Four steps to stabilize the price of pulses

Consumers worry about high prices of pulses and producers about low prices. Typically, inflation peaks whenever there is a production shortfall. On average, the peaks have hovered 40 percentage points above the “zero” level, while the dips are only 12-13 percentage points below. Somewhat predictably, therefore, pulses have seen an average annual inflation rate of 12%—the highest among food crops—in the past 12 years.

The current cycle has seen extraordinary volatility. The steepest peak (49%) was in November 2015 and the steepest fall (-32.6%) in June. Also, the price fluctuation has been broad-based (across pulses) compared with earlier cycles, where inflation was driven by individual categories of pulses. This dip is also different from those observed in the past, since more than half the price rise seen in the previous year has been wiped out. A bumper crop in fiscal 2017 (40% jump in production), accompanied by six million tonnes of imports and exports and stocking restrictions, led to oversupply and price collapse.

Our study of five key pulses—*tur, urad, gram, moong* and *masur*—shows that they all display a “cobweb” phenomenon, wherein production responds to prices with a lag, causing a recurring cycle of rise and fall in output and prices. This reflects the behaviour of farmers who base their sowing decisions on the prices observed in the previous period, and accordingly over- or under-produce crops, triggering price cyclicality. Gram is, however, an exception. Here, production responds more to global price trends than domestic, possibly because of open trade and exposure to the forwards market. Given this, we believe price stabilization measures should be a mix of government intervention and developing market-based mechanisms to protect against price risks, such as:

Effective MSPs and production

Over 20 crops are covered by the minimum support price (MSP) scheme. However, historically, only wheat and rice have benefited from effective procurement.

To be sure, MSPs help smoothen prices and act as price signals when procurement is effective. This reduces the farmer’s risk. In pulses, however, although MSPs are announced, procurement has been relatively weak and often, pulses are sold below the MSP and even below the cost of production. For instance, *moong* and *urad* are now selling below their production cost. Therefore, the government should raise procurement of pulses under the MSP scheme to make it effective. In addition, the procurement infrastructure needs to improve and focus sharpened on raising awareness of and access to government agencies procuring crops. The price stabilization fund could be used to improve procurement infrastructure. Buffer stocks can be created during years of excess production and used in times of shortfall. This should be the priority of the government till infrastructure and markets for agricultural products develop.

A nimble trade policy

The government has prohibited exports of pulses, except gram and organic pulses, since June 2006. The restriction, which was supposed to be valid for six months, has been extended from time to time, with the last extension order in March 2014. The case of gram has showed that the international market can absorb production in excess of domestic demand. Therefore, flexibility in export policy, in terms of permitting exports of the restricted pulses during times of excess production, will help provide some cushion.

Developing an irrigation buffer

Only a fifth of the area under pulses has irrigation support. This exposes production to the vagaries of the monsoon and amplifies the price cyclicality. Hence, there is a need to develop an irrigation buffer. Promoting water-conserving irrigation techniques such as drip irrigation can help.

Well-regulated markets

Developing agricultural markets is always a tough ask, particularly for essential commodities such as pulses that are prone to price manipulation. Most farmers sell their products locally below MSP due to lack of transportation and the long distances to *mandis*.

The government should reduce the transportation costs of farmers by linking them to markets with better roads. To incentivize private sector participation, ad hoc restrictions on stocks should be avoided.

Forward contracts help reduce the uncertainty of future market prices. The government can use future market signals to fix MSP values and make appropriate interventions before crises occur. The farmers can then make their decisions on the basis of expected prices and not past prices.

However, the vulnerable segments are geographically dispersed, asset-poor small farmers with limited access to knowledge and markets (*Price Volatility In Food And Agricultural Markets: Policy Responses*, FAO and OECD, 2011). This means the government and regulators have their task cut out to increase these farmers' awareness and information about futures markets.

Further, developing the spot and futures markets will require infrastructure improvements such as grading and storage facilities, and electronically linked warehouses. The regulator will also need to ensure that mechanisms to check unfair price speculation are in place.

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