FERTILISER PRICING—RECONCILIATION OF DIVERSE INTERESTS

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Pricing of fertilisers has an impact on foodgrains output, their prices and consequently on the general price stability and the overall growth of an economy which is still agrarian in character. Prices of fertilisers also have disributional implications and a bearing on the national budget and foreign exchange position. Moreover, fertiliser prices tend to be sticky as they have aquired political overtones because low prices of agricultural inputs are regarded as an important instrument of keeping a large chunk of rural voters satisfied. The twin considerations of encouraging the growth of agriculture through price incentive for greater use of fertilisers and providing sufficient incentive for investment in fertiliser industry require that fertilisers are supplied to the farmers at low prices, and simultaneously the industry is also paid a remunerative price based on cost plus pricing. This has been achieved through a system of retention prices involving heavy subsidisation, a system which has paid rich dividends both in terms of desired increase in agricultural production and significant expansion of capacities in fertiliser industry.

Low Input-Output Price Mix

In view of a low capacity of the Indian farmers to pay for agricultural inputs and also the general poverty of the Indian population making it difficult to pay high price for foodgrains, the government consciously favoured the low input-output price mix as the only way of simultaneously subserving the interest of the farming community as well as the majority of the poor consumers. This led to the policy of supplying power, irrigation, seeds, farm credit and fertilisers etc. to the farmers at low prices which at times did not cover even the variable costs on such supplies. Through administrative arrangements the prices of fertilisers to the farmers, which are notified by the Government from time to time, are kept uniform throughout the country subject only to local taxes enforceable by the concerned state governments and union territories. And to make the price control effective adequate supplies of fertilisers are ensured to farmers in all parts of the country through the operation of a system of distributional control under the Essential Commodities Act (ECA) wherein the manufacturers and the handling agents (in respect of imported fertilisers) are direced to sell the specified quantities of fertilisers in specified states and union territories. The logistics of fertiliser distribution including transportation (freight equalisation and freight subsidies), packaging, handling and storage etc., is also appropriately regulated to conform to the overall supply and demand position so as to strengthen the impact of the price policy regarding the farm produce and the farm inputs.

Low input-output price mix for agriculture is evident from the behaviour of the movement of prices of urea, agricultural produce and the prices in general. Table-1 clearly reveals that the Price Index of Agricultural Produce has consistently remained below the Wholesale Price Index of All Commodities. The increase in the fertiliser prices has been negligent compared to the increase in the prices of agricultural produce. The Price Index of

Agricultural Produce (Base 1970-71) moved from 169.9 in 1974-75 to 469.0 till 1990-91 i.e. 294 per cent price rise during this period of 17 years. On the other hand the price of urea (quantitatively the most important fertiliser) declined from Rs. 2000 per ton in 1974-75 to Rs. 1450 in 1979-80 to rise again to only Rs. 2350 per ton by 1990-91, an increase of only 175 per cent over the prices prevailing in 1974-75. Thus in real terms, vis-a-vis agricultural produce, the prices of fertilisers have got reduced to 42.6 per cent between 1974-75 and 1990-91. The story has been same in case of two other fertilisers i.e. DAP and MOP. The result of this pricing pattern has been that compared to 1974-75 when 4.14 kg. of wheat or 5.88 kg. of paddy could buy 1 kg. of Nitrogenous fertiliser, in 1986-87 only 3.08 kg. of wheat or 3.50 kg. of paddy was required to buy the same quantity of N.

