WHY MSP IS NOT A SOLUTION - EDITORIALS - HINDUSTAN TIMES

Relevant for: Indian Economy | Topic: Issues related to direct & indirect Farm Subsidies and MSP

A key debate after the enactment of three farm-reform laws and the subsequent protests is around the issue of federally-fixed minimum support prices (MSPs), a system guaranteeing farmers assured prices for their produce through procurement. MSP is an obligatory, not a statutory exercise. Farmers have demanded a legislation to prohibit sale of any farm produce below these minimum prices. If the government agrees to this, it is likely they will end their protests against the three new farm reforms.

But a law making MSPs the legal floor price defies economic logic. The government sets MSPs for 23 crops, but it is effective only in case of rice and wheat because it buys only these two commodities in sufficiently large quantities. MSPs are an assurance that the government will intervene if market rates fall below that threshold, thereby helping avoid distress sale. This policy was salutary when India faced acute food shortages. Farm policies to deal with surpluses will fundamentally have to be different from measures adopted to overcome a previous era of scarcity. A law barring purchases of the other 21 crops below MSPs by any private trader will also, immediately, fuel high inflation. Every one percentage point increase in MSPs leads to a 15-basis point increase in inflation. Higher MSPs could also upend the Reserve Bank of India's inflation targets, hurting economic growth. An MSP mechanism that ignores demand and global prices creates market distort-ions. If it is not profitable for traders to buy at MSPs, then the private sector will exit the markets. In such a scenario, the government cannot be a monopoly buyer. Mandatory MSPs will render India's agri- exports non-competitive because the government's assured prices are way higher than both domestic and international market prices.

MSPs have also incentivised foodgrains over other crops, giving rise to imbalances of water and land resources and shifting land away from crops such as pulses and oilseeds, necessitating costly imports. Surplus cereals can't be exported without a subsidy, which invites the World Trade Organization (WTO)'s objections. WTO rules cap government procurement for subsidised food programmes by developing countries at 10% of the total value of agricultural production based on 1986-88 prices in dollar terms. There is no argument that farmers need support, but policies that are less distortionary are in the interest of both farmers and consumers.

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