

**REVITALIZING POLICIES FOR FOOD SECURITY  
AND POVERTY ALLEVIATION IN SOUTH ASIA  
Three Case Studies in India**

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## **Revitalizing Policies for Food Security and Poverty Alleviation in South Asia**

### **1. Introduction**

South Asia Initiative (SAI) of the International Food Policy Research Institute (IFPRI) received overwhelming support from USAID (India and the agency's Global and Asia/Near east Bureaus) along with other donors (particularly Ford Foundation and Asian Development Bank) to strengthen policy research, communication and capacity development. The SAI launched various programs containing three layers: (i) regular dialogues with the Policy Analysis and Advisory Network for South Asia (PAANSA) to strengthen the policy dialogue between researchers and policy advisors/makers of the region, (ii) conduct high quality applied research on issues of importance to the region, and (iii) undertake capacity strengthening programs for researchers and policy advisors. The USAID (India) contributed towards implementing policy research in high priority areas delineated by the PAANSA members to strengthen action oriented research, exchange and training programs, and more effective and frequent policy dialogues with policy advisors and decision makers.

This project is supported by USAID (India) to provide alternative policy options in the emerging debate on following issues:

- a. What role can the private sector play in food grain management, especially in terms of procurement, stocking, distribution and external trade? How cost effective could it be vis-à-vis the public agencies? And finally, what is the appropriate overall regulatory environment for private sector operations?
- b. What has been the role of input subsidies in agriculture? Who really benefits from those subsidies, how effective are they in terms of their impact on agricultural production, what is their impact on the environment, and is there any need to rationalize the subsidy regime?
- c. What has been the nature and speed of diversification in food surplus states of Punjab and Andhra Pradesh? What sort of vertical linkages between the farm and firm are likely to emerge? What sort of enabling environment is necessary for India, particularly Punjab and Andhra Pradesh, to take a lead in graduating to high-value agriculture?

This report documents the activities and accomplishments of the studies for the quarter from October – December 2005.

## **2. Research**

Most of the interrelated case studies in Andhra Pradesh and Punjab are either completed or near completion. These studies are related to (i) rationalization of input subsidies; (ii) improving efficiency in grain management; and (iii) agricultural diversification and vertical coordination. During the reporting period following draft reports were prepared which are under revision and review. These include: (i) grain management in Andhra Pradesh: scope for reform and private sector participation; (ii) fertilizer subsidy in India; and (iii) a consolidated report on revitalizing agriculture sector of Andhra Pradesh: case studies on input subsidies, grain management and agricultural diversification. Other reports related to agricultural diversification in Andhra Pradesh and Punjab, and input subsidies in Punjab are under revision. A consolidated report on re-energizing Punjab agriculture based on three case study is also under preparation. A summary of the preliminary consolidated report based on the three case studies in Andhra Pradesh is given below:

### **Revitalizing Agriculture Sector of Andhra Pradesh: Case Studies on Input Subsidies, Grain Management and Agricultural Diversification**

Agricultural sector of Andhra Pradesh is confronted with inherent problems and emerging opportunities at domestic and global markets. The problems in agriculture sector are visualized mainly due to rising input subsidies, increasing inefficiencies in grain management, and declining total factor productivity. The subsidy regime, among other things, distorted prices, incentives and consequently popularized the production portfolio that enjoyed most of the subsidies (both input and output). It also promoted inefficient use of inputs. Based on the three case studies on input subsidies, grain management and agricultural diversification, the study prepared a road map for accelerating agricultural growth through rationalization of input subsidies, improvement of grain management system, and promotion of high-value commodities.

#### **Rationalize input subsidies**

There is alarming increase in the expenditure on agricultural input subsidies from Rs. 4.9 billion in TE 1983-4 to Rs 24.9 billion in TE 2002-03 (at 1993-94 constant prices), registered a compound growth rate of around 9 percent per annum. During 2002-03, the total expenditure on fertilizer, electricity and irrigation subsidies represented 12.9 percent and 2.7 percent of agricultural and aggregate gross state domestic product, respectively. Unequivocally, such a large expenditure on input subsidies needs to be rationalized. The question is how to do it when withdrawal of subsidy becomes a major political issue rather than an economic rationale. Therefore, the pre-condition for

rationalization of input subsidies is the political will to do that. This requires sensitization of political parties (ruling as well as opposition) on the adverse effects of input subsidies. IFPRI's study gives some interesting on this aspect.