Prices of Fertilisers vis-a-vis Prices of Agricultural Products

Year	Maximum Sale Price of Urea (Rs./Ton)	Wholesale Price Index of All Commodities (1970-71=100)	Price Index of Agricultural Produce (1970-71 = 100)	Percentage change over 1974-75 Prices		Change in Urea Price as a Percentage to the prices of Agricultural Produce with 1974-75 as base
				Agricultural Produce	Urea	
1974-75	2000	174.9	169.9	100.0	100.0	100.0
1975-76	1850	173.0	157.3	92.6	92.5	99.9
1978-79	1550	185.8	171.9	101.2	77.5	76.6
1979-80	1450	217.6	188.7	111.1	72.5	65.3
1980-81	2000	256.2	210.5	123.9	100.0	80.7
1981-82	2350	281.3	236.5	139.2	117.5	84.4
1982-83	2350	288.7	247.9	145.9	117.5	80.5
1983-84	2150	316.0	282.7	166.4	107.5	64.6
1984-85	2150	338.4	303.2	178.5	107.5	60.2
1985-86	2150	357.8	309.6	182.2	107.5	59.0
1986-87	2350	376.8	330.1	194.3	117.5	60.5
1987-88	2174	405.4	372.3	219.1	108.7	49.6
1988-89	2174	435.3	400.7	235.9	108.7	46.1
1989-90	2174	466.1	412.5	242.8	108.7	44.8
1990-91	2350	513.9	469.0	276.0	117.5	42.6

Note :- Fertiliser price came down from Rs. 2350 to Rs. 2174 due to $7\frac{1}{2}$% discount announced by the Government to push up the fertiliser demand depressed due to drought conditions.

Movement of Fertiliser Prices

With a view to ensuring adequate domestic supplies of fertilisers for sustaining proper distribution and adequate consumption of fertilisers, the government adopted a scheme of retention prices for encouraging creation of adequate indigenous fertiliser capacities and their efficient utilisation. Retention Price System (RPS), which has been in operation since Ist April, 1976, has served the industry well in terms of increased investment, greater capacity utilisation and higher production resulting in lower imports despite rapid increase in consumption.[1] The improved per hectare consumption and higher total production resulted from low prices to farmers on the one hand and higher retention prices to manufacturers on the other. Despite higher retention prices to the producers of fertilisers to compensate them for cost

hikes, the prices to farmers have remained relatively stable. This is clear from the movement of urea prices given in Table 2.

Movement of Urea Prices

Year	Date from which the price became effective	Per meteric ton price of urea (Rs./MT)	
1970-71		943	
1971-72	9.3.71	923	
1972-73	30.3.72	959	
1973-74	1.10.73	1050	
1974-75	1.6.74	2000	
1975-76	18.7.75	1850	
1976-77	16.3.76	1750	
1977-78	8.2.77	1650	
1978-79	12.10.77	1550	
1979-80	10.3.79	1450	
1980-81	8.6.80	2000	
1981-82	11.7.81	2350	
1982-83	11.7.81	2350	
1983-84	29.6.83	2150	
1984-85	29.6.83	2150	
1985-86	29.6.83	2150	
1986-87	31.1.86	2350	Less $7\frac{1}{2}$% Discount
1987-88	31.1.86	2350	Less $7\frac{1}{2}$% Discount
1988-89	31.1.86	2350	Less $7\frac{1}{2}$% Discount
1989-90	31.1.86	2350	
1990-91	31.1.86	2350	
1991-92	25.7.91	3300	
1991-92	14.8.91	3060	(for other than small farmers)
	14.8.91	2350	(for small and marginal farmers)

Price Control and Retention Prices—A historical perspective

There was no control on the prices and distribution of fertilisers till 1944. As stated earlier a partial control over fertilisers was initiated in 1944 through Central Fertiliser Pool (CFP) established for procuring and distributing fertilisers on a no-profit-no-loss basis. Formal price control on fertilisers commenced when 'Fertiliser (Control) Order 1957' was issued with the twin objectives of regulating distribution and making fertilisers available at fair prices. Under the Order maximum retail prices for different types of fertilisers could be fixed. The control price for each type varied from area to area and for different classes of consumers depending on local conditions.[2] Thus a system of discriminating controlled price was adopted, which continued up to September 1966. The prices of all straight, nitrogenous fertilisers including urea, ammonium sulphate and CAN have all along been subject to control since mid-sixties. Phosphatic fertilisers such as DAP and other

complex fertilisers were brought within the purview of price control in February 1979 and Single Superphosphate (SSP) in may 1982.

