THE HINDU • BUSINESS LINE
TUESDAY, JUNE 24, 2008

FERTILISER POLICY

Time to take hard decisions

Uttam Gupta

In recent times, fertilisers have been catapulted to the centre-stage for the following reasons:

Ballooning fertiliser subsidy that is likely to touch the Rs 100,000-crore mark during 2008-09;

Fertiliser producers facing unprecedented shortfall in subsidy payments due to huge under-provision in the Union Budget (during the current year, provision is only Rs 30,000 crore against a demand of Rs 100,000 crore!);

A substantial amount of subsidy payments to producers is in the form of bonds which they are forced to sell at discounts, thus denting their margin;

Surge in import of fertilisers and skyrocketing prices leading to huge increase in subsidy on imported products (a whopping Rs 50,000 per tonne on DAP);

Shortage of fertilisers in various parts of the country leading to farmers' protests (several cases have been reported in Rajasthan, Maharashtra, Karnataka etc);

Persisting imbalance in fertiliser use, leading to deterioration in NPK use ratio and consequential adverse effect on soil fertility.

IMPORTANT DECISIONS

In this backdrop, recently, the Cabinet Committee on Economic Affairs (CCEA) took two important decisions. First, the Government announced a nutrient-based price-cum-subsidy policy. Second, it has decided to pay freight subsidy for all fertilisers on actual basis.

To understand the first decision, a few basics are in order. Apart from three major well-known fertilisers — urea, DAP, MOP — there are a host of others where the three basic nutrients N, P and K are present in various proportions. The generic name for these is complex fertilisers. Historically, the Government had been fixing selling prices of various fertilisers in an arbitrary manner.

A close reality check would reveal that the only apparent consideration that went into the price setting was that it should be affordable to farmers. Each year, depending on the prevailing political situation, the Government would take a decision on the percentage increase in price that should be allowed. Invariably, urea being the most widely used and popular fertiliser, got the most favourable treatment implying least or no increase at all.

DECLINING YIELDS

As a result, an imbalance has been built up between the prices of different fertilisers. This has led to distortion in use patterns, deteriorating NPK-use ratios and increasing deficiency of micronutrients (such as sulphur and zinc). All this is showing up in the declining/stagnating yields.

In this backdrop, the first policy decision is welcome. Under the new dispensation, the prices of all fertilisers will be re-fixed by benchmarking them to the prices of N, P and K in the three main fertilisers — urea, di-ammonium phosphate (DAP) and Muriate of Potash (MOP).

At present, the selling price of urea (46 per cent N) is Rs 4,830 per tonne giving per kg N price of Rs 10.5. The selling price of DAP (18 per cent N and 46 per cent P) is Rs 9,350 per ton. Knock off value of 18 per cent N or Rs 1,890 (180x10.5) from this, we get Rs 7,460 which is attributable to 46 per cent P. This gives per kg price of P as Rs 16.2.

Now, for arriving at a price of, say, 20:20:0 (a product containing 20 per cent N and 20 per cent P), the derived value of N will be Rs 2,100 (200x10.5). And, the value of P will be Rs 3,240 (200x16.2). The price of this complex fertiliser will, thus, be Rs 5,340 per tonne.

The revised prices of complex fertilisers will be about Rs 1,000-1,500 per tonne lower than existing levels.

This will enable farmers to reconfigure use pattern keeping in mind crop/soil requirements instead of banking largely on three main fertilisers as at present.

FREIGHT SUBSIDY

As regards the second policy decision, the Government now gives freight subsidy to producers on a uniform basis, irrespective of the distance the fertiliser has to travel from the site of production to the consumer.

The producers, thus, have no incentive to reach the material to distant areas, especially in a situation of overall short supply. In this backdrop, switching over to payment of freight on actual basis will help achieve wider spread.

The above decisions reflect the government's seriousness in correcting the imbalance in fertiliser use, which will help increase crop yield, besides ameliorating soil fatigue. However, problems on the supply side remain.

This has to do with a dilemma that arises from the compulsion to rein in the ballooning subsidy and yet ensure adequate supplies to meet farmer's needs at prices much lower than the cost of supply.

In an era of skyrocketing fuel/feedstock prices, the cost of production and distribution of fertiliser is inevitably rising. And as prices to farmers cannot be raised, the Government either pays more subsidy or tells producers to absorb a portion of higher cost or both.

The Government must urgently put in place a nutrient policy that addresses stagnating production, rising imports and the ballooning subsidy bill.

Under the retention pricing scheme (RPS), the government has taken steps, especially since the mid-1990s, to make producers absorb a good portion of the rising cost by revising capacity utilisation, energy consumption norms and other efficiency parameters.

SCALING NEW HEIGHTS

And, yet, fertiliser subsidy has continued to scale new heights. From around Rs 10,000 crore in 1997-98, it grew to Rs 40,000 crore in 2007-08 and, during the current year, it is estimated at Rs 100,000 crore! This is mainly due to the unabated increase in fuel cost.

Thanks to a policy vacuum which has existed for close to a decade now, even the tempo of domestic production could not be maintained. Investors have not come forward to put up new capacity or even expand existing capacity.

The producers are not able to utilise even the existing capacity optimally due to the cash crunch resulting from huge under-provision in the Budget, issue of bonds that are not so easily tradable and ever rising prices of raw materials/feedstock.

This has led to increase in dependence on imports and prohibitive rise in the cost of imported fertiliser (in two years, the DAP prices have gone up from around $ 400 per tonne to $1,300 per tonne) and, in turn, increase in subsidy.

ISSUES TO BE ADDRESSED

We, thus, have on plate a deadly combination of stagnating production, rising imports and ballooning subsidy bill. The Government must urgently put in place a policy that addresses all the three. It may consider the following:-

It should give a clear policy direction to those who want to put up new greenfield projects as also those wanting to expand capacity at existing sites; both the categories may be considered for payment on import parity (IMPP) basis, of course, truncated by certain upper and lower limits;

Incremental production from existing plants — by way of de-bottlenecking and other efficiency improvement measures — too needs to be incentivised by paying them import parity price (IMPP) that will help ease supply constraint in the short run.

Additional supply from the above three routes will substitute the exorbitantly priced imports and, thus, ease the subsidy burden. Besides, supply from indigenous source is always preferred due to logistics reasons.

Among all existing producers, there is need to give some brownie points to those who perform better than others. This will help in extracting more output at a lower cost to the exchequer.

Feedstock/fuel issue has to be addressed on a war footing basis. The Government has done the right thing in giving fertiliser top priority in gas allocation.

The additional requirements — from capacity expansion — must also be considered on priority in all future allocations.

The Government has fixed a price of $4.25 per million British thermal units (Btu) for the Reliance gas from KG fields.

This is a good price for ensuring domestic production at competitive rates. It needs to be ensured that such supplies are not hamstrung by unnecessary legal wrangling.

Despite promising prospects of domestic gas supplies, we would still be heavily dependent on imported feedstock/fuel.

To get over this constraint, the Government should encourage joint ventures abroad — for finished products as in the case of urea and raw materials in the case of phosphate and potash.

(We need to have several Oman-type joint ventures, which during 2007-08 helped bring more than 1.5 million tonnes of urea at around $180 per tonne, nearly half the price at which normal urea imports were contracted.)

Finally, at some point, the Government must decide to give fertiliser subsidy directly to the **needy** farmers only, and allow the market forces to bring out the best from all stakeholders in the sector.

(The author is Resident Director, CropLife India, New Delhi. His views are personal.)