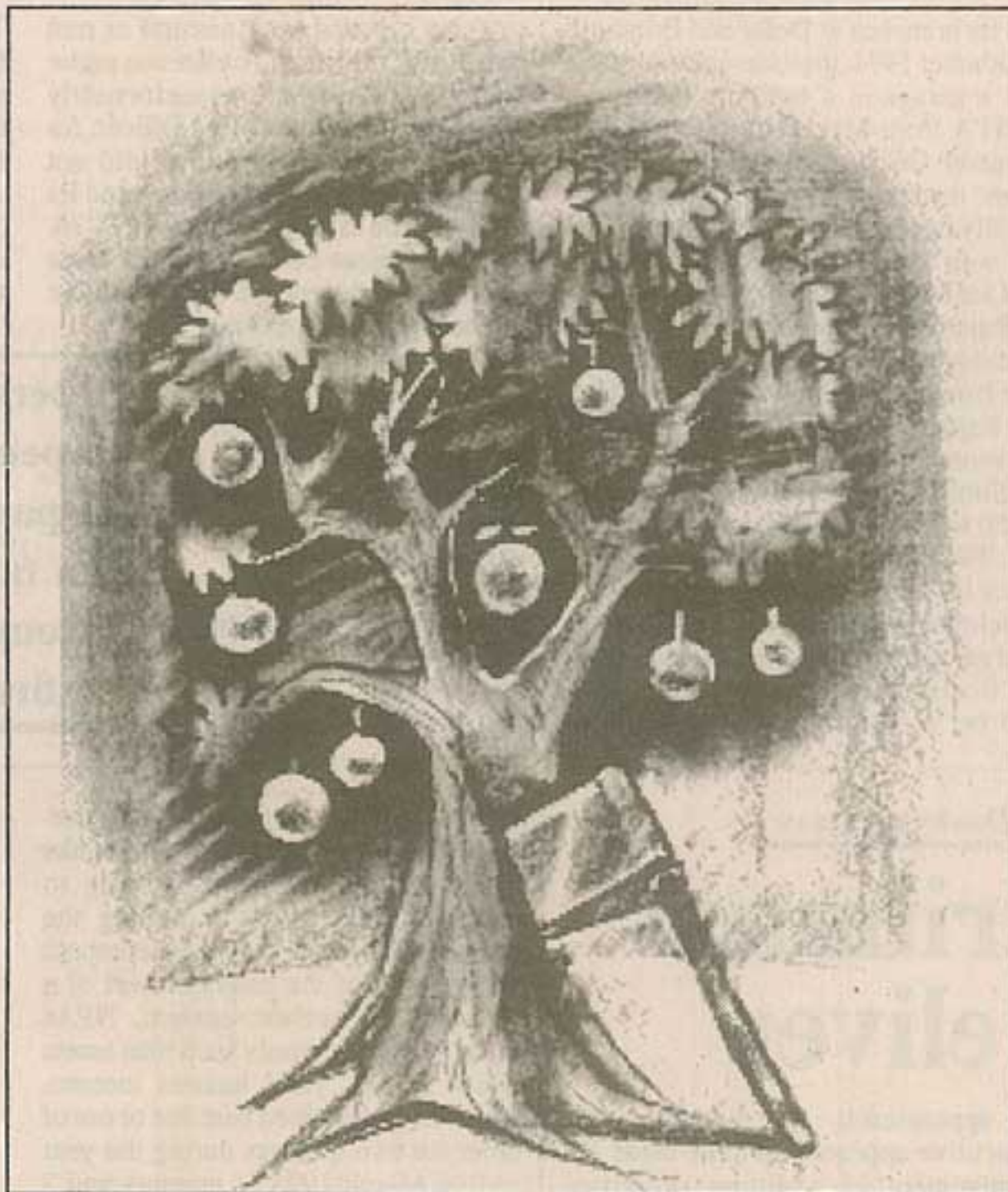


Ugly face of reforms

Govt reforms should help streamline industries, not kill the efficient ones, says Dr Uttam Gupta



under the erstwhile dual exchange rate regime.

With full convertibility of the rupee w.e.f. 1.3.1993, the latter was no longer available. Consequently, compared to August 1992 when the reasonable farm-gate cost (production and distribution) was higher by at least Rs 4,500 per tonne DAP, the only significant relief is by way of customs duty which would translate to about Rs 800 per tonne. In other words, the farmer would still have to pay about Rs 2,700 more than he was paying at the time of decontrol. The net result is that despite all the bravado of helping the farmers, both within Parliament and outside, consumption has declined and so has been the case with production.

It goes without saying that majority of the companies have taken a serious beating, which is totally contrary to the objectives of reform. Whereas the industry's pathetic situation has been in the limelight, there are two companies

that have fallen by the wayside crying desperately for intensive care. These are Deepak Fertilisers and Petrochemicals Ammonium-Nitrophosphate (23-23-0) plant at Taloja in Maharashtra and GNFC-Bharuch also 23-23-0 with Calcium Ammonium Nitrate (CAN), a straight nitrogenous fertiliser as a co-product. While the latter was commissioned in April 1991, the former started commercial production in July 1992 i.e. barely one month before decontrol. Their problem is that just when they were about to start receiving the benefit of the RPS for servicing the investment, the scheme was withdrawn. Although GNFC's production remained under RPS for about one-and-a-half-years (April 1991 to August 1992), it could recuperate only a part of its capital related charges.