The next question is how to do that? First, it seems in a democratic country like India, politically, it is 'gradualism' that is likely to work better than 'cold turkey'. But gradual withdrawal of subsidies should set a final date for complete phasing out. This will provide time to the producer for reallocating resources. Second, gradual phasing of subsidies should be supported by introducing input saving technologies. A shift in production portfolio and use of input-saving technologies would save inputs, minimize subsidy burden, augment income and contribute to higher agricultural growth in the state.

To do that, we need to reform agriculture sector which addresses such needs as: (i) market reform including resource pricing of both water and power, (ii) cost recovery of water infrastructure and provision of water supplies; (iii) reform agricultural markets that promotes HVCs, (iv) credit facilities to popularize technologies that reduce use of water, electricity and fertilizer, and (v) improve governance in revenue collection to improve supply and maintenance of infrastructure. The reforms need to be supported by creating appropriate institutions and governing structures for their effective implementation. The study recommends for re-introducing metering of power consumption in agriculture. Some innovative mechanisms need to be evolved for their effective implementation. For example, meters need to be designed in such a way that runs only with pre-paid cards. To benefit the smallholders, if any, the value of pre-paid cards may be discriminated based on the use of power (or water). Low power (or water) users may be charged relatively less on per unit basis than those use more units (or quantity).

#### **Improve efficiency of grain management**

The state is foodgrain surplus but food insecure at the household level. The existing grain management system in the state is inefficient and incurs a huge subsidy burden. Rice accounts for a major share in subsidy bill. The major players in grain management, the Food Corporation of India (FCI) and the Andhra Pradesh Civil Supplies Corporation Ltd (APSCSCL), incur higher economic costs than those of private players and that escalated over time in the state. The food subsidy on account of quantities handled and economic costs of food grains purchases and distribution, the food subsidy has increased from Rs. 24.76 billion in 1989-90 to Rs. 174.99 billion in 2001-02. The cost of grain management of private sector was much less than the FCI and APSCSCL despite FCI gets

credit at a concession interest rate (8.15% subject to government furnishing a single default guarantee).

The expenditure items of interest payments, freight expenditure and handling expenses constitute the major items of FCI's operational expenditure. The expenditure on interest payments made up more than 40 percent of the FCI's expenditure during 2001-02. Similarly, the departmentalization of contractual labor in FCI depots has contributed to the rise in expenditure on employee's remuneration and benefits in recent years. In view of rising cost on various items, there are two options to improve the efficiency of grain management: (i) cut down the cost of the items where there is high inefficiency; and (ii) involve private sector in those items which can be out sourced. Cutting down the cost of government run programs is rather difficult. Therefore, gradual transfer of grain management to private sector with some conditions may reduce state exchequer on this. Due care will have to be taken in the event of falling and rising prices beyond some band. Whether it is the Government intervention, or the increasing role of market instruments such as futures markets, that would be needed to contain wide fluctuations is to be seen in the context of their overall cost effectiveness. Therefore, it is imperative to promote private sector participation, and strengthen the institutions such as futures markets and warehouse receipts. These will help in minimizing the price instability. To begin with the state may reduce levy rates in rice, and outsource procurement as per the model initiated in Madhya Pradesh and Assam.

