Target incomes, not prices

Our farm policy is so bad, the proverb ‘you reap what you sow’ isn’t true any longer. A bumper crop is no different from a drought, for it too depresses farm incomes.

Good rains, excessive sowing and the bumper harvest last year produced gluts in the market that sent the prices of many crops, and therefore farm incomes, crashing. None of the economic tools available for protecting farm incomes — the price support scheme, the price stabilisation fund and the market intervention scheme — was employed to the best advantage. Quick and precise adjustments to the export and import rules could have arrested the price fall by diverting the excess supplies to overseas markets. But the changes required were not carried out in time. Instead, inflows of imports were allowed to go on, which worsened the price situation.

This year’s Budget promised that the Minimum Support Prices (MSPs) would be at least 150% of production costs, a longstanding demand of farmers and recommendation of experts. Even if the market prices fall below the MSP, as they did for major kharif crops in 2017, the government will procure the produce on MSP. And if it does not procure, it will provide a mechanism to ensure payments, equal to the gap between the MSP and the market price, would reach farmers.

The intention of assuring 50% profit margin over the cost of production is to make farming remunerative. On the formula for calculating production costs for plugging into the MSP formula, farmer groups and the government are not as yet on the same page. But howsoever production costs are calculated, simply announcing higher MSPs will not raise farmer incomes. The system is not geared for scaling up procurement.

For several crops last year, the quantities procured were small portions of the total produce. Although MSPs are announced for more than 20 crops, noteworthy procurement is conducted for three: paddy, wheat and sugarcane (procurement by sugar mills, not the government, given cane must be crushed within a few hours of being cut, or it dries, impacting sugar recovery drastically).

Further, procurement frequently takes places at prices below the MSP, as is happening this year, according to reports. Finally, small and vulnerable farmers usually do not get paid MSPs at all, as they sell their produce to aggregators, not directly in mandis.

In these circumstances, and given an imminent general election, the government is likely to take recourse to payments compensating for the difference between market prices and the MSP to appear farmer-friendly. In principle, it is only right and fair that the government pay reparations to farmers. The gluts, depressed market prices and mounting farmer losses are a direct consequence of the malfunction in agri-pricing policies.

But price differential payments, no matter what mechanism is used for calculating and distributing them, would be yet another example of economic policies that get drafted purely on political appeal, without full grasp of the underlying economic principle, and backfire badly.

A set of estimates of the price differential payments likely this year, premised on realistic assumptions, from agriculture economists led by Ashok Gulati projects that the MSP of paddy for the 2018-19 kharif season will have to be raised 11-14%, cotton 19-28%, and jowar 42-44%, if the MSP pricing formula of 1.5 times the cost is employed.

A rational response of farmers looking at this menu of MSPs would be to sow more jowar in the next season. The promise of profits is greatest for jowar. The policy will unwittingly lead to increased jowar production. There’s no reason the demand for jowar would also rise. A demand-

supply mismatch would be inevitable which would send the market prices for jowar way below the announced MSP, calling for significantly expanded jowar procurement at MSP.

The trouble is, pricing policies distort market prices and send the wrong signal to farmers on what to produce and how much. Our inept policy system fails to correct such situations, which then spiral out of control. But if the problem is volatile incomes, the solution must target incomes, not prices. Income support payments, paid on a per hectare basis through direct transfers, offer an administratively neater, economically far less distortionary and politically more attractive solution.

Telangana has announced such payments for farmers at the rate of 10,000/ha (4,000/acre) per season. The cost projections for scaling up this model to the national level, excluding the procurement of sugarcane, wheat and paddy, and non-MSP crops, are roughly as much as the estimated bill for the price differential payments. For total gross cropped area of 1,978 lakh ha, income support payments would add up to 1.97 lakh crore, which is equal to about a fifth of the total gross non-performing assets of the banking system in March this year. At 5,000/ha, the tab for income support would be about 98,500 crore.

The impression was that the farmers' long march to Mumbai a few months back forced urban India to reassess its position on the severity of the agrarian distress. But advantaged Indians have begun questioning the logic of fiscal support for farmers on the grounds that it is unfair to make the majority pay to keep afloat a high-cost, low productivity, income-tax exempt sector that contributes just 17-18% of the country's GDP. They forget that the agriculture sector engages more than 50% of the total workforce, and that agri-prices, and therefore farm incomes, are not free-market driven. They are kept artificially low, through use of pricing policy instruments, so that inflation does not erode the rest of the population's purchasing power.

The current farm crisis is purely because of policy failure. Fiscal space must be found for providing income support this year to the most vulnerable farmers at least. Over the longer term, there is no alternative to deep reforms.

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This refers to the tendency to form friendships and other forms of interpersonal relationships with people we come across often in our daily lives.

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