

Trade Liberalisation and Indian Farm Sector

Understanding the Situation from Available Evidences

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Trade Liberalisation and Rise in Wheat Price

Let us first try to understand the concern about how agricultural trade liberalisation has been affecting our food security issue via the hike in prices. The rise in wheat price in last couple of years in India has been mainly the result of trade liberalisation. It is true that due to rising population growth supply of wheat fell short what has been demanded after 2004-05, but in the last five years significant market reforms, resulting in increasing the participation of the private sector in foodgrain trade, have been mostly responsible for the rise in wheat price. Chand (2007) has analysed the case in a well manner. A number of big companies (including multinationals), e.g. ITC, Cargill, Australian Wheat Board, Britannia, Con Agro, Delhi Flour Mills and some others, are now operating in foodgrain trade, holding sizeable stocks and playing with their inventories to cause increases in price and to take advantage of the same. In case the government had a reasonable stock it could keep a check on any abnormal increase in prices. But the government has a faulty price policy. Every year the minimum support price (MSP), which remains fixed for the whole particular season, is announced and thereafter the government starts procuring commodities like wheat and rice either at the MSP or by adding a bonus to the MSP. This fixed price policy does not fit in the open market system and thus inhibit the government in procuring the required quantity of produce. The procurement either falls short or exceeds what is needed to be purchased by the government. There is another concept called procurement price (PP), but virtually in practice the MSP turns out to be the fixed PP (sometimes with added bonus, as said earlier). It allows the private sector to outstrip government agencies by offering a little more than the procurement price. In such a situation, the government becomes a helpless witness since the procurement officer cannot pay even a penny more than what is already fixed. According to Chand (2007), this is the sole reason for the failure of the government to achieve its procurement target and objective. This practice also puts the government in an embarrassing situation when it has to meet its needs through purchasing wheat from the multinationals, which are hoarding the grains, (or through imports) by paying higher prices than those paid to domestic producers.

Chand (2007) emphasises that there is an urgent need to follow a dual

price system in order to procure grain at required quantity and thus stabilise the market price of grain. The government should immediately differentiate between the MSP and PP and the latter should be higher than the former while at the same time the PP should also be kept flexible, meaning, for example, that the PP can be declared on a weekly basis. The MSP has an objective to save farmers by ensuring remunerative prices to them for their produces on the basis of the Commission for Agricultural Costs and Prices (CACP) recommendations while prices fall below the level fixed by the CACP. Such MSPs are fixed at incentive levels so as to induce the farmers to make capital investment for the improvement of their farm and to motivate them to adopt improved crop production technologies to step up their production and thereby their net income. However, how far these objectives are met through the MSPs is questionable and that is why the PP should be given substantial importance. When the market price of a grain is higher than the MSP, the PP should follow the market norms and offer market prices.

The Crises in Farm Sector

There are a large number of small and marginal farmers in India. They have been suffering from adverse effects of uneven liberalisation in international agricultural trade. In consequence, several small and marginal farmers have committed suicide in various states in India in last few years for the reason that they had been heavily indebted to the private non-institutional moneylenders and at the same time they had been unable to get the proper price for their products. Rural institutional credit supply failure is clearly one of the responsible factors for farmers' misery, but the more serious concerns are the distortionary tariff and price policies adopted by the developed countries. The huge subsidies which are given to the farmers in the developed countries have been artificially reducing the prices of their produces and simultaneously destroying the comparative advantage of the farmers of developing countries. While the developed countries are protecting their farmers through conservative measures (by imposing tariffs on imported

agricultural produces and by providing subsidies to their farmers) on the one hand, they are demanding for, and also forcibly implementing, market liberalisation in developing countries to capture the market. For such forcible implementation of liberalised policies in developing countries, the developed countries are taking help from the World Bank and International Monetary Fund (IMF) on which the developing countries are dependent for loans. Table 1 presents a picture of agricultural subsidies in India from 2000-01 to 2004-05. Fertilizer subsidy experienced a downward trend till 2002-03, except a marginal increase in 2003-04. In 2004-05, it has increased significantly due to the fact that the government realised that sluggish growth in agriculture was going to hamper the overall GDP of the country. As regards subsidy in power sector, one can hardly figure out about how much is going to the farmers as electricity subsidy since the Ministry of Agriculture itself finds lack of clarity in this regard (see note below Table 1). Irrigation subsidy figure is clearly lower in 2004-05 than that in 2000-01. Seed and other subsidies have experienced an increasing trend though, the overall picture is not impressive. The situation can further drastically worsen if people do not become conscious and raise voice since the pressure from the other side is mounting in order to liberalise our

Table 1: Agriculture Subsidies in India During 2000-01 to 2004-05

| Item | Rs. in crore | | | | |
|---|--------------|--------------|--------------|--------------|--------------|
| | 2000-01 | 2001-02 | 2002-03 | 2003-04 | 2004-05 |
| 1. Fertilizer | 13800 | 12595 | 11015 | 11847 | 16127 |
| 2. Electricity* | 6056 | 9342 | 7354 | NA | NA |
| 3. Irrigation** | 13465 | 13164 | 15012 | 11142 | 12990 |
| 4. Other subsidies given to marginal farmers and Farmers' Cooperative societies in the form of seeds, development of oil seeds, pulses etc. | 2686 | 3041 | 3133 | 4018 | NA |
| Total | 36007 | 38142 | 36514 | 27007 | 29117 |

Notes: * Includes all subsidies to Electricity Boards and Corporations. Separate estimates of subsidies on Electricity exclusively provided to agricultural sector are not available.
 ** The rates for supply of water to farmers are kept low as a matter of policy, resulting in losses to the Government irrigation system. The excess of operating costs over the gross revenue is treated as imputed irrigation subsidy.

