UNIT 19  AGRICULTURAL PRICING POLICY IN INDIA

Structure
19.0 Objectives
19.1 Introduction
19.2 Effects of Agricultural Prices
   19.2.1 Effects on Income
   19.2.2 Effects on Cropping Pattern
   19.2.3 Effects on Resource Allocation
   19.2.4 Effects on Income Distribution
   19.2.5 Effects on Industrial Output
   19.2.6 Effects on Technology
   19.2.7 Effects on International Competitiveness
19.3 Objectives of Price Policy
   19.3.1 Proper Remuneration
   19.3.2 Income Distribution
   19.3.3 Price Stability
19.4 The Commission for Agricultural Costs and Prices
   19.4.1 Political Economy of Procurement Prices
   19.4.2 Emerging Problems
19.5 Let Us Sum UP
19.6 Key Words
19.7 Some Useful Books
19.8 Answers/Hints to Check Your Progress Exercises

19.0 OBJECTIVES

After going through this unit, you will be in a position to:
- explain the influence of agricultural prices on major macroeconomic variables;
- identify the objectives that should be considered in fixing agricultural prices;
- explain the role of the Commission for Agricultural Costs and Prices in price fixation; and
- identify the emerging problems of agricultural pricing policy in India.

19.1 INTRODUCTION

In India nearly two-third of the population is dependent on agriculture directly or indirectly for their livelihood. However, agriculture and allied activities like fishing and forestry account for less than 25 per cent of the national income. This partly explains why the majority of Indian population is living in poverty and misery. As you know from previous Units, agriculture apart from being carried out using inefficient technology, suffers from extremely low land and labour productivity. Unemployment, disguised unemployment and poverty are some of the resultant ailments. In such a scenario the role of the government in providing a system of just and remunerative prices to the farmers is quite important. A remunerative price for agricultural products ensures that

a) farmers are not forced to sell at below cost prices in slump times (usually harvest times), which is often the case in a country with low purchasing power and market demand,
b) agricultural prices do not get out of control in a year of crop failure, and
c) prices that maximize long run growth of the economy prevail.

In short, pricing of agricultural products tries to strike a right balance between (a) the producers (in terms of ensuring a minimum support price), and (b) the consumers (in terms of ensuring that people in a poor country are able to meet their minimum food and other requirements). In order to maintain a balance, the government has undertaken several measures such as: (i) declaration of minimum support prices (MSP) and procurement prices for important crops, (ii) procurement of foodgrains, (iii) strengthening of agricultural marketing and warehousing, and (iv) distribution of foodgrains through a public distribution system. But how far have these objectives been achieved? We have learnt about the marketing and warehousing aspects in the previous block while public distribution system will be taken up in Unit 21. In the present Unit we will look into the process and effects of fixing of agricultural prices.

19.2 EFFECTS OF AGRICULTURAL PRICES

Fixing of prices of farm products not only determines the income level of the agricultural producers, it has other significant repercussions as well. Since a large section of Indian population live below or just above the poverty line and spend a sizeable portion of their income on food, the impact of food prices on budget allocation of individual households is quite significant. Moreover, agricultural prices influence the pattern of farming in different regions of the country. Higher prices for the farm produce, other things remaining the same, increase the farmers’ incomes, which in turn, encourages them to go for newer technology in farming that raises productivity. Let us systematically arrange the implications of agricultural price fixation.

19.2.1 Effects on Income

If the farmers are left to the whims of the market it may cause disaster for the entire economy. The marginal and small farmers constitute a sizable majority of Indian farming population. This segment of the population does not have the economic power to withhold supply to the market when prices are low. In case of a sudden drop in prices (which may happen due to bumper harvest) or strategic collusive behaviour by the crop merchants which artificially suppresses the market price, the income of the farmers are adversely affected. This affects adversely not only the absolute level of poverty and inequality, the effect spills over to other sectors of the economy as well in terms of low demand for industrial products and services. The entire economy may face a downward trend.