The appointment of Sivaraman Committee and acceptance of its report, which coincided with the green revolution, gave a solid base for the growth of fertiliser industry in India. The green revolution was based on intensive agriculture involving the use of high yielding varieties of seeds, adequate water and adoption of scientific package of practices requiring higher per hectare consumption of fertilisers so that growth of fertiliser availability and the success of revolution in agriculture became synonymous. With a view to providing inducement to more intensive use of fertilisers and encouraging their production, the Government reviewed the fertiliser price policy in October 1970. The control price announced for four nitrogenous fertilisers took care of the cost of producting individual fertiliser plants and the capacity of the cultivator to bear the price burden. Under the scheme there was a common controlled price for each type of fertiliser whether indigenously produced or imported though the retention prices to different plants in public and private sectors varied, depending on their cost differenial. The prices paid for all types of fertilisers went to the Common Fertiliser Pool,[3] out of which different retention prices were paid to individual manufacturers and for imports.

The need for varying retention prices to different producers arises not only due to variations in their capital servicing charge or the level of efficiency but also because of various types of feedstocks which different units are obliged to use. The feedstock has an important impact on both capital and operating costs of different plants. For example, in case of nitrogenous fertilisers, the total cost of production is lowest for plants based on natural gas or naphtha, considerably higher for fuel oil based plants and highest for coal based plants. The feedstock is assigned by the Government on the basis of location of the plant and availability of feedstock and without any option to an individual fertiliser plant. Thus at the time of inception itself, different plants are programmed to have widely divergent costs of production, for reasons not internal to the plants or to the efficiency of their operations. No wonder the individual retention prices of different factories producing urea vary substantially.[4]

Though retention prices granted to individual fertiliser plants took care of their costs of producion and return on invested capital, even then public sector fertiliser plants incurred losses due to actual costs exceeding normative costs. Per unit fixed as well as variable costs were high on account of under-utilisation and increases in the prices of raw materials, so much so that there were cases when total sales realisation was more or less equal to the total variable cost alone.[5]

The statutorily fixed prices remained unchanged between 1969 to May 1974. Prices of imported fertilisers skyrocketed after the oil price hike of 1973. The cost of indigenous production increased due to higher import prices for oil and naphatha. This led to the introduction of Fertiliser Pool Equalisation Charge (FPEC) in 1974. The indigenous manufacturers were required to pay Rs. 610 per ton of urea into the account of FPEC. This amount was used to subsidise the high cost of imported fertilisers.[6]

To cope up with the problem of rising landed cost of imported fertilisers resulting in lower conusmption on the one hand and excess profits to the domestic producers on the other, the Government adopted a two-fold strategy. On the one hand, the Government introduced a price pooling arrangement on

the basis of the wieghted average cost of imported and locally produced fertilisers to avoid increases in the farmgate prices to the full imported cost. The arrangement also facilitated maintenance of uniform consumer prices through the pool irrespective of source of supply, thus insulating the farmers from the possible adverse impact of the crisis situation. On the other hand, the government also introduced a cess known as Fertiliser Pool Equalisaion Charge (FPEC) to mop up the unintended profit accruing to the industry due to higher consumer prices than the ex-factory price fixed for the indigenous produce. The pooling arrangement till then did not involve subsidisation by the government. However, as a short term measure to ameliorate the difficulties of the farmers and the producers alike a system of subsidy on phosphatic fertilisers at the rate of Rs. 1250 per ton of Pnutrient was introduced in March 1976 so that farmgate prices could be kept low despite rising cost of production without jeopardising the interest of fertiliser industry.

Marathe Committee Recommendations and Retention Price Scheme (RPS) Involving Subsidisation

The oil crisis of 1974 not only resulted in 200 to 300 per cent increase in the international prices of imported fertilisers, but also escalated the costs of creating new capacities threatening both the fresh investments and the sale of fertilisers at acceptable prices to the farmers at large. The government therefore set up a High Power Fertiliser Prices Committee (popularly known as Marathe Committee) to suggest a suitable pricing system which would ensure higher fertiliser use, simultaneously maintaining the financial health and growth of the fertiliser industry. The acceptance of recommendations of the Committee was the gensis of the current fertiliser retention prices and the subsidy system that heralded a new era, both for fertiliser industry and self-sufficiency in major agricultural crops.