Source: Directorate of Economics and Statistics, Ministry of Agriculture, Govt. of India.

agricultural trade. Let us now try to understand the overall situation by looking at the available evidences and relevant existing literature.

Two opposing schools of thought are found in the literature on liberalisation and agriculture. A part of the literature has been well summarised by Vakulabharanam (2005). One school stresses that there is a policy bias against agriculture in LDCs, keeping output prices artificially low (as compared to the international prices) by maintaining subsidies on inputs. This school suggests removal of incorrect price incentives, i.e. input subsidies, from agriculture and making agricultural market more open to global trade. As for example, Khan (2004) argued that input subsidies led to misuse or over-use of inputs. However, another school of thought offers an argument, among others, saying that subsidies that the farmers of developed countries receive are much significant than that received by the farmers of developing countries (see, among others, Anderson, 1992; Tangermann, 2006), thereby resulting in unfair competition in international market. Bardhan (2006: 1395) argued that, in exports, the major hurdle the small producers face “is often due to not more globalisation but *less*.” In 2000, the producer subsidy in OECD countries was US\$ 330 billion – equal to Africa's entire annual GDP (Albert and Springer-Heinze, 2006). The protectionist policies of developed countries in agriculture are highly distorting and impose substantial costs on farmers in developing countries (Ismail, 2006). Recent estimates by International Food Policy Research Institute (IFPRI) suggest that protectionism and subsidies in industrialised countries cost developing countries about US\$ 24 billion in agricultural and agro-industrial income (cited in Pal, 2006). If all dynamic and spill-over effects are taken into account, the figure will be much higher. In the EU and USA, the subsidy level is very high for wheat, sugar and rice (Naik 2005, Chakraborty and Singh 2006). Sugar and cotton, along with some other items, which receive the highest level of subsidies in the EU or USA, are very important export commodities in the world market. Subsidies on these items are undermining the export potentials of many developing countries. The

trade opportunities of developing countries are being negatively affected both by the domestic support (on production or output) and export support in developed countries. Philip and Jenniah (2006) argued that the removal of subsidies by the US, EU and China would increase the world price of cotton by 18 per cent. They also argued that a small change in subsidy could create a phenomenal impact on the cotton production of some countries like the US and EU, to the extent of 15 and 32 per cent respectively. This, in turn, would result in supply shifts. Subsidies given in cotton at the global scale averaged US\$ 5 billion and the extent of subsidies prevailing in the global level is close to 13 per cent of the total value of cotton produced in India. US subsidy to cotton farmers is in the form of direct assistance to farmers through marketing loan assistance and market loss assistance. Stiglitz (2003: 206) commented that “[T]he U.S. pushed other countries to open up their markets to areas of our [the USA's] strength ... but resisted efforts to make us reciprocate”. Tangermann (2001) points out that, as regards reduction in export subsidies, the EU has created main problems since their share in total worldwide export subsidy on many agricultural products is very high. Naik (2005) states that the world prices of sugar now are below the costs of production of some of the most efficient producers. “In fact in some cases, such as cotton in India, the efficient producers are unable to compete in their own domestic market. Cotton imports in India have increased substantially due to the availability of cheap US cotton, as a consequence of the subsidies provided by the US to their farmers” (Naik and Singh, 2003: 60). Cotton farming occupies a significant place in the Indian economy as a means of employment to over one million farmers in the primary sector. It is also offering direct employment in the textile industry that significantly contributes to an extent of 14 per cent of the country's industrial production, 30 per cent of the country's export earning and 4 per cent of the GDP. Let us refer to Philip and Jenniah (2006) for the Indian cotton-case in liberalised era. Cotton imports were liberalised in 1991. With this the monopoly of Cotton Corporation of India was terminated and

imports were placed under the open general license, allowing unrestricted imports by private traders. The import duty was originally set to zero and there was a surge in imports in the late 1990s (see Table 2). On account of this surge, domestic prices too witnessed a major decline, resulting in incidents of suicides committed by cotton farmers. The situation forced the government to impose 5 per cent tariff in 2000. Still this could not provide cotton farmers with a major remedy.

