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FROM PLATE TO PLOUGH: A WIN-WIN DEAL

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

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In her budget speech, the Union finance minister (FM) said: "At the centre of everything that we do, we keep *gaon, garib aur kisan* in mind." Here then is a small mantra for her to transform the lives of the kisan and the poor in rural areas. Just streamline the food and fertiliser subsidies by converting them to direct cash transfers to identified beneficiaries. This can be done through the JAM trinity (Jan Dhan, Aadhaar and Mobile). Such a measure would not only empower the poor and farmers but also usher in a policy shift that can save the exchequer least Rs 50,000 crore every year. The government can invest this in agri-R&D and better water management, in measures to ensure the country's food security for the next 25 years and to augment farmers' incomes.

Let us first talk about the food subsidy. The food subsidy allocation in the budget is Rs 1,84, 220 crore — let us say Rs 1.84 lakh crore. How many are aware that the pending dues of the Food Corporation of India (FCI) stand at Rs 1.86 lakh crore? Year after year, there is under-provisioning of the food subsidy in the budget and the FCI is being asked to borrow from the banks so that the fiscal deficit can be shown under control. The FCI's loans from the banks have now crossed Rs 2.48 lakh crore (see figure).

Two things stand out. One, the under-provisioning of the food subsidy — including overdues — in the budget. There is more under the carpet (Rs 1.86 lakh crore) than in the budget (Rs 1.84 lakh crore). Two, the real deficit in the budget is much more than what is claimed.

But here I am more concerned about the efficiency, equity and sustainability of the food subsidy regime under the National Food Security Act (NFSA) — a legacy of UPA-2. Does the FM really think that 67 per cent of the population covered under the NFSA cannot afford basic food? There is more than 90 per cent subsidy on rice and wheat under the PDS — the economic cost of rice hovers around Rs 35 per kg and that of wheat is about Rs 25 per kg, while rice is being sold via the PDS at Rs 3 per kg and wheat at Rs 2 per kg.

Interestingly, in rural areas in a majority of states, rice (paddy) is sold at less than the minimum support price (MSP). The landless labourers and small and marginal farmers, most of whom are covered under PDS, produce these staples. The government first buys paddy and wheat from rural areas and, after adding almost 50 per cent cost for procurement, stocking and distribution on top of the MSP price, sells the back most of this grain to people in rural areas. The government can achieve its ends in a much more cost-effective way if it transfers an equivalent amount of food subsidy in the form of cash to the beneficiary's accounts. The beneficiary will have the freedom to buy anything — rice, wheat, coarse cereals, pulses or even milk and eggs, which are more nutritious. Diversified diets will signal the need for diversification in farms. The government can keep some stocks for strategic purposes but gradually reduce procurement and shrink the size and operations of FCI, especially in areas where the water table is depleting fast — the northwest of the country, for example.

Further, the government has to think whether the coverage under PDS should be 67 per cent of the population or if it should be brought down to, say, 40 or even 30 per cent. Also, the NFSA allows the government to hike issue prices. Why should the price of rice be kept at Rs 3 per kg and that of wheat at Rs 2 per kg? This leads to massive diversion of PDS supplies to the open market. The Shanta Kumar Panel had estimated the leakages in PDS at 46 per cent.

The Modi government has introduced PoS machines and weeded out some fake ration cards. But leakages continue — rough estimates put it at 30-40 per cent. Fair price shop (FPS) owners are much smarter than the government. Leakages can be reduced if the issue price is linked to say 50 to 75 per cent of the MSP. If the Modi government can do this, not only will it result in massive efficiency and equity but ensure sustainability as well.

Now, look at the fertiliser subsidy. The FM has allocated Rs 80,000 crore for fertilisers in the budget. The fertiliser industry says that there is massive under-provisioning. The industry also claims that Rs 38,000 crore of its dues are pending with the government. With this under-provisioning, the subsidy dues will cross Rs 50,000 crore. Which industry can feel upbeat if its dues from the government pile up, year after year?

The problem is that the government does not have the will to revise the urea price, which at roughly $80 per tonne, is the lowest in the world. The average cost of production of the industry is around $250 per tonne, import parity hovers around $300 per tonne and keeps fluctuating, depending on global prices. The government has revived some almost dead plants (for example at Gorakhpur and Ramgundam) that produce urea at more than $400 per tonne.

It seems there is no economic rationale either in the pricing of urea for the farmers at $80 per tonne or producing urea, at the margin, at $400 per tonne. This is leading to large leakages and inefficient use, besides polluting the groundwater table — in fact, the environment at large. Interestingly, crops do not absorb more than 25 per cent of the urea being applied in India. So, basically, we are subsidising the pollution of the environment.

Can the Modi government rationalise these subsidies by converting them into direct cash transfers on a per hectare basis? Our back-of-the-envelope calculations show that the government can save about Rs 50,000 crore every year through such measures. The money can be invested in agri-R&D and water management. That would be the biggest reform in agri-food space

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