Nitrogenous fertiliser prices were reviewed in 1977 on the basis of Marathe Committee recommendations. The retention prices for different plants were based on 12 per cent post-tax return on net worth at 80 per cent capacity utilisation w.e.f 1.11.1977. However, controlled selling prices of fertilisers were not disturbed. Varying retention prices based on cost differences in different plants involved higher subsidy to high cost units and no subsidy to low cost units. Ex-factory retention prices of complex fertilisers were revised on the basis of BICP recommendaions w.e.f. 1.12.1979 so as to provide for 12 per cent post-tax return on net worth.

As the price of imported fertilisers had not only been higher but also fluctuated markedly, subsidy on imported fertilisers continued. Other subsidies on fertilizers related to freight equalisation for supplying fertilisers at uniform price throughout the country and subsidies for use in backward, hilly, inaccessible and tribal areas and on account of use by small and marginal farmers in dry areas. These subsidies offer a unique example of retail price being consistently reduced between 1974 and 1979 (e.g. urea from Rs. 2000 per ton in June 1974 to Rs. 1450 after 1979 budget) and thereafter more or less stable for full one decade since 1980-81 despite substantial cost escalations during the intervening period.

Fertiliser prices payable by the farmers remained unchanged for the entire decade of the eighties while the cost of production as well as imports have been continuously rising resulting in mounting burden of fertiliser susbidies. As a corrective measure an across the board increase of about 40 per cent in the consumer prices of all fertilisers, except the low analysis

fertilisers, was announced in the Union Budget presented in Parliament on July 24, 1991. However, the pressure from various lobbies forced the government to totally withdraw the price hike for fertilisers used by small and marginal farmers and roll them back somewhat for other farmers w.e.f. Aug. 14, 1991. Prices of various types of fertilisers for farmers other than small and marginal farmers are given below :

	Price for Other than Small and marginal farmers	
	As per Budget Announcement 25.7.1991	Revised Prices w.e.f. 14.8.91
	Rs. Per Ton	Rs. Per Ton
Urea (46 per cent)	3300	3060
Muriate of Potash (60 per cent)	1820	1700
Diammonium Phosphate (18 : 46)	5040	4680
NPK (17-17-17)	3640	3380
NPK (15-15-15)	2940	2740
NPK (19-19-19)	4140	3840
Ammonium Phosphate Sulphate (20 : 20 : 20)	3640	3380
Nitro Phosphate (20 : 20 : 20)	3360	3120
Nitro Phosphate (23 : 23 : 0)	4120	3800
Ammonium Phosphate Sulphate (16 : 20 : 0)	3220	3000
Urea Ammonium Phosphate	5040	4680
NPK (14-28-14)	4280	3960
NPK (14-35-14)	4760	4420
NPK (10-26-26)	4140	3840
NPK (12-32-16)	4560	4220

Price and movement control was lifted from low analysis fertilisers like calcium ammonium nitrate, ammonium chloride, ammonium sulphate and sulphate of potash w.e.f. July 25, 1991.

In addition in the case of super phosphate a ceiling is planned on the subsidy payable to producers so as to move towards total deregulation in the next few years. This should act as an incentive for all high cost units to reduce costs and improve efficiency.

The hike in fertiliser prices was severly criticised by the farmers' associations, the fertiliser industry and the politicians—both within and outside the ruling party. An increase in procurement prices also would not fully neutralise the impact of fertiliser price hike because : (1) the government does not procure all agricultural commodities e.g., vegetables, fruits and number of other agricultural commodities, and (ii) it is only the surplus of big farmers which is available for procurement by the government. The small and marginal farmers with 76.3 per cent of land holdings consuming 30 per cent of fertilisers in the country, would suffer even if the compensatory increases in the procurement prices of foodgrains were granted.