19.2.2 Effects on Cropping Pattern

From the above, it is easy to understand that different sets of prices would imply different sets of income for their respective producers. As an example, let us consider two crops, viz., rice and wheat. Let us assume that (i) input prices of these two crops do not change relatively, (ii) the land which is under rice production is just as good to produce wheat, and (iii) the technology of wheat production is available to the rice producers as well. In that case a relative increase in price of wheat in comparison to rice would imply higher profits for wheat producers. In the long run this sort of divergent pricing and resulting profitability would induce the rice producers to transfer their land and capital to wheat production instead. In this way the cropping pattern gets affected. You may be aware that in an economy every production decision is taken on the basis of profitability or revenue generation. Therefore, price fixing of a particular product would ultimately influence the decision to produce the commodity itself.
19.2.3 Effects on Resource Allocation

As a farmer opts for a more profitable crop in place of a less profitable one, the resources he has at his command now get channelised for the production of the new crop. This is true at the individual, micro level. At a broader level also as large number of farmers start cultivating a particular lucrative crop, the authorities get pressurized to divert more resources to facilitate its production and marketing. Thus every kind of resource gets transferred at the service of the crop whose prices are more profit generating than the rest.

Let us take the case of Indian agriculture in the last few decades. Before the 1990s there were many restrictions on agricultural products’ exports. As a result, domestic production decisions were quite immune to international price movements. Crops of coarse variety such as jowar, bajra and ragi were produced in abundance which catered to the needs of the poorer sections of the country. After the export restrictions were lifted, the cultivators realised that production of cash crops such as sunflower, soya and cotton was much more paying since these crops fetched much higher prices in the international market. As a consequence, a shift in production is taking place. Production of coarse cereals has been declining and that of cash crops is rising. Results of this switching over have not all been positive. Coarse cereals which provide fodder and fuel as well as form a major part of the consumption basket of the poorer sections of the population, are now available in lesser quantities.

19.2.4 Effects on Income Distribution

Effects of changes in agricultural prices on income distribution work through demand and supply channels. A rise in the agricultural prices, keeping other things constant, would result in a rise in the income of the agricultural producers through the supply side. On the other hand, it would imply a contraction in the real income of the purchasers of agricultural commodities. Particularly, agricultural prices in a poor economy assume much more significance because food constitutes a large part of the budget of the poor people. Moreover, for the poor food is a commodity which has very low price elasticity. This means that if food prices increase the demand for food does not decrease much because it is a primary need for survival. In sum, therefore, a rise in agricultural prices would have a strong effect in terms of lowering the real income level of a sizable portion of the population in a poverty ridden country.

This issue of distributional effects of changes in agricultural prices, however, has other dimension also. If we find that most of the poor people are net purchasers of food then increase in food prices would affect the poverty level: a rise in agricultural prices would raise poverty and vice versa. On the other hand, if food is produced by poor people as well then the issue becomes more complicated. Low prices would benefit the poor consumers but impoverish the producers. High prices on the other hand, would benefit the producers but harm the purchasers. State intervention is needed to equitably solve such a problem.

19.2.5 Effects on Industrial Output

Output of the industrial sector is affected through both demand and supply as a result of changes in agricultural prices. As we have seen above, as a result of the rise in agricultural prices the real income of a large section of the population is adversely affected. Assuming that the rise in real income of the sellers of agricultural goods is less than the fall in the real income of the rest, the net effect would be a contraction of the aggregate income. That means people as a whole would be left with less money to buy industrial goods and services. With output of the industrial sector and services being demand determined their volume would fall. Thus the relative increase in agricultural prices influences the sectoral composition of the economy as well.
The other effect is through the supply side. You know that agricultural products are used as inputs in the production of a number of industrial goods. Therefore, a rise in agricultural prices would push up the prices of such industrial goods. We know that the demand for industrial goods is inversely related to their prices. Therefore, the demand for industrial goods would fall resulting in shrinkage of their output and employment.

Fig. 19.1

19.2.6 Effects on Technology

More profitability induces producers to raise the productivity of the crop in question by introducing newer technology. Newer technology many a time involves a fixed cost
of introduction. As long as the profits are high that should not be a major problem because higher profits besides encouraging technology also enables the producers to bear this high cost. Thus higher prices for agricultural products help in the introduction and use of new technology. In the Indian context this is illustrated by the following example:

Punjab and Haryana have been the birthplace of green revolution and these are the areas where there is widespread use of more productive technology. This is explained by the fact that a large quantity of grain procurement by the government is undertaken from these two states alone. Regular procurement and higher assured prices offered by the government in purchasing grains from the farmers have encouraged the farmers in these areas to go for more productive techniques.