Table 2: Import Trend of Raw Cotton Lint in India

| Year | Import quantity (in metric tonne) | Import value (in 1000 US\$) | Unit price of import (in US\$ per metric tonne) |
|------|--------------------------------------|--------------------------------|--|
| 1990 | 167 | 311 | 1862 |
| 1996 | 8795 | 2850 | 3086 |
| 2003 | 241787 | 333282 | 1378 |

As we already said, liberalisation has caused several Indian cotton farmers to commit suicide. Narayanamoorthy (2006) observes that profits have been declining particularly since late 1990s, because of a substantial increase in the cost of cultivation. He asserts that farmers need remunerative prices for their crops because their income from crop cultivation is not enough to even cover their consumption expenditure. Moreover, the farmers have been indebted to moneylenders, traders etc. for they had taken loans from these non-institutional sources. There is another concern in cotton farming. Let us refer to the observations of Narayanamoorthy and Kalamkar (2006) for elaborating the concern. Cotton's productivity in India is one of the lowest in the world mainly due to attacks by pests/insects and low coverage of irrigation facility. In spite of using pesticides, farmers are unable to control the bollworm – the key pest in cotton – that ravages up to 80 per cent of crop output. In India, *Bt* (which stands for *Bacillus Thuringiensis*) cotton was introduced in March 2002 for commercial cultivation. This variety can protect itself from the bollworm. Although the productivity and profit from *Bt* cotton cultivation is substantially higher than the conventional hybrid cotton varieties, the seed cost of *Bt* cotton is very high as compared to non-*Bt* hybrid varieties. At least as a short term measure, direct subsidy

should be provided for *Bt* cotton seed, but liberalization is standing in the way of such measure.

Shah (2006) analyses the effect of WTO on Indian dairy industry. Milk is such a product using which (as input) a number of by-products (e.g. butter, different kinds of sweets, *ghee*, *paneer* etc.) have grown (or even can further grow in the future) in the rural agro-industrial sector in India. The success of milk producers' unions/cooperatives, like AMUL, is well-known in India. But let us not forget that millions of small farmers who produce nominal quantity of marketable surplus of milk (only a litre or two) are majority in this industry. Landless labourers in India account for 21 per cent of the total rural households.¹ Though they do not have any share in the total landholding, they own 12 per cent of the milk produced. At current prices, the value of livestock products in the country in 2003-04 is estimated at Rs. 164,509 crores with milk and milk products accounting for 67 per cent. Indian dairy industry has the potential to capture a considerable part of the world market but, as Shah (2006) argued, currently this industry is adversely affected by distorted world prices of dairy products due to export subsidies extended by the EU and US. Moreover, developing countries cannot participate in international trade because their products are barred from entry into rich countries by trade barriers, restrictive trade policies and stringent health and sanitary standards.² Even if Indian dairy producers could initially afford to pay EU tariffs of 144 per cent on butter and 76 per cent on milk powder, it could hardly compete in Europe with domestic producers, half of whose income is derived from subsidies (Oxfam, 2002a). At the same time, India's efforts to export milk and other dairy products to new net dairy-importing

¹Oxfam (2002b) has noted that India has now become the world's largest dairy producer, producing 84 million tonnes of milk. Its dairy sector includes a network of cooperatives serving more than 10 million farmers in over 80,000 villages.

²Albert and Springer-Heinze (2006) argues that although stringent regulatory requirements contain risks, the rural producers in developing countries should consider such requirements as opportunities which would allow them to meet rising quality demands of consumers throughout the world.

markets in countries in South-East Asia, the Gulf, and the southern Mediterranean are being hampered by unfair competition from subsidised European dairy exports (Oxfam, 2002b). On the other hand, as Shah noted, Indian milk producers are rather worried because an increase in cheap imports of milk products, particularly milk powder, would further adversely affect their milk production by lowering the price of the milk they sell.

Globalisation has created some positive effects on Indian economy too as we have seen that through the 1990s the share of handicrafts exports in the overall manufacturing exports of India has risen from 2 per cent to 5 per cent (Leibl and Roy, 2003). But Basu (2006), while visiting to the village of Jakorta in a remote corner of Gujarat and talking to the villagers who were engaged in earning their livelihood largely from handicrafts and mainly embroidery work on textiles, found “double-edge sword of globalisation”. What is that? On the one hand, the villagers had benefited in the last decade because of globalisation by selling their products to other countries. On the other hand, they feared that their livelihood could get wiped out by competition from some international producers who decide to export to India. Basu emphasises that the villagers are still poor enough since end of prosperity for them could mean poverty, destitution and even starvation. In the present situation, producers cannot avoid this double-edge sword of globalisation. But the sword has already started hinting that quantity of loss is much higher than that of gain due to access to limited resources. For keeping a balance, within WTO a low income country should have adequate scope for adopting conservative import policy while at the same time it should take advantage of trade liberalisation and promote its products in other countries. In the whole dynamics, south-south trade related matters are also involved. For example, removal of subsidies from groundnut in India and China would greatly benefit the African countries in international trade (Beghin *et al.*, 2006). To conclude, WTO needs to take a very careful look at the country specific cases while trying to pursue trade liberalisation in the world, so that the poor countries' interests are fully protected.

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