It is also argued that compared with 1970-71, the procurement price of wheat is up 296 per cent and of paddy 380 per cent. The latest fertiliser price increase for general category of farmers took them up 375 per cent and diesel oil is up 644 per cent, making the input-output cost ratio for Indian farmers one of the most adverse in the world. The paddy/nitrogen price ratio for Indian farmers is below 0.4 against much higher paddy/nitrogen price ratios in most Asian countries : 0.84 in South Korea, 0.75 in Taiwan, 0.62 in Indonesia, 0.56 in Malaysia, 0.57 in Bangladesh, 0.45 in Nepal and 0.43 in Sri Lanka.[7]

Retention Price Norms

For the last 15 years, i.e. the five three yearly completed cycles and the sixth currently in progress,[8] fair ex-factory retention prices for various products for different producers have been fixed and administered by Fertiliser Industries Coordination Committee (FICC). RPS allows for reimbursement of reasonable costs of production including a margin of 12 per cent post-tax on net worth subject to prescribed efficiency norms of capacity utilisation and consumption of utilities. Norms have been fixed for all input costs and other fixed and variable costs including maintenance and repairs and short-term working capital as well as long-term capital. The norm for Debt-Equity Ratio has been allowed at 4 :1 and the normative level of inventories for purposes of fixation has been taken at 3 weeks for urea and 2 months for DAP. Till 31.3.1988 depreciation on fixed assets was allowed assuming the life of assets to be 10 years i.e. at 10.56 per cent and the standard capacity, utilisation for purposes of determining normative cost structure was taken at 80 per cent. Under the scheme the provision is for more or less automatic increase in the retention price, after due scrutiny, for every increase in the price of feedstock like gas or naphtha and other input costs.

For practical operation of the Retention Price Scheme (RPS) the Fertiliser Industry Coordination Committee (FICC) fixes normative allowance of costs covering a full period of three years called a pricing cycle. Such allowance does not allow escalation in overheads that take place during the pricing cycle of three years. Escalation in raw material related service costs such as stevedoring, clearing, transport and demurrage etc. are also not allowed. Cost increases in packing materials and marketing costs such as godown rents, handling and transport costs are also not allowed fully.

For fixing retention prices FICC allows return on net worth only on net fixed assets which are in actual operation at the beginning of the pricing period.The additional investment by a producer on renewal; replacement, revamping and modernisation which are in progress or addition to operations made during the pricing period do no qualify for return and are considered for price fixation for the next pricing period. Facilities which are created even at the instance of the government policy but remain idle also do not qualify for return.

The following capital expenditures are also disallowed by FICC for determining retention prices :

(i) those related to delay in completion of the project i.e. financing charges and project management expenses related to delay, and
(ii) the excess expenditure relating to delay in commissioning of the plants i.e. expenditure on trial runs beyond provison or project estimates.[9]

The sysem of RPS in operation since 1977 had produced excellent results in terms of increase in installed capacity which has reached 13 million tons, and the consumpion exceeding 11 million tons. Overall capacity utilisation rate increased from 53 per cent to 85 per cent in 'N' and 65 per cent to 87 per cent in 'P' resulting in a self-reliance of around 90 per cent.

However, the system of RPS which was programmed to be self-financing in early seventies resulted in huge subsidies due to the bottleneck in consumer prices and rise in input costs, increased output and high capital

costs of production, especially from the new gas-based plants. The direct budgeted subsidy alone on indigenous and imported fertilisers had touched Rs. 3651 crore for the year 1989-90. These rising subsidies together with high average capacity utilisation in the industry reaching 85 to 87 per cent and in some cases even upto about 120 per cent (as in the case of many plants of IFFCO and KRIBHCO) led to the announcement of tighter RPS norms for the fifth pricing period i.e. from 1.4.1988 to 31.3.1991.

Revised Retention Price Norms w.e.f. 1.4.1988

Mounting subsidies and rising profits of fertiliser companies made government set tougher norms as regards capacity ufilisation and depreciation so as to bring down retention prices with a view to mop up extra profits of fertiliser companies and reduce subsidies. In January 1989, the government revised the capacity norms from 80 per cent flat to 80 to 90 per cent on graded basis and the depreciation based on 20 years life instead of exising 10 years life. These norms have been made retrospectively effective from 1.4.1988.

It was laid down that the gas based units would be allowed 12 per cent post-tax return on net worth at 80 per cent capacity utilisation for the first year of its operation. From the second year to the tenth year of operation, the units were to be allowed a 12 per cent post-tax return on net worth at 90 per cent capacity utilisation. From eleventh year the return on net worth of 12 per cent was to be allowed at 85 per cent capacity utilisation. The depreciation charge in the price build-up was also brought down to 4.75 per cent based on 20 years estimate of plants life.