19.2.7 Effects on International Competitiveness

Besides meeting the domestic needs the agriculture sector also needs to look beyond the national boundaries. Global market for foodgrains obviously is a different playground than the domestic market. Consumers in importing countries are more quality conscious though the prices there are generally higher than in India. In the international market, the Indian agricultural products have to compete with the products of other countries. Hence, competitive prices are essential to get access to global agricultural market. Changes in agricultural prices in our country definitely affect competitiveness of agricultural products in the global market.

The impact of agricultural price rise can be summarised through Fig. 19.1 given in the previous page.

Check Your Progress 1

1) Point out the effects of agricultural prices on the overall economy.

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2) Industrial production is affected by agricultural prices in two ways. What are those?

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3) In an economy where majority of the population are net food buyers, increase in food price may lead to fall in the general standard of living. Substantiate.

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19.3 OBJECTIVES OF PRICE POLICY

Role of the government in monitoring, fixing and balancing agricultural prices should be clear in the light of the above mentioned points. Prices should not be such that they result in losses for the producers. They should be conducive to higher agricultural production, investments and growth. These aspects are of paramount importance, particularly in a low income country such as India. On the other hand, prices should not be such that they bite into poor consumers’ pockets. Retardation of growth of industries and services may come about if people end up spending a larger chunk of their budget in meeting essential food requirements. In this section we briefly point out what should be the objectives of a proper price policy.

19.3.1 Proper Remuneration

About 80 per cent of the farmers fall under the category of small and marginal farmers. Apart from the uncertainty of the monsoon and irrigation, the other main risk they have to bear is the movement in market prices of their product. Unlike industrial products, agricultural commodities have many features of a perfectly competitive market. They are more or less homogenous in nature. There are large number of insignificant buyers and sellers. Therefore, producers have no control over prices and prices are much more volatile than those of industrial goods. Low prices of the produce often ruin the farmer. In such a scenario price-regulating authorities should always try to fix and maintain the range of price variation such that it becomes possible for the agricultural producers to make ends meet. One should also keep in mind that the less endowed farmers often borrow huge sums to carry out production and in the face of unremunerative prices it becomes more difficult for them to repay the loan. You might be aware of the suicidal deaths by cotton farmers in recent years in the face of falling global cotton prices and harvest failures.

The issue of remunerative prices for the producer is interlinked with the input prices. A sharp rise in the price of inputs, other things remaining the same, would adversely affect the profitability of the producer. The authorities, keeping this in mind in the years immediately after Independence, stressed on the importance of subsidized inputs. But in the 1990s with economic liberalization and globalization, most of these subsidies are being scrapped. Free or low priced electricity to the farmers, subsidized fertilizers, seeds and irrigation charges are slowly being withdrawn. This has adversely affected the farmers by increasing cost of production. In fact, the growth rate of output as well as investments in agriculture have declined in the 1990s compared to the previous decade. This issue is also related to the shrinkage of infrastructure facilities in agriculture. In order to cut overall expenditure, the government is not spending enough on basic infrastructural facilities in agriculture. These pressures ultimately lower the profitability of agriculture and the authorities are left with no other choice than raising the prices of agricultural products.

19.3.2 Income Distribution

We mentioned earlier that agricultural prices influence personal income distribution and employment opportunities. The agricultural producers gain as a result of jacking up of prices. But the consumers and industrial producers suffer. In the long run the industrial workers also face declining employment opportunities. So what should the regulatory authorities do? In the post-independence India the dilemma was resolved by envisaging an elaborate system of Minimum Support Prices (MSP) and procurement prices. The procurement prices are the ones at which foodgrains are purchased from the farmers by the government. This food is subsequently distributed through the Public Distribution System (PDS) at controlled cheap rates (the issue price). Often the procurement price is higher than the issue price. The loss is borne by the government as a subsidy given partly to:
i) the consumers, since the issue price at the PDS outlets is lower than the open market price; and the remaining part to

ii) the producers, since the procurement price would be higher than the market price.