Consequently, the entire interest and depreciation in the case of Deepak and an overwhelming share of GNFC still

remained unabsorbed.

Presently, urea is under control and is covered by the RP and subsidy scheme. The controlled selling price of urea even after the 20 per cent hike is only Rs 3,320 per tonne.

As against this, the retention price, which is expected to cover the reasonable cost of production and a margin of profit (currently at 12 per cent post tax return on networth), is about Rs 8,500 per tonne for Nagarjuna Fertilisers and about Rs 6,500 for Chambal Fertilisers. These are recently commissioned projects i.e. August 1992 and October 1993 respectively. Now, if the Government takes a sudden decision to decontrol urea and abolish the RP and subsidy scheme which will practically kill both these projects, can we argue that these with an unprecedented investment aggregating to over Rs 2,000 crores should be allowed to die down or should not have been set-up at all?

The approach to solving the problem of these two plants has to be two-fold. First, there is no escape from raising the selling price of urea to bring it to a more realistic level. Presently, it is artificially suppressed and very much out of line even with the cost of production and distribution which on a weighted average basis would not be less than Rs 5,000 per tonne. The latter is without the revision under sixth pricing and would increase further with that.

It should not be forgotten that nitrogen, phosphate and potash are all essential plant nutrients and the pricing policy with regard to them has to be well-coordinated to avoid distortions. Consequently, if the Government recognises that P and K prices need to be market-based, there is no logic in leaving nitrogen out. Although, sudden decontrol of the latter may be catastrophic; the least that could be done is to raise the controlled selling price of urea in small doses.

Second, although there is Rs 1,000 per tonne ad hoc subsidy on DAP, it is not clear as to whether it is entirely to make up for the higher cost of the phosphate content or it includes some subsidy on the nitrogen element also. This has to be clearly spelt out and besides the subsidy on the phosphatic content, some subsidy on the nitrogen element has also to be built-in.

Third, there is an urgent need to give a one-time capital subsidy to Deepak Fertilisers and GNFC to off-set their high capital cost disadvantage vis-a-vis the other phosphatic plants commissioned in the 80s.

While implementing these supporting decisions, the Government should be guided by the overriding consideration of ensuring continued health, efficiency and growth of the well-run companies.

If, however, because of overall macroeconomic considerations it wishes to change the policy, the ideal approach would be to give the industry advance notice and provide them adequate time to face the formidable challenge of decontrol.

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SIMPLY stated, the objective of any reform exercise has to be to make our industries do better and not kill them. Of course, there can be no sympathy with a company which is inefficient and is a drain on the national exchequer. Indeed, this is true of a large number of enterprises which are sick for several years but are languishing between life and death for want of timely action aimed either at rehabilitating them or formally pronouncing them dead.

But to kill a unit which is efficient, employs the state of art technology and is run by a good management is totally unacceptable. In fact, that would be tantamount to demeaning the very philosophy behind the reform exercise. Sudden decontrol of the phosphatic fertiliser industry two years back in August, 1992 has led precisely to this kind of situation. During 1991-92 (the financial year just before decontrol) the all-India capacity utilisation for the entire phosphatic industry, was 94 per cent as all the 10 AP manufacturers in the country were operating at a minimum of 100 per cent. During 1992-93, this declined to about 80 per cent and in 1993-94, when the full impact of decontrol was felt, it was just about 60 per cent.

It was not as if the plants suddenly became inefficient. Their capacity utilisation dipped because the demand plummeted consequent to decontrol, causing a steep increase in selling prices to the farmers. The latter was inevitable as the controlled selling price of phosphatic fertilisers was kept artificially low. In fact, for one decade i.e. July 1981 to July 24, 1991, these remained more or less unchanged. Even after the 1991 increase, the DAP selling price was only 30 per cent more than it was in 1981.

During this long period, the cost of purchased inputs, including imported raw material/intermediates kept increasing. Depreciation of the rupee from Rs 8.97 way back in 1981 to Rs 31.7 now alone pushed up the cost of production to exorbitant levels. All along, the difference was being met through subsidy from the Government. In fact, at the time of decontrol, the subsidy amount per tonne DAP was almost equal to the selling price which was Rs 4,680 per tonne.

When you keep the selling prices artificially suppressed for several years and then suddenly ask the farmers to pay 100 per cent more, there is bound to be resistance. And, when there is substantially reduced offtake, production will inevitably go down; companies will suffer substantial financial loss.

The plethora of measures such as removal of customs duty on imported phosphoric acid, reduction in the railway freight and ad hoc subsidy etc. that were announced after decontrol, failed to measure up to the challenge thrown up by the suddenness of the decision. From the Government's angle, the two important reliefs were the removal of customs duty on phos acid imports and the benefit of lower official rate of exchange on import of raw materials