It was estimated that the combined impact of revision in capacity utilisation and depreciation norms could be between Rs. 40 crore to Rs. 60 crore for a new plant with an invesment of about Rs. 750 crore. The private secor industry resisted this move. The profitability of the industry declined after the price revision despite higher production and sale, adversely influencing the future of an industry which had shown remarkable performance during the eighties. In view of these developments, the Ministry later decided to relax RPS by allowing higher depreciation rate of 6.5 per cent spread over 15 years.[10] The government was also contemplating to withdraw subsidy to units operating at 100 per cent or more capacity. However, the move was subsequently rightly dropped as it tantamounts to penalising efficiency and taking away whatever incentive existed for profit maxmisation through higher capacity utilisation.

There was also a move to revise the pricing norms for phosphatic fertilisers by taking stream days as the basis for formulating norms of production level instead of capacity utilisation which would go up to 82.5 per cent. For imported phosphoric aacid the norm is proposed to be raised from the existing 6000 hours per stream per annum to 6300 hours per stream per annum. These proposals are not welcomed by the industry circles due to frequent interruptions in the supplies of imported phosphoric acid and delays in their price fixation leading to closures of plants.[11]

The new three year fertiliser pricing policy in the offing is likely to allow for automatic increases in the retention prices within a set of streamlined norms. Adoption of automatic escalations and simplification of procedures will bridge most of the delays and lags between price revisions and payment of subsidies. It is believed that there is little scope of saving on the subsidy burden by tinkering around with the pricing system which has been optimised over a period of time. However the new policy, which was to be ready by the

end of 1991 to be effecive from April 1, 1991, is expected to contain some disincenives by which a loss making unit would have little alternative but to improve productivity or close down quickly. The modalities of the policy are being worked out.[12]

Evaluation of Operation of Retention Price Scheme

It is more or less universally acknowledged that the system of RPS as operated between 1977 and 1988 despite certain deficiencies, has served the twin objecives of fertiliser pricing policy—supporting higher agricultural growth through more intensive use of fertilisers and creation of larger fertiliser capacities and their fuller utilisation—creditably well. There has been a phenomenal increase in investment and installed capacity (N + P) from Rs. 800 crore and 3.5 million tons in 1975-76 (prior to the introduction of the RPS and subsidy scheme) to about Rs. 9300 crore and 10.8 million tons during 1988-89. There has been a consistent improvement in the capacity utilisation rate on all India basis in both N and P sectors. By adopting normative basis of price fixaion the system of RPS has provided a tremendous incentive to units to improve their profitability by seeking to work better than norms and enhance their profitability even above 12 per cent of net worth granted under the scheme. The units are automatically warned to be on their toes because any deaccleration in capacity utilisation, wastages and inefficiency would result in losses not reimbursable under the scheme. The overall effectiveness of RPS is reflected in the fact that during 1988-89 the capacity utilisation of gas based plants improved to as high as 95 per cent, that of Naphtha based plants to 84 per cent, and that of fuel based plants to 88 per cent.

Though the RPS has encouraged higher, capacity utilisation it is alleged that it has made industry less energy efficent. Energy efficiency varies between 16 and 9 mega calories. As per the existing practice of FICC, investments made in improving the energy consumption as well as benefits derived therefrom in terms of reduced energy consumption are ignored for fixing RPS for a period of six years. Industry sources are irked not only by the changes in pricing parameters in 1988 but also due to implementation of RPS involving delays in reimbursement of cost escalations, non-provision for replacement cost depreciation, non-reimbursement of special discounts granted by the industry at the instance of the government, collection of levies by the state governments even on fertiliser subsidies and non-provision of number of cost escalations during a pricing cycle.

No wonder, these flaws in principle and implementation reduced the profitability of the industry to 5.6 per cent against stipulated 12 per cent on net worth despite high level of utilisation during 1987-88, even before the changes in pricing parameters effecive from 1.4.1988 which brought the profitability further down to 3-4 per cent of net worth.[13] The latest criticisms by the industry of the practical operation of RPS, therefore, need a thorough study.