![Diagram](https://via.placeholder.com/150)

Fig. 19.2

In Fig. 19.2 we explain this diagrammatically. Here $P_m$ is the open market price, which is too low for the producers to earn a reasonable profit and too high for the consumers to satisfy their food requirements. Therefore, the government intervenes in the market. It purchases grains from the farmer at price $p_c$ which is greater than $P_m$ (therefore $p_c - P_m$ is the subsidy to the producers). Subsequently, the grains are sold at price $p_i$ through fair price shops which is less than $P_m$ (therefore $P_m - p_i$ is the subsidy given to the consumers). The total subsidy given per unit of crop is thus the difference between the procurement price ($p_c$) and issue price ($p_i$), i.e., $(p_c - p_i)$.

The situation depicted in the figure is, however, an ideal one which need not always be held. In recent years, an anomalous situation has developed in our country where market price is lower than the issue price.

The government intervention in the prices of agricultural products is not limited to foodgrains only. Cotton, jute and other produce also are protected through the Minimum Support Price scheme. For products which are of non-food nature, various agencies like the CCI (Cotton Corporation of India), JCI (Jute Corporation of India) and Tobacco Board intervene in the market to ensure that the prices harm neither the producer nor the buyer.

Apart from the issue of relative distribution between the producer and the consumer, agricultural pricing policy should also consider the distribution of gains between the producers of various regions. Setting of higher prices in a particular region or for a crop makes the producers of that region and crop better off than the rest. Therefore, the producers of other crops may shift to the production of that particularly remunerative crop. Higher procurement prices in a particular region also results in grievances...
among the producers of the same crop in other regions. The regulatory authorities should keep all this in mind while designing the prices. In India since most of the foodgrains procurement is undertaken in Punjab, Haryana and western Uttar Pradesh, the surplus producers from other states such as Andhra Pradesh, Maharashtra and Karnataka often feel that they are not being treated fairly.

**19.3.3 Price Stability**

We have noted above that the small farmers are adversely affected if there is uncertainty regarding the prices that they are going to receive for their products. If the prices are higher than what is necessary to earn a minimum profit level then the producers earn more than their expectation. If, on the other hand, prices fall below the level at which a minimum profit level can be maintained then the small farmers are affected very badly. Since they are often dependent on the loans to carry out their production such depression in the prices leave them bankrupt. Therefore, the pricing authorities not only have to provide a remunerative price to the producers but also it should be stable and consistent. It is a fact that stability in the procurement prices often has a stabilizing influence on the open market price. Stability of prices also reduces the uncertainty on the part of the producers to make future plans regarding investments, employments, etc.

**Check Your Progress 2**

1) Enumerate the main objectives of agriculture price policy.

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2) Through the minimum support price policy government gives subsidy only to the consumers of agriculture produce. True or false?

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3) Should issue price be higher than market price? Comment.

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**19.4 THE COMMISSION FOR AGRICULTURAL COSTS AND PRICES**

In 1965 the Government of India constituted the Agricultural Prices Commission. The commission was to advise the government on “the price policy of agricultural...
commodities with a view to evolving a balanced and integrated price structure in the perspective of the overall needs of the economy and with due regard to the interests of the producers and the consumers”. While recommending the price policy and relative price structure the commission was enjoined to keep in view among other things, “the need to provide incentive to the producer for adopting improved technology and for maximizing production and the likely effect of the price policy on the rest of the economy, particularly on the cost of living, on wages, industrial cost structure, etc.”

It is evident that various policy statements do not show any indication to deliberately keep farm prices low, though the need to protect the consumers from the consequences of an inordinate rise in prices has been kept in view. It has been made clear that the concern for consumer interests should not be allowed to take away the farmer’s incentive to adopt improved technology and make necessary investments for the purpose.