#### **Promote agricultural diversification**

Agricultural diversification towards high-value commodities is offering an opportunity to the state for accelerating its agricultural growth. The state is well positioned to take advantage of this opportunity. Agricultural diversification towards HVCs will also reduce the burden of subsidy to some extent. Already a gradual transformation of agriculture towards HVCs is taking place. The share of high-value commodities in the total value of agricultural produce has increased from 23 percent in 1980-81 to 44 percent in 2001-02. The livestock and fisheries grew much faster; their share in agricultural GDP increased from 23 percent in 1991-92 to 44 percent in 2001-02. Share of horticulture in the crop sector increased from 19 percent to 22 percent between 1993 and 2001. The pace of agricultural diversification towards HVCs can be further accelerated by developing a comprehensive strategy. This will require: (i) promoting contract farming; (ii) enhancing credit facilities for HVCs; (iii) amending age-old market related acts; (iv) investing in infrastructure such as cold storage, roads, agricultural research and port; and (v) involve agri-business in HVCs. The pre-condition to promote HVCs is to invest on infrastructure development especially cold storage, cold chains, roads, ports and

agricultural research. Similarly, access to credit at reasonable rate of interest is important. At present, informal sources of credit dominate the rural credit sector with interest rates ranging from 24 to 40 percent compared to 12-15 percent from formal sources adding to the cost of borrowing.

Agricultural research also needs to tune its research agenda in view of changing demands for food commodities, especially HVCs. Involvement of private sector (especially agri-business) in understanding and identifying constraints in supply chain of HVCs would help in better targeting technologies for different markets.

The state has provided a good business environment to the private sector, especially IT sector. Similar business environment may be evolved for promotion of high-value and processed commodities to harness the emerging opportunities at domestic and global markets. It requires political will and reform agriculture sector in favor of high-value and processed commodities. Subsidies need to be rationalized and investment needs to be increased for creating infrastructure to provide better services and promote high-value and processed commodities. Government should also facilitate evolution of innovative institutions for linking producers with the agri-business. A comprehensive strategy to reform agriculture would revitalize agriculture and accelerate growth with equity.

### **3. Visitors' Exchange**

Dr. R.S. Sidhu from Punjab Agricultural University visited IFPRI-New Delhi office to closely work with P. K. Joshi and Karl Rich on agricultural diversification in Punjab from 25-28 October and 14-18 November 2005.

### **4. Review Meetings**

Several rounds of review meetings were organized with the collaborators to finalize the studies. These were on input subsidies in Punjab, fertilizer subsidy in India, grain management in Andhra Pradesh and agricultural diversification in Andhra Pradesh.

## **5. Conclusions**

The studies in Andhra Pradesh and Punjab on (i) grain management, (ii) input subsidies, and (iii) agricultural diversification, are near completion. It was planned that consolidated reports will be prepared for respective states. Accordingly, the draft of Andhra Pradesh was prepared during the reporting quarter. The Punjab consolidated report is expected to be ready by next quarter. A summary of the research studies in different areas is given in Annexure I.

During the reporting period three draft reports have been prepared which are undergoing review. These included (i) fertilizer subsidy in India (agriculture and industry); (ii) grain management in Andhra Pradesh; scope for reform and private sector participation; and (iii) consolidated report on revitalizing Andhra Pradesh agriculture. Other reports are expected to be submitted by the next quarter.

**We express our appreciation to the USAID (India) for extending full support for undertaking policy research in 3 key areas, which influence agricultural growth in India.**

## Summary table on progress of the project

S. No.	Activity	Achievement
1	Private sector participation in grain trade in Punjab and Andhra Pradesh	<ul style="list-style-type: none"> <li>• First draft report prepared.</li> <li>• Report will be reviewed in the next quarter</li> </ul>
2	Rationalization of input subsidies in agriculture	<ul style="list-style-type: none"> <li>• Draft of fertilizer subsidy in India has been prepared.</li> <li>• The preliminary draft on 'input subsidies in Punjab' is under preparation and is expected to be ready in the next quarter.</li> </ul>
3	Diversification of agriculture and farm-firm linkages in Punjab and Andhra Pradesh	<ul style="list-style-type: none"> <li>• Drafts on 'agricultural diversification in Andhra Pradesh and Punjab' were prepared and are being reviewed.</li> <li>• Collaborators from Punjab worked closely with IFPRI counterpart in New Delhi office.</li> </ul>
4	Consolidated report on Andhra Pradesh and Punjab	<ul style="list-style-type: none"> <li>• A consolidated draft report on 'Revitalizing Andhra Pradesh Agriculture: case studies on input subsidies, grain management and agricultural diversification' has been prepared and is being reviewed.</li> </ul>