Transition from WPI to PPI

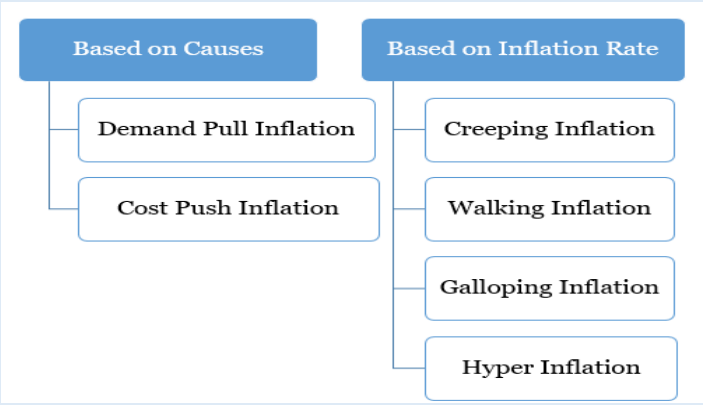
Why in news?

The Department for Promotion of Industry and Internal Trade (DPIIT) in consultation with the Ministry of Statistics is close to finalise a model to launch a PPI in India that may eventually replace the WPI.

How inflation is measured in India?

Inflation

• **Inflation** – It refers to *consistent increase in the general prices* of goods and services.
• **Inflation rate** – It is a metric used to gauge how fast the general prices rise over a defined period, often a year.
• **Disinflation** – It is *decrease in rate of inflation*, whereby prices *continue to increase but at a slower rate*.
• **Types of inflation**



• **Impact of inflation** - Over time, the purchasing power of money diminishes as the cost of living rises.
• This can impact consumers, businesses, and the overall economic landscape.
• **Deflation** – It is a *sustained decrease in the general price level* of goods and services.

- **Calculation** – Authorities in India *use price indices* to determine the change of rates of commodities and services, thus the inflation or deflation is calculated.
  - **For example**, if the rate of rice a year ago was Rs 20 a kilo and currently it is Rs 22 a kilo, the inflation in the rice prices would be at 10%.
- **Assigning weightage** – While calculating inflation, the weight of a product is considered higher if consumers expend larger share of their income on that product.
  - **For example**, *household expenditure is higher on food and fuel* than postcards or shaving creams, hence given more weights while calculating the inflation.
- **Evolution of measurement** – In India, generally, two kinds of indices are used to measure inflation—Wholesale Price Index (WPI) and Consumer Price Index (CPI).
- **Before 2014** – RBI had given more weightage to *WPI as the key measure of inflation* for all policy purposes.

- The WPI was calculated by the Ministry of Commerce and Industry shows the combined prices of a *representative basket of wholesale goods*.
- It is *primarily used as a GDP deflator*.
- **After 2014** – Based on the Urjit Patel committee recommendations, RBI had adopted *CPI (combined) as a key measure of inflation*.
- CPI considers the weighted average value of a basket consisting of 299 items.

	CPI	WPI
Definition	Measures changes in the price level of a basket of *consumer goods and services* purchased *by households.*	Measures changes in the *price of goods at the wholesale level*, before they reach the consumer.
Base Year	2012	2011-12
Frequency	Monthly	Weekly and monthly
Components	Food, beverages, housing, clothing, health, education, etc.	Primary articles, fuel and power, manufactured products.
Reflects	*Cost of living and inflation* experienced by consumers.	*Inflation at the wholesale* level, affecting business costs.
Measuring agency	Central Statistics Office (CSO)	Office of Economic Adviser, Ministry of Commerce and Industry

The lowest inflation rate, technically deflation, was recorded in May 1976 at (-) 11.31%. On the other hand, highest inflation rate observed was 34.68% in September 1974.

Why India needs a transition from WPI to PPI?

***BN Goldar Committee** is a 13 member committee to devise an all new barometer called Produce Price Index instead of Wholesale Price Index*

- **PPI** - Producer Price Index (PPI) measures the *average change in the selling prices received by producers* for their goods and services.
- It is calculated based on the prices of goods and services at various stages of production.
- It *excludes indirect taxes* from calculation and thus can avoid any tax fluctuations.

	WPI	PPI
Scope	Domestic and International goods	Only domestically produced goods
Coverage	Only on goods	Both goods and services
Purpose	It looks at wholesale prices	It emphasizes on production costs
Tax fluctuations	Yes	No
Multiple Counting Bias	Yes	No

- **Need of PPI** – Unlike WPI, it *includes services* along with goods and captures price changes from the *perspective of producers*, *offering a supply-side inflation measure*.
- **Better targeting** –It leads to *more targeted monetary and fiscal policies* and also aids in understanding inflation transmission from production to consumption.
- **Global comparability** – It will *align India's inflation measurement standards with international practices.*
- It facilitates better comparison with global economies, aiding in economic analysis and decision-making.
- **Improved economic analysis** - It enhances the understanding of *industry-specific inflation trends* and also assists businesses in pricing strategies, contract adjustments, and financial planning.
- **Enhanced transparency** - It *promotes transparency* in the pricing mechanisms and cost structures of industries.

What are the challenges in transition to PPI in India?

India have taken the International Monetary Fund's advice on the methodology to devise PPI model and the National Statistical Commission (NSC) is examining a working group report on the roadmap for introducing PPI in India.

- **Difficulty in data collection** - Gathering detailed data from diverse industries and services is complex and resource-intensive.
- **Lack of infrastructure** - Establishing and maintaining IT systems for comprehensive data reporting requires significant investment.
- **Lack of expertise** - Training personnel for accurate data collection and analysis is challenging due to lack of expertise.
- **Structural issues –** Bureaucratic hurdles and lack of cooperation can slow down the transition process.
- **Stakeholder resistance** - Businesses and industries may resist the transition due to increased reporting requirements and potential cost implications.

What lies ahead?

- **Enhance data collection** - Implement reliable and accurate data collection systems using advanced technology.
- **Standardize protocols** - Develop and enforce uniform data collection and reporting standards across sectors.
- **Upgrade infrastructure** - Invest in IT infrastructure and provide training to improve data management and analysis.
- **Broaden sectoral coverage** - Expand efforts to include informal and small-scale industries, ensuring comprehensive data representation.
- **Reform policies** - Create supportive policies and align regulations to facilitate the PPI transition.
- **Increase awareness and training** - Conduct training and awareness programs for stakeholders on PPI benefits and implementation.

- **Pilot and phased implementation** - Start with pilot projects and adopt a phased approach for gradual and effective PPI rollout.

References

1. The Financial Express | Producer Price Index
2. Business Standard | Producer Price Index in India
3. Investopedia | Inflation