But this is as far as the policy goes on paper. Operationally there has been failure more in respect of curbing the inflationary pressure on prices than in maintaining what may be termed as incentive level of prices. The minimum support prices (MSP) set by the commission was always set at a lower level then the procurement prices. Thus MSP was meaningless because the Food Corporation of India always procured necessary articles at procurement prices. In fact procurement operation by the government many a time led to a price rise in the open market. Many state governments sought to protect the consumers by setting an upper limit to the price level but these were never implemented properly. In the years following 1965, severe food crisis due to drought resulted in many parts of the country. Starvation deaths were reported from Andhra Pradesh, Bihar, Bengal and Orissa. Food riots broke out. However, this was the time when green revolution was taking birth largely in Punjab, Haryana and Western UP. This could not have been possible without newer production technology, chemical fertilizers, HYV seeds, etc. The rising prices of agricultural articles therefore we can say, helped the green revolution. The increasing trend of agricultural prices continued till the middle of 1970s. Pricing policy of the government therefore has been more in favour of the producers than the consumers. Perhaps this prompted the government to rename Agricultural Prices Commission as Commission for Agricultural Costs and Prices (CACP) in the year 1985, the emphasis now being more on costs. The Sixth Plan (1980-85) document has the following to say about agricultural prices,

“Prices of agricultural commodities exercise a dominant influence on the behaviour of the overall or general price level. Agriculture accounts for nearly half of the national income…Past experience suggests that relative stability in general price level has more often coincided with years of good harvest and, on the other hand, the inflationary pressure have more often been triggered by a fall in agricultural output and consequent rise in agricultural prices. Agricultural production strategies in the Sixth Plan should hence be based on the need for increasing the production of commodities in short supply and thereby helping to maintain price stability.”

The Seventh Plan (1985-90) document has the following to say on agricultural price policy:

“Whereas the use of high yielding varieties aided by incentive prices and public procurement have contributed to a break-through in the output of certain crops, notably wheat, they have also led to the creation of surpluses which cannot readily be absorbed while shortages persist in respect of certain other commodities. Agricultural price policy needs to be increasingly concerned with the maintenance of a scale of appropriate relative prices of crops so that the supplies of different commodities are brought in line with the respective demands. Also procurement operations have to be
Issues Before Agricultural Development

strengthened for crops like rice, oilseeds and pulses in areas inadequately served with marketing infrastructure, to ensure that the producers are in fact able to sell at prices fixed by the government.”

Table 19.1: Procurement / Minimum Support Prices for Agricultural Commodities
(as on 12.2.2001)

(Rs. per quintal)

