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Fertiliser subsidy

Time for decontrol has not come

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> There are a few clearcut messages. First, the government must immediately put an end to dual pricing. If allowed to continue, it will only mean increase in fertiliser subsidy bill for 'unproductive' and perhaps even 'unethical' use. Second, existing target-oriented programmes/schemes used to be adjusted to reach out help to small and marginal farmers. Third, administered prices of inputs to the fertiliser industry should be frozen at their existing levels.

When the finance minister presented his budgetary proposals on fertilisers, his objective was primarily to reduce subsidy. And, this was because the IMF wanted the G.O.I. to reduce fiscal deficit to the magic figure of 6.5 per cent of the GDP. By how much the fertiliser subsidy should be reduced to ensure this achievement is, perhaps, best known either to the B/F itself or to the key officials in the Government who have been negotiating the package. Whatever that may be, one thing is quite clear. Even those who were quite optimistic about achieving a breakthrough on this front, appear to have reconciled themselves to the "ground realities" which in any case were not reflected while formulating the proposals.

When the Budget was presented to the Parliament on July 24, 1991, the Rs 4000 crore allocation (Rs 2900 crore domestic and Rs 1100 crore on imported) for fertiliser subsidy looked quite impressive. It was Rs. 400 crore less than last year. Indeed, a good signal to the IMF that we were proceeding in the direction it wanted us to move. What happened in a short span of less than three weeks thereafter both in the Parliament and outside, made it clear to our managers of the Budget that the task was not that easy.

Subsidy allocation for domestic fertilisers had to be increased by Rs 450 crore and a separate provision of Rs 405 crore made to exempt the small and marginal farmers from the 30 per cent increase in the price that was to replace the original proposal of 40 per cent hike across the board. Though the latter may be appearing under a separate head, the fact cannot be denied that this is in all legitimacy a part and parcel of the fertiliser subsidy.

Well then, on this basis the budgetary allocation for fertiliser subsidy increases to Rs 4855 crore. Some may still feel complacent because this figure apparently is only marginally higher than what was paid last year. But, let us not allow ourselves to be deterred by this and face what is happening. In an editorial which appeared in this daily some time back, reference was made to a "hole" in finance minister's pocket of about Rs 1200 crore because of the need to exempt small and marginal farmers from the 30 per cent price increase. This may look a bit exaggerated. Nevertheless, the underlying trends do point towards the allocation being substantially short of the likely requirements.

Only recently the chief minister of Uttar Pradesh made a statement that about 90 per cent of cultivating households in his state are small and marginal farmers. This is against a national average of 75 per cent. No surprisingly, a number of other states have also claimed that they have preponderance of small and marginal farmers and some have even announced their decision as in the case of Haryana, to sell the entire quantity of fertilisers at the pre-25th July prices.

The allocation of Rs 405 crore was based on the implicit assumption that consumption by small and marginal farmers is 30 per cent of the total as per the results of the NCAER survey. Because of the 30 per cent increase in the consumer price, the finance minister estimated a saving of Rs 1350 crore on the total consumption of fertilisers during 1991-92. And, 30 per cent of this (1350 x 0.3) gives Rs 405 crore. The figure of 30 per cent is indeed a crucial factor. On the face of it, there is no baisis to question its authenticity. However, given the dynamics of our political economy which is showing up prominently in the rural belt, it is quite plausible that are likely actual could be much more.

This can happen in two ways. First, as per the results of the NCEAR Survey, about 45 per cent of the small and 37 per cent of marginal farmers are not using fertilisers. When presented with the opportunity of fertilisers being available at subsidised price, many of them are likely to join the ranks of those using fertilisers. However, their primary interest will be in "trading" rather than actually using fertiliser on their

of large size holdings to enable access to subsidised fertilisers even by better off farmers. The fact that such a scenario is already taking shape is clearly reflected in the demand by many state governments for a significant increase in their respective allocations.

