

Fertilisers: Less control more policy

Giving uniform subsidies at fixed rates and allowing producers and importers the freedom to fix selling prices will mean that suppliers can assess their viability based on reasonable cost of supply *vis-a-vis* prices, and plan accordingly. Farmers too will benefit from competition among suppliers, and subsidy outflows can be restricted to pre-determined levels, says **Uttam Gupta**.

SINCE decontrol in August 1992, the mess in the phosphatic and potassic segments of the fertiliser sector continues. While, on the one hand, the industry is sinking deeper and deeper into crisis, on the other, soil health is being affected due to the declining/stagnating consumption of phosphorous and potassium. The NPK-use ratio is also getting skewed. All these pose a great danger to the sustainability of agriculture and need to be addressed quickly.

Consumption of phosphatic fertilisers declined from 3.32 million tonnes in 1991-92 to 2.98 million tonnes in 1996-97 and potassic from 1.36 million tonnes to 1.03 million tonnes. Due to continued control and heavy subsidies for urea, consumption of nitrogenous fertilisers rose from 8.04 million tonnes in 1991-92 to 10.30 million tonnes in 1996-97. The NPK ratio worsened, from 5.9:2.4:1 in 1991-92 to 10.2:2.9:1 in 1996-97.

In 1997-98, consumption of P and K recovered to 3.92 million tonnes and 1.37 million tonnes respectively. With consumption of N going up to 10.91 million tonnes, the NPK use ratio improved to 7.95:2.85:1. However, even this was much worse than the pre-decontrol level of 5.9:2.4:1.

On the supply side, the installed capacity of P rose from 2.80 million tonnes in 1991-92 to 3.03 million tonnes in 1996-97. Production increased from 2.56 million tonnes in 1991-92 to 2.58 million tonnes in 1996-97, that is, a mere 0.02 million tonnes.

In 1997-98, the installed capacity moved up to 3.14 million tonnes. Production recovered to 3.06 million tonnes. However, for the producers margins continued to be under stress primarily due to the reduction in the concession rates — under the *ad hoc* concession scheme — retrospectively on February 3, 1998, in respect of sales during rabi 1997-98.

The bleak situation continues. During kharif 1998, production of P at 1.44 million tonnes was only 0.02 million tonnes more than in kharif 1997. Imports of diammonium phosphate (DAP) declined from 1.5 million tonnes in kharif 1997 to 1 million tonnes in kharif 1998 and the sale from 2.88 million tonnes to 2.78 million tonnes.

The trends during rabi 1998-99 being no different — inadequate supplies have led to widespread shortages in Uttar Pradesh, Rajasthan, Haryana, and elsewhere — the year would see a further worsening

of the NPK use ratio. Whereas, in the beginning of the 1990s, India aimed at an ideal ratio of 4:2:1, just a distant dream now.

While one may be tempted to attribute all this to the sudden decontrol, such an interpretation would be highly misleading. This is because these fertilisers were never decontrolled. In fact, within a month of announcing decontrol, the Government re-introduced subsidy, with effect from December 1, 1992, as *ad hoc* concession and, thus, brought controls back in through the back-door. However, these were fundamentally different from controls under the retention price scheme (RPS).

Before March 1976, all P and K fertilisers were free from pricing and distribution controls. In March 1976, the Government introduced a flat subsidy, that is, Rs. 1,250 per tonne of P-205, or Rs. 575 per tonne of DAP. However, producers were free to fix the selling price taking into account the reasonable cost of supply and the subsidy amount.

Since February 1979, the Government started controlling the selling price at a low and uniform level. For producers, it introduced the RPS, under which a fair ex-factory price was given to cover rea-

tion from 1.21 million tonnes in 1980-81 to 3.32 million tonnes in 1991-92.

Whereas under the RPS, the Government was committed to compensating producers for all increases in the cost of production (caused by any rise in input prices, depreciation of the rupee, and so on) thereby keeping the selling price immune, under the *ad hoc* scheme there was no such obligation. Although nothing prevented the government from adjusting the concession amount, considering that it was not specifically incorporated in the system, it was unlikely that cost escalations would be fully absorbed. The apprehension was not just theoretical.

Despite costs rising continuously, the concession amount — initially fixed at Rs. 1,000 per tonne of DAP — remained unchanged until 1995-96. As a result, there was pressure on the selling price. It rose from Rs. 4,680 before August 25, 1992, to a high of Rs. 9,500-10,000 in 1995-96. Following the increase in concessions in July 1996 and April, 1997, to Rs. 3,750, the price fell to Rs. 8,300 in kharif 1997. This is in sharp contrast to the RPS days when the price remained unchanged at Rs. 3,600 through the 1980s and increased to Rs. 4,680 in August 1991.

Fertiliser consumption is highly seasonal, necessitating timely supplies. This is especially so with phosphate, which has to be applied at the time of sowing. This, in turn, requires that manufacturers/importers know in advance, that is, before the commencement of the season, how much they would receive from selling the product. In other words, both the selling price and the concession amount — which add up to the realisation — should be notified in advance.

Until 1996-97, while the government notified the concession rates, the selling prices were fixed by the State governments. Generally, both delayed the announcement of the concession rate/selling prices, leading to uncertainties. In sharp contrast, under the RPS, there was no involvement of the States as both the selling prices and the subsidy rates were fixed by the government. Moreover, in the event of cost increases, the industry could get a fair idea of the likely new subsidy rate as per prescribed norms and continue production uninterrupted.