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<tbody>
<tr>
<td>Paddy</td>
<td>360.00</td>
<td>380.00</td>
<td>415.00</td>
<td>440.00</td>
<td>490.00 (11.4)</td>
<td>510.00 (4.1)</td>
</tr>
<tr>
<td>Jowar</td>
<td>300.00</td>
<td>310.00</td>
<td>360.00</td>
<td>390.00</td>
<td>415.00 (6.4)</td>
<td>445.00 (7.2)</td>
</tr>
<tr>
<td>Bajra</td>
<td>300.00</td>
<td>310.00</td>
<td>360.00</td>
<td>390.00</td>
<td>415.00 (6.4)</td>
<td>445.00 (7.2)</td>
</tr>
<tr>
<td>Maize</td>
<td>310.00</td>
<td>320.00</td>
<td>360.00</td>
<td>390.00</td>
<td>415.00 (6.4)</td>
<td>445.00 (7.2)</td>
</tr>
<tr>
<td>Ragi</td>
<td>300.00</td>
<td>310.00</td>
<td>360.00</td>
<td>390.00</td>
<td>415.00 (6.4)</td>
<td>445.00 (7.2)</td>
</tr>
<tr>
<td>Wheat</td>
<td>380.00</td>
<td>475.00 (25.0)</td>
<td>510.00 (7.4)</td>
<td>550.00 (7.8)</td>
<td>580.00 (5.5)</td>
<td></td>
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<tr>
<td>Barley</td>
<td>295.00</td>
<td>305.00</td>
<td>350.00</td>
<td>385.00</td>
<td>430.00 (11.7)</td>
<td></td>
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<tr>
<td>Tur (Arhar)</td>
<td>800.00 (5.3)</td>
<td>840.00 (5.0)</td>
<td>900.00 (7.1)</td>
<td>960.00 (6.7)</td>
<td>1105 (15.1)</td>
<td>1200 (8.6)</td>
</tr>
<tr>
<td>Moong</td>
<td>800.00 (5.3)</td>
<td>840.00 (5.0)</td>
<td>900.00 (7.1)</td>
<td>960.00 (6.7)</td>
<td>1105 (15.1)</td>
<td>1200 (8.6)</td>
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<tr>
<td>Urad</td>
<td>800.00 (5.3)</td>
<td>840.00 (5.0)</td>
<td>900.00 (7.1)</td>
<td>960.00 (6.7)</td>
<td>1105 (15.1)</td>
<td>1200 (8.6)</td>
</tr>
<tr>
<td>Gram</td>
<td>700.00 (4.5)</td>
<td>740.00 (5.7)</td>
<td>815.00 (10.1)</td>
<td>895.00 (9.8)</td>
<td>1015 (13.4)</td>
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</tr>
<tr>
<td>Groundnut-in-shell</td>
<td>900.00 (4.7)</td>
<td>920.00 (2.2)</td>
<td>980.00 (6.5)</td>
<td>1040.00 (6.1)</td>
<td>1155 (11.1)</td>
<td>1220 (5.6)</td>
</tr>
<tr>
<td>Soyabean Black</td>
<td>600.00 (5.3)</td>
<td>620.00 (3.3)</td>
<td>670.00 (8.1)</td>
<td>705.00 (5.2)</td>
<td>755 (7.1)</td>
<td>775</td>
</tr>
<tr>
<td>Soyabean Yellow</td>
<td>680.00 (4.6)</td>
<td>700.00 (2.9)</td>
<td>750.00 (7.1)</td>
<td>795.00 (6.0)</td>
<td>845 (6.3)</td>
<td>865 (2.4)</td>
</tr>
<tr>
<td>Sunflower seed</td>
<td>950.00 (5.6)</td>
<td>960.00 (1.1)</td>
<td>1000 (4.2)</td>
<td>1060 (6.0)</td>
<td>1155 (9.0)</td>
<td>1170 (1.3)</td>
</tr>
<tr>
<td>Rape &amp; Mustard</td>
<td>860.00 (3.6)</td>
<td>890.00 (3.5)</td>
<td>940.00 (5.6)</td>
<td>1000 (6.4)</td>
<td>1100 (10.0)</td>
<td></td>
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<tr>
<td>Toria</td>
<td>825.00 (3.1)</td>
<td>855.00 (3.6)</td>
<td>905.00 (5.8)</td>
<td>965.00 (6.6)</td>
<td>1065 (10.4)</td>
<td></td>
</tr>
<tr>
<td>Safflower</td>
<td>800.00 (2.6)</td>
<td>830.00 (3.8)</td>
<td>910.00 (9.6)</td>
<td>990.00 (8.8)</td>
<td>1100 (11.1)</td>
<td></td>
</tr>
<tr>
<td>Cotton</td>
<td>1150 (15.0)</td>
<td>1180 (2.6)</td>
<td>1330 (12.7)</td>
<td>1440 (8.3)</td>
<td>1575 (9.4)</td>
<td>1625 (3.2)</td>
</tr>
<tr>
<td>Jute</td>
<td>490.00 (4.3)</td>
<td>510.00 (4.1)</td>
<td>570 (11.8)</td>
<td>650 (14.0)</td>
<td>750 (15.4)</td>
<td>785 (4.7)</td>
</tr>
<tr>
<td>Sugarcane</td>
<td>42.50 (8.7)</td>
<td>45.90 (8.0)</td>
<td>48.45 (5.6)</td>
<td>52.70 (8.8)</td>
<td>56.10 (6.5)</td>
<td></td>
</tr>
<tr>
<td>Tobacco (VFC) Black Soil</td>
<td>19.00 (2.7)</td>
<td>19.00 (0.0)</td>
<td>20.50 (7.9)</td>
<td>22.50 (9.8)</td>
<td>25.00 (11.1)</td>
<td>26.00 (4.0)</td>
</tr>
<tr>
<td>Light Soil (Rs per kg.)</td>
<td>21.50 (2.4)</td>
<td>22.00 (2.3)</td>
<td>23.50 (6.8)</td>
<td>25.50 (8.5)</td>
<td>27.00 (5.9)</td>
<td>28.00 (3.7)</td>
</tr>
<tr>
<td>Copra Milling</td>
<td>2500 (6.4)</td>
<td>2500 (0.0)</td>
<td>2700 (8.0)</td>
<td>2900 (7.4)</td>
<td>3100 (6.9)</td>
<td>3250 (4.8)</td>
</tr>
<tr>
<td>(For Calender Year) Ball</td>
<td>2725 (5.8)</td>
<td>2725 (0.0)</td>
<td>2925 (7.3)</td>
<td>3125 (6.8)</td>
<td>3325 (6.4)</td>
<td>3500 (5.3)</td>
</tr>
<tr>
<td>Sesamum</td>
<td>850.00 -</td>
<td>870.00 (2.4)</td>
<td>950.00 (9.2)</td>
<td>1060 (11.6)</td>
<td>1205 (13.7)</td>
<td>1300 (7.9)</td>
</tr>
<tr>
<td>Niger Seed (12.0)</td>
<td>700.00 -</td>
<td>720 (2.9)</td>
<td>800 (11.1)</td>
<td>850 (6.3)</td>
<td>915 (7.6)</td>
<td>1025</td>
</tr>
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Note: Figures in parenthesis indicate percentage increase over previous year.
The following is what the official website for information on agriculture in India says:

“The main objectives of the Government’s price policy for agricultural produce aims at ensuring remunerative prices to the growers for their produce with a view to encourage higher investment and production. Towards this end, minimum support prices for major agricultural products are announced each year which are fixed after taking into account, the recommendations of the Commission for Agricultural Costs and Prices (CACP). The CACP while recommending prices takes into account important factors, viz.

1) Cost of production
2) Changes in input prices
3) Input/Output price parity
4) Trends in market prices
5) Inter-crop price parity
6) Demand and supply situation
7) Effect on industrial cost structure
8) Effect on general price level
9) Effect on cost of living
10) International market price situation
11) Parity between prices paid and prices received by farmers (terms of trade)

Of all these factors, cost of production is the most tangible factor and it takes into account all operational and fixed costs. Government organises Price Support Scheme (PSS) of the commodities, through various public and cooperative agencies such as FCI, CCI, JCI, NAFED, Tobacco Board, etc., for which the MSPs are fixed. For commodities not covered under PSS, Government also arranges for market intervention on specific request from the States for specific quantity at a mutually agreed price. The losses, if any, are borne by the Centre and the State on a 50:50 basis. The Government have raised substantially the MSPs in recent years as may be seen from the statement enclosed.”

19.4.1 Political Economy of Procurement Prices

We have seen that though the issue of fixing procurement/minimum support prices may seem simple it is not so in reality. Since procurement price influences the terms of trade between the sectors and distribution of income, the pressure groups in the economy try to move the official procurement prices in their favour. This perhaps explains why throughout the whole span of 55 years after Independence procurement prices have been continually raised. Often it has been observed that this price is higher than the prevailing market price. Moreover, the clout of the regionally concentrated rich farmers lobby have ensured that almost the entire procurement of grains take place from the traditional green revolution area.

Since the consumers of agricultural products are not united as the producers, the latter group has been able to influence the pricing policy of the Government in their favour much more than the former.
19.4.2 Emerging Problems

Since the early 1990s, the planners of the Indian economy have more or less adhered to the directives of the IMF and the World Bank. Liberalization and globalization are the two major prescriptions of this new era. The new policy package includes cutting down subsidies and budget deficit. As we learnt earlier the price differential between the procurement price and the issue price is the subsidy that the Government provides. One way to cut this subsidy was to lower the procurement price, and the other way was to raise the issue price of the Public Distribution System (PDS).

Because of political economic problems pointed out above, lowering of procurement prices or curtailing the procurement operations could not be carried out. So the only way out was to further squeeze the ordinary consumers by raising the issue price.

In this context the government declared two issue prices: one for people above Poverty Line (APL) and another for people below Poverty Line (BPL). Price offered to the APL population were found at many a time above the market price; substandard quality food were offered as well. The food earmarked for BPL population actually never reached the target group. Identification of BPL population was fraught with corruption and mismanagement at various levels. Many a time the rich and the influential got themselves recorded as part of the BPL group and cornered the subsidies.

There has been a fall in the per capita food consumption in the last decade, increasing poverty and inequality especially in rural areas. We will discuss more about these issues in Unit 21.