Even assuming that about Rs 1000 crore are needed to take care of the small and marginal farmers, the likely expenditure on fertiliser subsidy during the current year will be about Rs 5455 crore. To this, must also be added the under-provision of about Rs 800 to Rs 1000 crore towards the subsidy on indigenous fertilisers. The budgetary provision towards this does not take into account the impact of various cost push factors such as the Gulf surcharge introduced in October, 1990, increase in railway freight and devaluation etc. How many of us know or even care to know that devaluation of the Rupee alone will increase total fertiliser subsidy by about Rs 900 crore (including Rs 450 crore on domestic). And, this constitutes nearly 2 thirds of the total saving in subsidy the finance minister has sought to achieve through increase in the consumer price of fertilisers.

All said and done, at the end of the year we would have landed up with a whopping fertiliser subsidy bill of about Rs 6500 crore. The million dollar question we need to address is whether with this result, we would have met one of the important conditions laid down by the IMF for India to qualify for the major loan under the stand by facility. One may say that notwithstanding the numbers, we are still moving in the "right" direction. We are moving progressively towards a regime of total de-control and that would automatically mean elimination of fertiliser subsidy. Are we? To seek an answer, let us take a look at the other angle to the finance minister's proposals.

Though not clear in so many words, it was certainly reflected in the government's decision to de-control some of the fertiliser types i.e. AS, Acl and CAN. In respect of SSP, while prescribing a ceiling on subsidy a move towards ultimate de-control was hinted. These fertilisers touch only a small segment of the industry. The three fertilisers which have been de-controlled account for only 3 1/2 per cent of the 'N' production in the country. SSP (where intention to this effect has been expressed,) contribute only 18 per cent of the total P_2O_5 application. Major fertilisers i.e. urea and complex/ P contributings 80 per cent and 84 per cent of the N and P supplies respectively have been left untouched. Perhaps, the government seems to be totally unprepared to de-control fertilisers which may not be to the liking of the IMF.

Whether or not the Government will undertake this extreme step? This is a question which will perhaps be answered by the events in the near future. But, a more important question is, IMF or no IMF, whether this may be considered a desirable option? Apart from the much trumpeted argument that this will help in reducing the fiscal deficit, we are being told that a number of other developing countries such as Pakistan, Bangladesh, Sri Lanka and Indonesia have already de-controlled the nitrogenous segment of the fertiliser

suit? Our government has clearly preferred to wait as it is certainly not unaware of the likely risks/dangers that may be in the offing as a result of the complete de-control of fertilises.

Could we care to take a close look at what could possibly in the offing? In the event of de-control, the "minimum" price of a tone of urea to the farmer will have to be about Rs 4000 per tonne. The farmer who is already burdened with a hefty increase of Rs 700 per tonne will certainly not be able to pay at that rate. That would mean a major chunk of the urea producing units in the country will have to close down. This holds for other fertiliser material as well. Already, we are short of fertilisers. During the current year i.e. 1991-92, we would have landed up spending about Rs 6000 crore on fertilisers imports. And, most of it having to be financed from the loan from the IMF and other international/bilateral assistance. Imagine the situation of these were not to be had. And, on top of all that if the existing units become unviable, how shall we cope up with the consequential loss of production and that too in a global market which is increasingly becoming tight.

Those with a somewhat orthodox view might still welcome these developments on the plea that units closing down must be inefficient. We need to be a little careful here. The Rs 4000 per tonne figure referred to above is the weighted average cost of making urea available at the farmgate. The reasonable cost of production subsumed in this is not the actual but, in fact, based on retention prices allowed to individual units on the basis of "efficiency norms". Likewise, the freight and distribution margin which make up for the distribution cost, are also taken at normative level as prescribed by the government. Consequently, when we talk of a unit becoming unviable in a de-control situation, it is not due to the inefficiency factor but, because of the higher cost vis-a-vis what the farmer can pay. The former is primarily caused by steep increase in prices of inputs, utilities and services supplied to it, impact of taxes and duties besides bulk of increase in production during 80s coming from newly commissioned plants entailing higher capital cost.

