ensure FPS Continuity

Table 1 highlights that standalone FPS business is not financially viable. Obvious responses could be to increase the beneficiary base, which is already about 500 households per FPS. At this level—assuming, on average, five minutes per transaction (including weighing commodities, Aadhaar authentication, and payment in cash)—it would take a minimum of five days to deliver the benefits. This is all the time available to the FPS as almost all these transactions take place within a week of arrival of commodities. Thus, going beyond this number is improbable. Enhancing commission for the commodities sold could be another solution. However, that option is not currently acceptable to the government.

In order to make sure that the government is meeting its commitment of ensuring food security, it is essential that the FPS network (or alternative outlets with cash transfers under TPDS) is in place. We know from our experience that the private sector is in no position to serve this segment, especially in difficult terrains (please read our note here). It is thus imperative to cross-subsidise FPS to ensure service availability. There are two potential methods of cross-subsidisation.

The first method would be to deliver TPDS through social organisations such as NGOs/cooperatives/ SHGs. The second method would allow FPSs to sell items other than only subsidised food grains, as is currently the practice.

a. Social organisation-run FPSs: The Government of Chhattisgarh received many complaints about irregularities after the

1 Please see http://pdscvc.nic.in/Annexure%20C.pdf for statistics

2 Please see http://dfpd.nic.in/public-distribution.htm for a brief history of evolution of public distribution system

3 Assumptions: Average number of cards per FPS=total cards/total FPS; allocation per AAY is 35 kg, whereas, for PHH, average is three units per card

partial privatisation of FPS network in 2001. Of the 1,525 cases registered against FPSs in the period 2001–04, approximately 1,200 (79%) were against private dealers. The State Advisor for the Supreme Court investigated these complaints and issued a report indicting the role of private dealers in the PDS. Following the release of the report, the State government introduced the 'Chhattisgarh Public Distribution System (Control) Order' in 2004. Within six months of the commencement of this order, the government cancelled all FPS licences given to private persons and allotted these to grassroots level, non-private organisations including: Large Aadim Jaati Multipurpose Cooperative Societies (LAMPS), Gram Panchayats, Women's Self-Help Groups (SHGs), Forest Protection Committees (FPCs), and other cooperative societies. The Chhattisgarh Government took two measures to strengthen the economic viability of the new FPS, primarily:

- It provided each FPS run by the Panchayat or SHGs, financial support of INR 75,000 (US$ 1,100) to ease the challenges associated with the upfront costs, inventory management and working capital requirements.
- Commission to the FPS operators was also enhanced to ensure a minimum net profit margin.

Out of 11,077 fair price shops, as many as 4,131 shops are being operated by Gram Panchayats, 4,354 shops are operated by cooperative societies and 2,405 shops are operated by women's SHGs.

Similarly, to ensure a member-oriented and self-reliant FPS network, the government of Madhya Pradesh mandated cooperatives to manage FPS operations. Currently, 322 lead and 4,724 link cooperative societies run 20,920 FPSs. Of these, around 75% of the shops are in rural areas and in some remote areas, the State Civil Supplies Corporation operates Fair Price Shops through mobile vans.

In both states, cooperatives also run other lines of businesses. These primarily include forward and backward integration activities for farmers, savings and thrift accounts for members, etc. These activities ensure that the sustainability of running an FPS is not significantly affected by the low margins (or even negative margins in some cases) earned from standalone FPS business. Additionally, as the very members who are also recipient of subsidised food grains run the FPS, it ensures accountability and responsiveness.

b. Private sector and diversified inventory: Rajasthan entered into an MoU with Future Group—a giant private retailer—to supply branded, high quality goods to be sold through FPS outlets.

In this model, FPSs are revamped and turned into commodity super stores, branded 'Annapurna Bhandars' (ABs) (literal "Food Bounty Stores"). The objective is to enhance the financial viability of FPSs, as well as to modernise PDS in the state, by offering a wide range of quality goods for consumption by the beneficiaries. By offering competitively priced, multi-brand goods, FPS owners are able to build a stronger customer base and higher sales. This is expected to offset the risk associated in selling only PDS items. Table 2 highlights the economics of the model.

Table 2: Revenue Structure of Annapurna Bhandar Owner

Particulars	INR
Additional sales/month	66,000[4] (US$ 988)
Profit margin	10%
Additional revenue	6,600 (US$ 98.8)

This looks quite attractive in addition to the profit / surplus from basic PDS commission. While the real benefits (and drawbacks) of this tie-up will only be visible over time, for now it has definitely enhanced the product range resulting in enhanced incomes (and profit) for the FPS owner from sale of non-PDS items.

Conclusion

In the absence of either an expanded beneficiary base or significantly enhanced commissions/salaries for FPS owners, state governments are largely left with two options:

a. Handing over the operations of FPS to community-run organisations: This model affords PDS the advantages of customer centricity, transparency, and accountability. Co-operatives that are already running parallel business lines, such as credit or dairy, can cross subsidise the losses or low margins from selling only PDS products.

b. Public–private partnerships: ABs are a bold initiative. However, there are some short-term challenges that must be addressed. These include capacity building for FPS owners in modern retail management, inputs on better cash flow management, and maybe even access to working capital loans. Another concern is that, by handing over FPS outlets to a large chain, such as the Future Group, the state may create a monopolistic market in rural areas. The assured footfall that subsidised food-grain supply will bring to AB outlets can potentially create unfair competition.

Considering the challenges, infrastructure, and the magnitude of grain distribution, state governments will have to choose carefully between these two options (or explore others) and monitor them closely over time.

4 Figures based on our field research with Annapurna Bhandar owners in Kota, Rajasthan