Check Your Progress 3

1) Under what circumstances was the Agricultural Prices Commission set up?

2) Procurement prices have been rising consistently in the last few decades. What are the reasons?

3) What is the need for setting different prices for APL and the BPL? Has this Targeted Public Distribution System benefited the country?
19.5 LET US SUM UP

We have seen that agricultural prices play a major role in a poor country where majority of the population is dependent on agriculture. It affects the overall economy mainly through two channels. First, price affects profitability of producers thus affecting the area under different crops. It affects the resource allocation by the same logic, both at the individual and the aggregate levels. Moreover, the future adoption of technologies and investment decisions are also affected by changes in prices. Second, it affects the real income of the purchasers. With this class constituting the majority in a poor country, if agricultural prices increase rapidly it adversely affects poverty and reduces demand for industrial products. Agricultural goods entering as inputs into the production of industrial goods means their prices go up as well. This leads to a fall in industrial demand and ultimately industrial output and employment.

Therefore, pricing of farm products has to be a well thought exercise and it has to maintain certain balance. However, when we look at the Indian experience we find that throughout the history of independent India the pricing policy has been more tilted in favour of the producers than consumers. Subsidies were granted to make up for the gap in procurement price and issue price but they could not keep pace with the constantly rising procurement prices. To reduce subsidies, issue prices at PDS outlets had to be raised.

In the wake of globalization and liberalization during the 1990s, these issues are moving in a newer direction. Government have been forced to cut subsidies and the result has been that whereas the rise in procurement prices and procurement operations could not be stopped due to political lobbying, it is the PDS which is being dismantled. Issue prices have risen, while PDS operation has shrunk. All these have led to falling cereal consumption, industrial recession, rising rural poverty and above all a wasteful accumulation of PDS stock.

19.6 KEY WORDS

**International Competitiveness** : This determines whether the goods or services we are talking about are capable of getting sold in the global market. It depends upon factors such as the price at which the good in question is offered for sale at the international market, its quality and trading at the global market.

**Issue Price** : The price at which goods are sold through the PDS outlets. This price is decided upon after taking into consideration things like the purchasing power of the poor, market price level and subsidy margin offered by the Government.

**Minimum Support Price (MSP)** : The MSP is fixed by the government. It indicates the minimum price level which is guaranteed to the sellers by the government. If the market price slips down below the MSP level, the government intervenes and undertakes procurement at MSP level. Earlier MSP and procurement prices were set at different levels, MSP being lower than procurement prices. However, in recent years both have been kept at equal level.
**Issues Before Agricultural Development**

**Open Market Price**: The price that is determined in the market by the interaction of demand for and supply of goods, without external intervention.

**Price Elasticity of Demand**: This measures the responsiveness of demand for a good to change in its price. Generally food has low price elasticity of demand especially for the poor people. Food being a necessity, the effect of price rise on reduction in quantity demanded is low.

**Procurement Price**: The price fixed by the Government for different crops. The government buys crop from the farmers at this price.

**Terms of Trade**: It is the ratio of prices prevailing in two sectors. For example, if agricultural price is $p_a$ and industrial price is $p_b$ then the terms of trade between the sectors would be $p_a / p_b$.

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**19.7 SOME USEFUL BOOKS**


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**19.8 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES**

**Check Your Progress 1**

1) Agricultural prices affect profitability, cropping pattern, resource allocation, income distribution, industrial output, technology and international competitiveness.

2) Increase in agricultural prices leads to high input cost. It increases price of industrial goods which reduces demand for them. It also reduces the purchasing power of consumers thus reducing demand and output of industrial goods.

3) See Sub-section 19.2.4 and answer.

**Check Your Progress 2**

1) The purpose of agricultural policy is to see that proper remuneration is ensured, income distribution is even and price stability is attained.

2) False

3) Issue price should be lower than the market price if the purpose of the government is to provide food for the poor and needy.

**Check Your Progress 3**

1) It was the food crisis period of the mid 1960s that prompted the setting up of Agricultural Prices Commission.

2) Political influence exerted by the rich farmers lobby has been one major reason.

3) Please see Sub-section 19.4.2 and answer.