



## Ensuring Remunerative Prices to Farmers Challenges and the Way Forward

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### Background

Doubling farmers' income by 2022 is a paradigm shift in transforming policies and programs from production to income. Ensuring remunerative prices to the farmers is one of the several pathways to achieve the objective. In the Union Budget 2018, the Government of India (GoI) accepted the long-awaited demand of the farmers regarding the new minimum support price (MSP) at 1.5 times more than the cost of production. It appears that Cost A2 + FL, which covers the cost of production, interest on working capital, and imputed value of unpaid family labor is the cost of production that the government will be considering. The government has also announced the development of mechanisms to ensure that farmers receive at least MSPs of their produce.

To make the proposed policy effective, the government will develop and upgrade 22,000 agricultural markets, known as Grameen

Markets, to link these with the APMC (Agriculture Produce and Market Committee) mandis, and e-NAM (electronic-National Agriculture Market). It is proposed to upgrade existing local markets with the necessary infrastructure so that the benefits of the new price policy penetrate to the last mile.

NITI Aayog in consultation with state governments has proposed the following three alternative mechanisms:

**(i) Market assurance scheme** - This proposes procurement by government machinery from the farmers at MSP in case farm harvest prices fall below that.

**(ii) Price deficiency payment scheme** - Under this scheme if the farmers' sale price is below a modal price, then they will be compensated the difference between MSP and actual price subject to a ceiling that may not exceed 25 percent of the MSP.

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***(iii) Private participation in stockers scheme*** - This scheme relates to the procurement at MSP by the private entrepreneurs. A transparent mechanism will be developed so that private sector can empanelment for procurement if prices fall below MSP. The mechanism will also be developed to compensate private sector.

A policy dialogue was organized on “Innovations in Ensuring Remunerative Prices (MSPs) to Farmers: Challenges and Strategies” on 23rd March 2018 to (1) list possible ways of ensuring remunerative prices, and (2) explore feasible solutions of improving the existing institutional and market arrangements. The key highlights of deliberations are given below:

### **Challenges to Ensure MSPs**

One of the key challenges for making MSP effective is its actual administration in all the states. Though MSP is declared for 26 commodities, the actual procurement is mainly done for rice and wheat, sometimes oilseeds, onions, and recently pulses and potato (in Uttar Pradesh). The Situation Assessment Report of the National Sample Survey Organization (NSSO) shows that a small fraction of farmers is realizing the MSP. The main challenges of ensuring MSPs are: (1) inadequate markets and collection centers, (2) lack of appropriate infrastructure and storage facilities, (3) social safety net programs confined to rice and wheat only, and (4) imperfect information due to a weak price monitoring and forecasting system. There are very few years when MSPs are lower than the farm harvest prices (FHPs), and only during those years government intervention is needed either to procure from the farmers at MSPs or compensate them the difference.

Domestic production, global prices and trade policies determine the FHPs.

### **The New MSP**

The ‘New MSP’ is 1.5 times the cost of production, interest on working capital, and imputed value of family labor. There are apprehensions that this will have strong budgetary implications on the overall economy due to increased food subsidy bill. Some fear that this will also have inflationary pressure on food commodities. There is counter argument that the New MSP will raise farmers’ incomes, increase demand for non-farm commodities to boost economic growth, and improve marketing efficiencies. Empirical analysis can only provide the implications of the ‘New MSP’.

The policy dialogue deliberated on various issues related to MSPs and alternative ways of ensuring remunerative prices to the farmers.

### ***The New MSP and its implications***

- The origin and aim of MSP was to provide guaranteed prices to the farmers in the event of a glut in the market. The MSP policy significantly contributed to bringing about the Green Revolution that led to food self-sufficiency in the country. The scenario has completely changed from deficit to surplus of most of the food commodities. It is important to create a market driven economy by improving market efficiency, strengthening agro-processing, and promoting trade. It is not possible for the government to procure so many crops at MSP, therefore institutional innovations, agri-infrastructure, and the private sector will play an important role in the future. The role of the government should be to ensure that farmers are not exploited, and to share due benefits of

opportunities in domestic and global markets.

