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Appeasing producers

The move for a sugar buffer is not only anti-consumer but also anti-exchequer, says **Uttam Gupta**

PRICING of sugar defies economic logic. It has no relationship whatsoever to the cost of production and distribution which, in any case, lacks transparency. No producer would give the break-up of the cost and the underlying norms for computing it. Nor has the government ever shown any inclination to make them do so. This is despite the fact that it controls almost every aspect of the industry from issue of licenses to controlling monthly releases even of the so-called free sale sugar.

Can we say that sugar price is determined by the forces of demand and supply? Going on the basis of recent trends, the answer is a categorical 'No'. Irrespective of whether you have surplus or deficit, the sugar prices have ruled high. While in the former situation, the producers consider more than reasonable profit margin as their fundamental right, in the latter they rule the roost reaping super-normal profits.

Sustained high price of sugar despite a huge stock of 54 lakh tonnes (as of September end 1995) and the anticipated bumper production during the 1995-96, defies logic. Yet the Prime Minister has reportedly agreed to the demand of the sugar industry to create a 10-15 lakh tonnes buffer stock. In fact, a sum of Rs 200 crore is proposed to be dedicated from the Sugar Development Fund (SDF) for this purpose.

The government should clearly spell out the reasons for conceding to this request and indicate as to what it proposes to do with the buffer and the modalities of creating and running it. Decision of such far reaching dimensions cannot be taken only on the basis of propaganda unleashed by the sugar barons that the country will be plunged into a sugar crisis in case the buffer is not created.

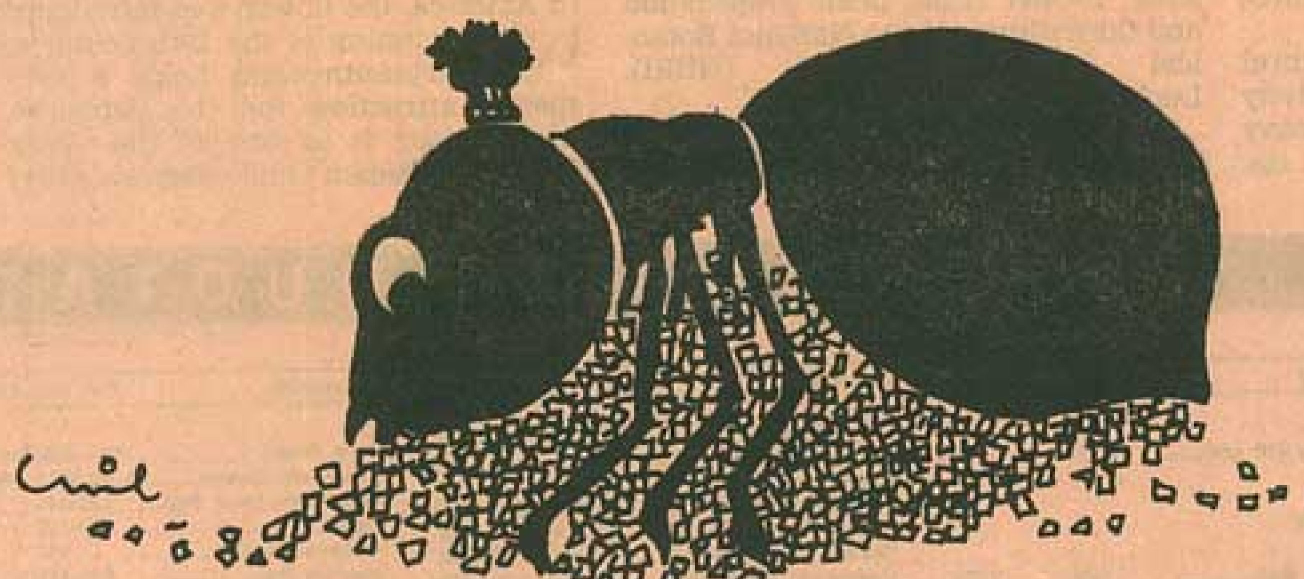
By definition, buffer is the reserve of any commodity aimed at offsetting the fluctuations in its prices and maintain stability. It is intended to reconcile the interests of the producers on the one hand and consumers on the other. At any point of time, the prices should not be too high as to adversely affect the consumers and, at the same time, it should not be too low so as to render production unremunerative.