In addition to less than optimum satisfaction of the industry, the operation of RPS for more than a decade has also resulted in an unabated annual increase in fertiliser subsidies, which now constitute about a half of annual total Central Government subsidies. With a view to reducing fertiliser subsidies without jeopardising the interest of small and marginal farmers the government introduced dual pricing of fertilisers in August 1991.

Dual Pricing Policy for Fertilisers

Dual pricing policy for fertilisers which envisages a 30 per cent price increase for big farmers and pre-budget prices (i.e. prices as prevailing on July 24, 1991) for small and marginal farmers, effecive from August 14, 1991 is ill conceived and administratively impractical. Large farmers will begin to chop their holdings, at least on paper, into smaller one to qualify. Millions of marginal farmers who used little or no fertilisers in the past will suddenly demand several tons each in order to sell their entitlements at a profit. Some institutions will have to be nominated which check the claims of the farmers to be small and these institutions will become hotbeds of corruption. In addition, large farmers will use small farmers as proxies to get cheaper fertilisers.[14]

Small and marginal farmers[15] account for about 76.3 per cent of the country's about 90 million holdings i.e. they number about 68 million. In order to ensure that small and marginal farmers actually get the benefit of the old prices, the state governments will have to make 68 million coupons or identity cards, or else the ration cards are to be prepared for all small and marginal farmers; and these ration shops may not be in a position to handle the huge supply of fertilisers honestly and effectively due to financial, administrative and other constraints. In the absence of these and other controls there is a potent danger that the large farmers will grab the concessions by engineering distortions in the scheme. No wonder, the state governments have serious reservations about being able to implement the dual pricing scheme. The Agriculure Minister, Mr. Balram Jhakar too has argued that the dual pricing scheme for fertilisers would not be practicable and the intended benefits might not reach the small and marginal farmers at all, and that some other means to uplift them would be desirable.[16]

The state governments have also made it clear that the provison of Rs. 405 crore for the scheme of financing supply of fertilisers to small and marginal farmers at concessional rates is too meagre. It is believed that without adequate central assistance the burden of exempting the large number of these farmers from the price hike would be unbearable for state governments.[17] Infact the states want a uniform fertiliser price or an open-ended scheme where the central government continues to finance the subsidy to small and marginal farmers even after the budgetary allocaion of Rs. 405 crore runs out.[18]

Fertiliser Subsidy Linked to Cooperative Loans

Central government has directed the state governments to link the fertiliser subsidy for small and marginal farmers to cooperative loans. Most states are therefore, to provide the subsidy through the credit system under crop production loans. The system could be effectively implemented because a part of these loans is usually provided in kind, of which about 80 per cent consists of fertilisers. This subsidy is to be adjusted by the states against central loans for the cooperative sector.

The implementation of the scheme through the credit system provides for an automatic safety net as the process of identification and eligibility will be met through the normal vetting process. However, a lacunae in the implementation of the scheme through the cooperative credit system is that all

small and marginal farmers will not be entitled to the subsidy because entitlement to the concessional fertiliser price would require that a farmer must be a member of a cooperative, must fulfil eligibility standards and must not be a defaulter. It is also contemplated that the states with weak cooperative credit system may provide the subsidy through the state agro-industry corporations which have the requisite experience and infrastructure.[19]

The states are to be allocated fixed sums from the total outlay of Rs. 405 crore earmarked for the subsidy according to a formula that takes into account the consumption of fertilisers and the area under cultivation by the small and marginal farmers in each state. The states have been directed to ensure that the target farmer is in the small and marginal category and that there is a proof of purchase in addition to taking into account factors such as holding size and previous use patterns. In addition, the quantity to be distributed is sought to be linked to fertiliser availability in the area.

The Centre has left to the states to work out the detailed modalities of implementing the dual pricing scheme in view of different agricultural delivery systems prevailing in different states and their other peculiarities and limitations. As such different states are bound to evolve different modalities and delivery systems to suit their specific needs and socio-political environment prevailing, keeping in view the broad policy parameters. Accordingly the effectiveness in implementation is also bound to vary in different states.

