Editorial

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THE HINDU **BUSINESS LINE**

Urea glut

Importing trouble

Unrealistic demand projections coupled with unpredictable monsoons have rendered the business of tackling excess supply quite daunting. Mindless exports do not help things either, says Uttam Gupta.

ARE developments on the urea front creating a 'no-winner' situation, as it were? The current year began with an unprecedented quantum of urea stocks (28 lakh tonnes as on April 1, 1996, about 133 per cent more than the stocks as on April 1, 1995).

This is pregnant with the possibility of leading us into a glut situation which may result in cut-throat competition with major adverse effects on much more than the profit margins of manufacturers.

The situation has developed mainly because of the mismanagement of the supply-demand balance during 1995-96. To get an idea of where things went wrong a recap is in order.

The year started with an opening inventory of 12.5 lakh tonnes as on April 1, 1995. During the first half of the year — April-September (*kharif*) 1995 — the additional supply of urea was 90.7 lakh tonnes which included 75.4 lakh tonnes from domestic production and 15.3 through imports.

But consumption was only 88.2 lakh tonnes, leaving a surplus of 2.5 lakh tonnes out of the additional supplies. Together with the stock of 12.5 lakh tonnes at the beginning of the year, this led to a total inventory of 15 lakh tonnes as on October 1, 1995. The situation at this point of time caused little anxiety.

During October-March (*rabi*) 1995-96, however, we were gradually moving towards a situation of excess availability. During this period, domestic production was 82.6 lakh tonnes while imports were a record 22.6 lakh tonnes, giving a total additional availability of 105.2 lakh tonnes. But then consumption was only 92.5 lakh tonnes, leaving a surplus of 12.7 lakh tonnes.

Together with the stock of 15 lakh tonnes at the beginning of the season, this led to a pile-up of about of 28 lakh tonnes at the beginning of '96-97. Apart from being substantially higher than the stock as on April 1, 1995, this was far in excess of the quantity considered as safe cushion.

There is nothing unusual about the trend in urea consumption. During the whole of the year, it was 180.7 lakh tonnes (88.2 lakh for *kharif* and 92.5 lakh for *rabi*), an increase of 5.9 per cent over 1994-95. Domestic production was 158 lakh tonnes (75.4 lakh for *kharif* and 82.6 lakh for *rabi*) — about 5 lakh tonnes more than the targetted 153 lakh tonnes. This was unlike the earlier years when actual production was fairly close to the targets.

Undoubtedly, the excess production during 1995-96 has contributed to the overall glut situation, but the predominant factor has been excessive imports. During 1995-96, a record 37.8 lakh tonnes was imported, almost 10 lakh tonnes more than in 1994-95.

The imports would have been higher by another 2 lakh tonnes had the quantities under the controversial deal by NFL with the infamous Karsan, the Turkish firm, had actually been supplied in the second half of the year.

The quantum of imports is decided after assessing the likely shortfall in indigenous availability (opening inventory plus production) *vis-a-vis* projected consumption. During *rabi* 1995-96, while consumption (gross requirement) was projected at 107 lakh tonnes, the actual figure was only about 92.5 lakh tonnes. The excess supply was thus inevitable.

The Government has reportedly argued that the unsatisfactory progress of the North-East monsoon (this affects agricultural prospects and consequently fertiliser use in the southern and western regions) has hit actual consumption. However, this argument does not cut much ice, as agriculture even during the *rabi* season is largely dependent on the South-West monsoon and the extent of moisture retention/precipitation in the soil.

Notwithstanding this, however, and assuming that the North-East monsoon played a decisive role in influencing consumption, its full impact is known by the end of the December.

Thus, the Government could have regulated or, perhaps, even completely eliminated imports during January-March 1996. What happened instead was that about 12 lakh tonnes of imported urea moved into the country.

The point is, the projected demand of 107 lakh tonnes for *rabi* was itself inflated (it was about 17 per cent higher than the actual consumption for *rabi* 1994-95). This was unrealistically high if you go by the projections in the preceding years despite the monsoon conditions being no better during the current year.

A more realistic assessment of the demand on the one hand and regulation of imports in tune with the emerging situation during the course of the season on the other, could have helped prevent the situation.

And the country has been made to pay a heavy price for this. Taking 12 lakh tonnes as a fairly safe number of hedge against possible disruption in supplies, the resultant excess in stocks is about 16 lakh tonnes. This would entail an avoidable foreign exchange outgo of about $380 million (taking $240 per tonne as the C&F landed cost).

The rupee depreciation against the dollar since coincided with the period when the major chunk of the urea was imported. By avoiding import of the 16 lakh tonnes (representing the excess), the demand for dollars would have been lower by as much as $380 million. That indeed would have been a great help in preventing the rupee slide and erosion in forex reserves.

Under the existing controlled regime, urea imports also entail a subsidy outgo. This is equal to the difference between the C&F landed cost of imports, handling and distribution cost on the one hand and the lower controlled selling price on the other.

During 1995-96, on the basis of the prevailing average C&F cost of $240 per tonne, the former was about Rs. 9,500 per tonne as against the latter being Rs. 3,320 per tonne. This implied a subsidy of Rs. 6,200 per tonne on imported urea. Thus, the excess import must have resulted in an excess subsidy outgo of about Rs. 990 crores.

During 1995-96, the actual subsidy payment on imported urea was Rs. 1,935 crores. By avoiding excess imports, the subsidy outgo could have been restricted to just Rs. 950 crores. This, in turn, would have produced a sobering effect on the overall fiscal deficit situation.

Considering the controls on urea supply and distribution, ships carrying it must get priority in berthing and handling at ports. The situation on the railway front is also no different. Thanks also to the limitations of our ports, ships carrying decontrolled fertilisers had to wait for long periods, leading to heavy demurrage. In fact, some of these had to be diverted to neighbouring countries. Timely handling and distribution of imported raw materials too have been adversely affected, leading to reduced production, especially by the SSP units.

Regulation of the quantum of urea imports would have reduced pressure on the limited handling and distribution infrastructure and, to that extent, helped in accommodating other traffic, including for the decontrolled segment of the fertiliser industry.

Two imperatives emerge: Proper and realistic projection of demand, and effective supply management. During 1996-97, this will be of paramount importance not only to prevent worsening of the glut conditions, but also to conserve foreign exchange and keep subsidy outgo under check.

With an opening inventory of 28 lakh tonnes and likely production of about 75 lakh tonnes during April-September 1996 the total availability of urea from indigenous sources alone will be more than adequate to meet a likely demand of 94 lakh tonnes during *kharif* 1996 (this assumes a growth of about 7 per cent) and still leaves reasonable stocks at the beginning of *rabi* 1996-97.

This being the case, virtually no import of urea would be necessary during *kharif* 1996. Even during *rabi* 1996-97, the quantum of urea imports need to be regulated on the basis of realistic demand assessment and likely production.

The Government should also regulate release of stocks of imported urea in a manner that prevents any adverse effect on sales of the domestic output.

In other words, the residual role of imports needs to be maintained in line with the overall government policy. This is also necessary to prevent recurrence of the glut situation of the type witnessed in 1986-87 and 1987-88.

During that period, while the actual consumption was much short of the target because of unfavourable weather conditions and unrealistic demand projections, continued excessive imports led to a situation of glut. Simultaneous release of this material in the market, ignoring its residual role, led to an unprecedented discount war. Let history not be repeated as in such a situation, while both the industry and the exchequer lose heavily, there is no gain to the farmer either.

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