- There are apprehensions that higher MSPs will disincentivise the production of non-MSP crops. Farmers will tend to go for more assured and higher MSPs rather than non-MSP crops. This policy distortion will generate a surplus of MSP crops at the cost of non-MSP crops. A strong market structure that assures remunerative prices coupled with effective crop insurance can provide income insurance to the producers of all crops.
- Price volatility is higher for perishable commodities such as vegetables, fruits, milk, meat, eggs and fish, for which MSPs are not announced. It is important to ensure market stability and remunerative prices to the producers of these commodities. Sometimes the government intervenes in non-MSP crops, like potato and onion, through either procurement or export/import decisions to stabilize their prices. Recently, the Government of Haryana announced an MSP-like scheme for four vegetables-- tomato, potato, onion, and cauliflower. The compensation mechanism will be of similar type as of the price deficiency mechanism. The effectiveness of the scheme is yet to be seen.

#### ***New institutional arrangements***

- A deficiency price mechanism is always cited as one of the ways to compensate farmers in the event of prices falling below MSP. The Government of Madhya Pradesh has piloted the scheme for a few commodities during the last monsoon season. The scheme known as '*Bhavantar*

*Bhugtan Yojana*' (*Price Deficiency Payment Scheme*) shows the potential of scaling out to other states and commodities. The scheme is still at the pilot stage and needs corrective measures in its implementation. There are some media reports that traders are suppressing the prices but no such evidence was observed with large participation of sellers and buyers. The scheme appears to be cost effective as there is only 2 percent procurement cost compared to FCI's 15 percent.

- Market reforms are needed to integrate markets and connect with smallholders. Karnataka's model of electronic agricultural marketing platform with the NCDEX (National Commodity and Derivative Exchange) spot exchange is a success. At the national level, e-NAM is based on a similar pattern to connect buyers and sellers. The question is how to connect smallholders with these platforms in view of their small marketable surplus. Farmers appointed aggregators for marketing will help in consolidating produce for trading in e-NAM or any remunerative market.

#### ***Market instruments***

- To develop new market architecture, there is a need to invest in creating market infrastructure, especially to develop wet and cold storage, cold chains, and agri-packers and movers. These facilities contribute in controlling price crashes, ensuring higher FHPs and integrating with remunerative markets. Studies have shown that smallholders gain more during the post-harvest period if adequate

storage and transport facilities are available.

- Warehouse receipt is one way of postponing the sale of food commodities to realize higher prices. Farmers can get a receipt of their produce from the registered warehouse and become eligible to access loans. Recently, the government has come out with an e-format scheme for negotiable warehouse receipts. Unfortunately, very few warehouses (980) have registered with the Warehouse Development and Regulatory Authority (WDRA), out of 20,000 warehouses. There is a need to have more warehouses so that farmers can take advantage of warehouse receipt to defer the distress sale.
- Futures trading is another instrument to give price signals. Global experience reveals that it is an effective tool of price discovery. Unfortunately, farmers, especially small and marginal farmers, are unable to participate in futures trading due to (1) lack of knowledge, and (2) meagre marketable surplus. Therefore, there is a need to educate farmers about the benefits of futures trading. This also requires mechanisms to aggregate their produce for bulk trading.
- A pro-farmer trade policy will also contribute in ensuring higher prices to the farmers. Liberal export and careful import of agri-food commodities will help farmers to share some benefits of global opportunities. A stable trade policy, effective global food outlook monitoring mechanism, and responding to taste and preferences of importing countries will signal to farmers how to decide their production portfolio to harness global opportunities.

- To cover costs of production, the Government of Telangana has come out with an input assistance scheme. As per the scheme, the government will transfer ₹ 4,000 per acre per season to all the farmers. The total cost of the scheme will be about ₹ 8,730 crores for one year. This will help farmers to cover their cost and encourage improved input use efficiencies. Other states may soon follow the scheme to incentivize farmers to support them.