Subsidy Implications of Dual Pricing

The original Budget estimate of subsidy, based on the 40 per cent price increase, was Rs. 4000 crore. Of this Rs. 2900 crore was on account of indigenously produced fertilisers and Rs. 1100 crore on imports. While announcing the 10 per cent roll-back in prices in Parliament, the Finance Minister Dr. Manmohan Singh said that this would add Rs. 900 crore to the fertiliser subsidy, escalating it to Rs. 4900 crore. Even this figure of subsidy appears to be an under estimation as a number of factors having bearing on the subsidy seem to have been ignored.

Devaluation of rupee in July 1991 itself is likely to push up costs of imported rock phosphate, sulphur and phosphoric acid by about Rs. 450 crore. Moreover, the probable increase in fertiliser production from nine million tons in 1990-91 to ten million tons in 1991-92 will add another Rs. 350 crore to the subsidy because the subsidy is reckoned per ton of fertiliser produced and consumed. Subsidy is likely to go up further by another Rs. 300 crore due to recent increases in the prices of naphtha and fuel oil, the increase in railway freight rates and the increase in natural gas prices resulting from the recommendations of the Kelkar Committee.[20] Difficulties and the corrupt practices in the implementation of dual pricing scheme is likely to push up the subsidy still further.

Reports regarding the operation of dual pricing are not encouraging. Some of the states may find it difficult to implement the scheme due to enormity of the task and the weak infrastructure. There is, therefore, a legitimate apprehension that different states may evolve widely different schemes, making countrywide monitoring difficult. No wonder, state governments have ignored repeated queries from the Centre about the progress made in implementing the subsidy to small and marginal farmers. Instead they have written back demanding more funds. The demand for additional money by some states is as high as three times the sanctioned

amounts indicating that the total demand for funds for financing dual pricing could be as high as Rs. 1000 crore against the allocation of Rs. 405 crore by the central government.[21] However, it is encouraging that the sale of fertilisers is brisk even at maximum prices, i.e. at prices 30 per cent higher than the pre-budget prices.

Mounting Subsidies—Some Issues

Subsidies on fertilisers have gone up from Rs. 381 crore in 1981-82 to a budgeted subsidy of Rs. 3651 crore for 1989-90 including a subsidy of Rs. 530 crore on account of imported fertilisers. During this period the share of explicit fertiliser subsidies in total subsidies has gone up from 20 per cent to 43 per cent. The actual subsidy is even higher. For 1989-90 originally Rs. 3121 crore were provided for indigenous fertiliser subsidy which had to be revised upwards to Rs. 3771 crore. The subsidy is threatening to reach a staggering figure of Rs. 12000 crore on an estimated consumption of 20 million tons of nutrients by 1999-2000 for an estimated production of 240 million tons of foodgrains. As a matter of fact the industry is enjoying a much higher subsidy because it also has the benefit of indirect subsidies through the system of diffrential pricing with reference to feedstock and fuel.

These staggering increases in fertiliser subsidies raise many issues relating to the fertiliser pricing :

(i) Can the exchequer bear the burden of menacingly rising fertiliser subsidies?

(ii) Is the increase in procurement prices of foodgrains more inflationary than the rising budget deficits due to fertiliser subsidies?

(iii) Is the demand for fertilisers sufficiently price elastic to justify low fertiliser prices?

(iv) Is the fertiliser pricing providing desired incentive for cost efficiency in the fertiliser industry?

(v) Does fertiliser pricing not lead to subsidisation of urban population at the expense of rural population?

(vi) Are the fertiliser subsidies together with exemption of agricultural income from tax and the procurement price policy of the government not leading to accute inequalities in the distribution of rural income and wealth because the benefit of all the three goes basically to the large farmers as the smaller ones have neither income that could come under the tax net, nor resources to buy fertilisers, nor surplus agricultural produce that could be procured by the government?.

(vii) In nutshell, is the fertiliser pricing policy leading to ever rising subsidies promoting economic efficiency and socio-economic equity?

These questions require an in-depth examination to determine future course of fertiliser pricing having a bearing on policy regarding price stabilisation and distribution of income and wealth.

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