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Time to act on the urea crisis

The government should state clearly whether it intends to decontrol urea and, if so, when. Ideally, it should allow for a transition period of a minimum five years, during which the retention pricing scheme should be continued, says Uttam Gupta.

A disquieting feature of the fertiliser scenario has been the steep increase in the subsidy on imported urea. During 1994-95, as against a budget provision of Rs 500 crore, the actual turned out to be Rs 1,166 crore. Almost the entire increase of Rs 666 crore was due to the higher landed cost of imported urea.

A close scrutiny of India's imports would reveal that, of the total 3 million tonnes, about 2.2 million tonnes were imported during the second half of 1994-95, when the international urea prices had accelerated substantially. Had these imports been made in the first half of the year, we could have saved heavily on the cost and the subsidy outgo.

The budget provision for subsidy on imported urea during 1995-96 is Rs 1,650 crore, which is Rs 500 crore more than the revised budget estimates for 1994-95. For imports even at the 1994-95 level, these will have to be paid at a still higher rate. The assumption of domestic production at about 15 million tonnes is much too ambitious in view of uncertainties in the supply of various hydrocarbon feedstock.

Increasing dependence on imports and associated heavy cost is indeed painful, considering the fact that not long ago (in 1990-91), we were totally self-sufficient in urea.

Clearly, we have not added to the production capacity at the pace we should have done. It is not as if the growth in demand was not known. The Eighth Plan Working Group on fertilisers had, in its report, made projections of nitrogen demand upto 2000. And yet, no fresh projects have been taken up for implementation. The last few years have seen commissioning of three major plants i.e Nagarjuna Fertilisers and Chemicals at Kakinada (1992), Chambal Fertilisers and Chemicals, Kota (1993) and Tata Chemicals at Babrala (1994). However, these were all conceived and planned in the early 80s. Bindal Agro's plant at Shahjahanpur, expected to be commissioned by the third quarter of 1995, also falls in the same category.

Even the existing production capacity in the country is not being fully utilised. In 1991-92, the overall capacity utilisation was 89 per cent. Barring the sick plants of the FCI and the HFC, the utilisation rate for all others was averaging about 98 per cent. All gas-based units were doing well above 100 per cent. During 1993-94, the all India utilisation came down to 83 per cent and even for the gas-based units there was a perceptible decline, as the petroleum ministry has decided in principle not to give gas for captive power and steam generation facilities.

The third factor is the continued uncertain policy environment for urea. In August 1994, while approving the major parameters of the retention pricing policy, the Union cabinet sought the opinion of the law ministry on the question of imposing a ceiling on capacity utilisation beyond which capital-related charges to the units will be disallowed. But the government is yet to make up its mind on the issue.

At the prevailing c&f landed cost, the farmgate cost of imported urea works out to about Rs 8,800 per tonne against a cost of Rs 5,500 per tonne for domestic urea on a weighted average basis for the industry. On imports, thus, the government has to pay a higher subsidy of about Rs 3,300 per tonne. It makes sense to encouraging domestic production from existing plants and maintain the necessary incentives.

Even the broader question of whether to continue with the Retention Pricing Policy (RPS) is not free from confusion and uncertainties. Press reports give an impression that the RPS may eventually be phased out. And, even assuming that this happens in a time span of 3-4 years hence, the government must take a decision now. An investor contemplating to initiate work on a project now, should know what would be the policy environment at the time when his project is ready to go in for commercial production. The point is equally relevant to existing units where the managements will have to take appropriate decisions with regard to their expansion.

Contemplated deregulation of the oil and gas sector has further added to the uncertainties. All naphtha and fuel oil-based plants are getting worried whether, in a decontrolled regime, they would continue to get the required supplies at the existing prices which are concessional. So long as the RPS continues, any increase in price charged by oil companies will be absorbed by a corresponding increase in the subsidy amount. However, as and when the RPS and concomitantly the subsidy support is abolished, such increases will eventually make all these plants unviable.

The need for protecting the existing urea plants and ensuring maximum utilisation of their installed capacity cannot be overemphasised. Barring the sick units of the FCI and the HFC, these plants are amongst the best in the world. They are only being squeezed between the high cost of feedstock and other inputs on the one hand and farmers on the other, who are not being allowed to pay a reasonable price for reasons best known to the political establishment. Presently, the cost of production and distribution is higher than the selling price by about 65-70 per cent and is bound to increase further if no corrective actions are initiated.

The government should adopt a reasonable approach on these two fundamental issues. Allowing the oil and gas companies to get away with substantial increase in prices of feedstock and preventing farmers from paying even the bare minimum cost escalations, will be suicidal for all urea manufacturing units.

A categorical announcement of the urea policy brooks no further delay. As part of it, the government should state clearly whether it intends to decontrol urea and if so, when? Ideally, it should allow for a transition period of a minimum five years during which the RPS should be continued.

During the transition, the selling price to the farmers should be raised gradually every year in small doses of 15-20 per cent. At the same time, the government should undertake to maintain the administered prices of various hydrocarbon feedstock at reasonable prices should be avoided at any cost as that could be disastrous and ensure full supply of the fertiliser industry requirements.

That seems to be the only way to protect the industry, huge investments made in it and the employment. That is also the only way to induce fresh investment on the desired scale to bridge the projected demand-supply gap.