### ***Collective action***

- Most of the farmers in India are marginal and small. Their marketed surplus is too low. Their marketing and transactions costs are very high. Therefore, most of the farmers dispose their produce to the village traders at lower than MSPs or wholesale prices in main *mandis*. Collective action in transport and marketing is therefore necessary to reduce the transactions and marketing costs and realize the wholesale prices. Studies have shown that the Farmer Producer Organizations (FPOs) are accessing remunerative markets, and are engaged in retail, food processing, and exports. The government is already incentivizing farmers to form FPOs and take advantage of emerging and remunerative markets. The recent budget has exempted 100 percent income tax for those FPOs having business of less than ₹ 1 billion.
- Cluster farming is another way of aggregating farm produce and attracting agri-business to procure from the farm gate. Cluster farming linked with self-help

groups (SHGs) will benefit more if produce is transported to remunerative markets. Cluster farming helps in improving bargaining power, market access, and price realization.

- Contract farming, if implemented effectively, ensures better prices to the farmers. Global literature shows that contract farming helps in getting improved technologies and better prices. The GoI has prepared a model Contract Farming Act to overcome various problems in contract farming. It has protected the interests of farmers.

### **The Way Forward**

The following suggestions are made to strengthen the government policies to assure better realization of remunerative prices to farmers:

1. To ensure procurement of agricultural commodities at MSPs will require a strong network of collection centers for different commodities. The procurement can be done either by the public or private sector. A deficiency price model can also be tried to compensate farmers when FHPs fall below MSPs.
2. Engaging the private sector will be important, but appropriate and transparent mechanisms are to be evolved to check leakages.
3. There is a need to reduce market inefficiencies. Consumers are already paying much higher prices than the MSP. This is an indication of huge inefficiencies in the marketing system. More institutional reforms are needed to

shorten supply chains so that farmers get a larger share in retail prices.

4. There is a need to transform marketing arrangements for improving market efficiency by strengthening existing institutions, like FPOs, contract farming, cooperatives, and SHGs. These institutional arrangements will help in aggregating farmers' produce to reduce transactions costs and access remunerative markets.
5. A significant investment in agri-infrastructure is needed to make markets accessible to the farmers. Investment in developing agricultural markets, warehouses, cold storage, cold chains, and transport will integrate farmers with the remunerative markets.
6. A universal price policy will not solve the problem of price volatility. There is a need to classify commodities according to their status. These may be classified as: (1) commodities required for the social safety net program (e.g., rice and wheat), (2) surplus but not needed by the government (e.g., maize, coarse cereals), (3) deficit commodities but available in the global markets (e.g., edible oil), (4) deficit commodities and not available in the global markets (e.g., pulses), and (5) perishable commodities (e.g., fruits and vegetables). For each group, a different price and trade policy will be needed.
7. Pro-farmer trade policies need to be implemented for better price realization. Farmers need to be integrated with the global markets for commodities where the country has comparative advantage. There

is a need to identify commodities and niche markets to tap global opportunities.

8. The role of artificial intelligence (AI) will be helpful in effectively monitoring and forecasting the prices of agri-food commodities. Establishing monitoring and forecasting units at the state and national level will help in taking informed decisions well in advance.

In the short-run, a higher MSP will be important in raising farmers' income, but price-driven growth may not be sustainable in the long-run. In the future, technology will play a key role in driving farmers' incomes.

Therefore, in the long-run efforts are needed to improve efficiency and reduce cost through technologies. Technology-led income growth will make agriculture more efficient, competitive and sustainable.



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**National Academy of Agricultural Sciences (NAAS)**, established in 1990, is among the youngest of the Science Academies of India. The Academy's role is to provide a forum to Agricultural Scientists to deliberate on important issues of agricultural research, education and extension and present views of the scientific community as policy inputs to planners, decision/opinion makers at various levels.



**International Food Policy Research Institute (IFPRI)** provides research-based policy solutions to sustainably reduce poverty and end hunger and malnutrition in developing countries. Established in 1975, IFPRI currently has more than 600 employees working in over 50 countries. It is a research center of CGIAR, a worldwide partnership engaged in agricultural research for development.

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