Fixing prices is a ticklish business. A good knowledge of the industry, principles of costing, prices of imported raw materials/intermediates, exchange rates and so on, is needed to do a fair job. State governments do not have adequate expertise. Quite expectedly, they acted in an arbitrary manner and fixed prices at unrealistically low levels.

This resulted in huge shortfalls in realisation *vis-a-vis* reasonable costs of production and distribution. Thus, supplies became unviable. For instance, during kharif 1996, in some States, realisations were Rs. 10,400 per tonne (selling price Rs. 7,400 per tonne plus concession Rs.

3,000 per tonne) against the production cost of about Rs. 11,400 — leaving a gap of Rs. 1,000.

Beginning 1997-98, the attention shifted to the Union government as, apart from the concession rate, it was to fix the selling price as well. It did a good job in kharif 1997. The price/concession rate was fixed at the reasonable level of Rs. 8,300/3,750 per tonne on indigenous DAP and these prices were announced before the season began. This paid rich dividends by way of adequate and timely sup-

were making payments as well, thereafter the government paid, but only after receiving certificate from the States. This inevitably led to inordinate delays, blockage of huge funds and liquidity problems.

Since 1997-98, the government decided to give 80 per cent of monthly claims upfront and the balance on receipt of verification report from the States. This was a good move, but the 20 per cent — that is, Rs. 880 per tonne (at Rs. 4,400 per tonne) — is a substantial amount and still

(in '000 tonnes)

	Production		Production N+P+K	Subsidy (Rs.cr)		Total
	N	P		Domestic Fertiliser	Imported Fertiliser	
1960-61	98	52	419	—	—	—
1970-71	830	229	629	—	—	—
1980-81	2,164	841	2,759	170	335	505
1990-91	6,993	2,052	2,758	3,730	659	4,389
1995-96	8,777	2,558	4,008	4,300	1,935	6,235
1996-97	8,599	2,556	2,014	4,743	1,350	6,093
1997-98*	10,086	2,976	3,246	6,600	826	7,426

* Estimated

Source: Economic Survey 1997-98

plies and resultant surge in consumption.

Thereafter, the Centre has acted no differently from the States. On supplies in rabi 1997-98, the concession rate on indigenous DAP was reduced to Rs. 3,500 per tonne (proportionately for other complexes) despite an increase in the reasonable cost of production and distribution to about Rs. 12,400 per tonne (primarily due to a depreciation in the rupee). Together with selling price, that is, Rs. 8,300, the realisation of Rs. 11,800 fell short of the latter by about Rs. 600 per tonne.

The reasonable cost of production and distribution increased to about Rs. 13,300 per tonne in kharif 1998 and further to about Rs. 13,600 in rabi 1998-99. Against these, the selling price of Rs. 8,300 and a likely concession of Rs. 4,400 — common to both seasons — would leave a difference of Rs. 600 in kharif 1998 on a realisation of Rs. 12,700 and Rs. 900 in rabi 1998-99.

The possibility of substantial under-recovery under the RPS regime was ruled out as the relevant norms for compensation of various input costs such as the phosphoric acid/ammonia needed to produce a tonne of DAP, the basis for allowing conversion costs, and so on, were clearly laid down. This reduced the scope for subjectivity and arbitrariness and minimised the possible deviation of the expected subsidy rate from the number eventually notified.

In regard to payments as well, the system is seriously flawed. This is on the basis of sale duly certified by State governments unlike the RPS, wherein manufacturers were paid subsidy on despatch. Whereas, until 1993-94, the States

prone to delays. Besides, if the report on 20 per cent is delayed for too long, then, the 80 per cent on account payment may be affected too.

What, then, is the way out of the mess? Reverting to the RPS is one option. In fact, this system continues for urea. However, following the recommendation of the High Powered Fertilisers Pricing Policy Review Committee (HPC), which recommended dismantling the RPS, there is a question mark on its continuation even for urea.

The alternative is to give uniform subsidies at fixed rates and allow producers/importers the freedom of fixing the selling prices. This can take care of most of the problems. The suppliers will be able to assess their viability based on reasonable cost of supply *vis-a-vis* prices the market can bear and, accordingly, plan production/imports without delays. Farmers too will benefit from the competition among suppliers. Subsidy outflows can be restricted to pre-determined levels.

Such a dispensation was proposed under a new policy notified on August 28, 1998 for the October 1, 1998 to March 31, 2000 period. Unfortunately, this was reversed in three weeks, thus, restoring the *status quo*. It would appear that the pleasure of exercising controls far outweighs the overriding objective of promoting balanced fertiliser use and improving soil health.

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	Nitrogen	Phosphate	Potassic
1960-61	7.2	1.8	1
1970-71	6.5	2.0	1
1980-81	5.9	1.9	1
1990-91	6.0	2.4	1
1995-96	8.5	2.5	1
1996-97	10.0	2.9	1
1997-98*	8.0	2.9	1

* Estimated

Source: Economic Survey 1997-98

sonable production costs plus a post-tax return (on net worth) of 12 per cent. The excess of this over net back from sales were reimbursed as subsidy.

While on the one hand, by ensuring a reasonable return to producers, RPS contributed to the rapid growth of the industry, on the other, by maintaining a low and stable 'price to farmer', it facilitated rapid and sustained increases in consumption. This is amply demonstrated by the increase in the production of P from 0.84 million tonnes in 1980-81 to 2.56 million tonnes in 1991-92 and consump-