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Challenges for urea and QR-free regime

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CONSEQUENT to the recent ruling of Dispute Settlement Panel (DSP) of WTO, India will have to dismantle all quantitative restrictions (QRs) on imports by 2001. In case of urea, its imports will have to be decanalised and any one allowed to freely import. To assess the implications, let us take a quick look at the existing policy dispensation.

The selling price of urea is controlled at a low level unrelated to reasonable cost of production and distribution which is higher. The excess of latter over former is subsidised under unit-wise retention pricing scheme (RPS). The higher cost of imports (C&F landed cost plus handing and distribution) over selling price is also subsidised.

Under the present system thus, viability of domestic units is ensured subject to their operating at prescribed efficiency norms in regard to capacity utilisation and consumption of raw materials and utilities. Imports are also fully taken care of at actual cost. However, the quantum is restricted to the extent of shortfall in domestic production vis-a-vis demand.

After removal of QRs, imports will no longer be on residual basis; instead, these will be at par with domestic supplies. Freeing imports has no meaning if controls on price and distribution are retained. Therefore, these will have to go. Along with this, RPS too will have to be dismantled.

Consequent to above, producers will be free to sell at market determined price which will be higher than existing artificially low selling price of Rs 4,000 per tonne. It will settle somewhere in between prevailing cost of imports and weighted average cost of domestic units. At current levels ie, Rs 5,000 per tonne for former and about Rs 8,500 per tonne for latter, this would be Rs 6,500 per tonne.

The above being a steep about 62 per cent higher than current level, consumption will decline drastically in turn, leading to substantial reduction in foodgrains production. Within the industry, production cost of a number of units being more than this price, they will be wiped out leading to substantial loss of domestic output.

The reduction in domestic production is most likely to be higher than reduction in demand. This will lead to substantial imports even to meet reduced demand. This is bound to push up international price. This indeed, has been the experience whenever, imports were increased in the past viz, 1995-96, 1996-97.

In post-QR removal scenario thus, the Government will have to put in place adequate safeguards to protect domestic industry. For if, it does not, we are bound to be exploited perpetually in international market. Then, how do we go about?

Ideally, this could be achieved by giving concession support to indigenous industry at a higher rate than on imported urea. This approach also has the advantage of ensuring low price to farmers.

The above could, however, be construed as an unfair and discriminatory treatment of imports and therefore, violative of underlying spirit of WTA (1994). As an alternative, the Government may put a duty on imports, rate of duty to be determined on the basis of differential between weighted average cost of domestic units and cost of imports.

Considering the possibility of import price going as low as it is now, the bound rate may be declared at fairly high level say, 100 per cent (even developed countries maintain very high rates eg, 300 per cent on sugar by Europeans). Within this ceiling, the rate may vary depending on the prevailing cost and price situation.

Despite duty, several plants ie, those having production cost higher than weighted average will face serious threat. Despite high efficiency (read physical), they produce at high cost primarily due to high cost of feedstock; for instance, cost of naphtha is more than double that of gas. Urgent steps are needed to bring about uniformity in price of various feedstock and lower these to internationally comparable levels.

Likewise, assistance by way of one time capital subsidy will have to be given to newly commissioned plants to enable them overcome burden of servicing investment. Similar dispensation will be needed to attract capital for setting up new projects. Removal/reduction in various taxes and duties, lowering of interest rates etc. will also contribute to keeping cost low.

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