Quite often, the text-book assumption is invoked that free market can help in lowering costs. Yes, provided we have it in the entire economy. We can't reduce fertiliser production cost so long as the prices of naphtha, fuel oil, gas, coal and power etc., continue to be administered which can certainly not be treated as pricing based on free market. We also tend to remain under the impression that there is something like free market in the context of world trade in fertilisers. Some even suggest that the prices of our produce should be linked to that. But, how many of us know that the things are quite different in practice. Or else, the farmgate cost of urea that we are importing from Soviet Union would not have been as high as Rs 5200 per tonne. The cost to the farmer of urea bought against free foreign exchange at the current world market prices will be Rs 5600 per tonne (Table). In sharp contrast, the cost of indigenous urea is only about Rs 4100 per

some of us may still continue to believe that importing fertilisers is a cheaper option.

So by making our industry unviable, what are we going to achieve? Are we prepared to pay a price for imports which will be substantially higher than the cost of our own material? And above all, how shall we afford it? Perhaps, these are questions which must be agitating the minds of our planners and policy-makers. In the context of the Aid India Consortium meeting, the World Bank has held that the donors should take a very "liberal" view of the need for assistance to India during its present phase of adjustment. While the massive dose of assistance, both in the pipeline as well as being contemplated, may take care of our needs for fertiliser imports in the short run, in the medium to long-run, we need to fend for ourselves.

A sudden move towards de-control is certainly not a step in the right direction. Given our present high cost structure, on the one hand, and the price currently being paid by the farmer which even after the 30 per cent increase is low in comparison, introduction of free market can mean serious problems unless either (a) the farmer is geared to pay a price at which the industry can be viable or (b) the cost to the latter is reduced substantially. Let us see which of the two is plausible.

Already, there has been a strong resistance to the 30 per cent increase. The government was in fact, forced to consider exempting the small and marginal farmers straightaway. To take care of those producing marketable surplus, the procurement price have been raised. To expect that, a further increase of at least Rs 1000 per tonne that would follow de-control, will be acceptable to the farmers, is a near-impossibility.

In regard to the allowable cost of production under the Retention Pricing Scheme, efforts were made in recent years through tightening of the pricing norms. Various steps taken have pushed this industry in to a situation of heavy loss-making. And yet, no dent was made on subsidy. Clearly, our diagnosis of increasing fertiliser subsidy was not correct. A very vital factor responsible for high cost of domestic fertilisers has not been addressed. Unfortunately, while we bemoan high cost, various administrative actions have only aggravated this phenomenon. Be it the Gulf surcharge, increase in railway freight, devaluation, or the contemplated increase in gas price etc., the list appears to be unending.

Before we think of drastic steps like introduction of dual pricing or total decontrol of fertilisrs which can mean food insecurity, why not initiate sincere action on these fronts. This can help us a lot. For instance, removal of customs duty on phosphoric acid imports will give us a saving of about Rs 212 crore. Reduction in gas pricing by Rs 100 per 1000 cubic metre can yield about Rs 55 crore savings. Elimination of customs duty on fertiliser project imports can substantially lower the cost of projects currently under implementation. While we do this, let us try and increase consumer price only in steps, shedding thereby the practice of no increase for years together followed by hefty hike at one go which may not be acceptable politically or perhaps, even psychologically.

There are a few clear-cut messages for us. First, the government must immediately put an end to dual pricing. If allowed to continue, it will only mean increase in fertiliser subsidy bill for "unproductive" and perhaps even "unethical" use. Second, existing target Oriented programmes/ schemes need to be re-oriented to reach out help to small and marginal farmers for getting better results from use of fertiliser bought at higher price. Third, administered prices of inputs to the fertiliser industry should be frozen at their existing levels. Reduction to put them at par with levels obtaining internationally could be still better. Fourth, increase consumer price in bits, say, 10 per cent every alternate year. If only we can follow it up for a period of say, 5 years, not only will that help in reducing fertiliser subsidy, but also, enable smooth