In the context of sugar, however, all this is theoretical since prices have a tendency of moving upward only despite bumper production. There is, thus, absolutely no question of production becoming unviable. Consequently, the case for government buying the excess stocks with manufacturers is untenable.

In a reverse situation of shortage, as in 1993-94, the buffer was also unnecessary as increase in prices could have been prevented by resorting to timely imports. Necessary adjustment in the release of free sale sugar and continuous monitoring of the stock position would have also helped. All this was not done.

The industry has argued that it is incurring financial loss on account of carrying the excess inventory and that it is not even in a position to pay wages and salaries to the workers on time and unable to clear the arrears to the farmers. The alleged problems have been blown out of all proportions. Assuming for a moment that the industry is cash strapped, it is of their own creation and the solution lies with them only.

All that it needs to do is to deflate price sustantially. This will spur demand and thus enable liquidation of stocks and generate necessary cash. Further, it should also release bank funds which, in the present tight conditions in the money markets, could be better used elsewhere.



The manufacturers should also realise that even after reducing the selling prices, they would still be fully covering their reasonable cost of production and distribution. Considering the prevailing procurement price of sugarcane at about Rs 40 per quintal and taking a recovery factor of 8 per cent, the raw material cost works out to about Rs 5 per kg.

Taking Rs 12 per kg selling price to the consumers as the benchmark, the balance Rs 7 per kg should be adequate to meet the cost of fuel, water, conversion cost, marketing and distribution etc. This is especially so for majority of the sugar mills which are fully depreciated entailing negligible burden of capital servicing.

The intervention of the government by way of buying the industry stocks and creation of a buffer is totally unjustified and unwarranted. And yet, if it goes ahead, it will inevitably aggravate the miseries of the common man. To the extent of the purchases made by the government, effective supplies of sugar in the market will be reduced. Already, authorisation of substantial exports i.e. about 6.5 lakh tonnes has given the industry some leverage. Together with this, the buffer will help in sustaining existing high price or two even raising it further.

Even as the government is yet to decide on the terms of purchase of sugar from the manufacturers, it is likely to be the prevailing high market price. The possibility of the former buying at a lower price (as applicable to the levy sugar for sale thru the PDS) is ruled out as that would be unacceptable to the latter.

Having bought the stocks at prevailing high market prices, the government has two options. It may either sell the stocks immediately through the PDS at the lower controlled price i e about Rs 9 per kg or through departmental stores/Super Bazars at a slightly higher price, but still below its purchase price. This will mean an indirect subsidy payment to the extent of the differential between the purchase price, handling and distribution cost, on the one hand, and sale price, on the other. The exchequer will be indirectly paying for the profits of the sugar industry.

Alternatively, if the government holds on to the stocks, then, the situation will be even worse. The cost of sugar in the buffer will keep on increasing until it is finally disposed off. The Government cannot get rid off the stocks until shortage situation develops. Surely, this will not come about at least until the end of 1995-96 as production for this year also is expected to be a repeat of 1994-95. The possibility of sugar stored for too long getting damaged is also not ruled out.

Consequently, the loss to the exchequer in this alternative will be even more and will keep on increasing depending on the quantum of sugar purchased from the industry, the purchase price and the period of stay in the government's buffer.

Already, too much of intervention by the government and its agencies has imposed heavy penalties on the hapless consumers. The proposal to establish a buffer will make the situation even worse. It is not only anti consumer, but also, anti exchequer. At a time, when fiscal deficit is getting out of control, creation of the sugar buffer will cause extra subsidy burden.

The government should drop the contemplated move in the overall national interest. Instead it should undertake long pending reforms of the sugar sector which should include, amongst others, delicensing of sugar industry, removal of quantitative controls and distancing itself from the cooperative sugar mills.