The perils of deregulated imperfect agrimarkets

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The Farm Acts were legislative misadventures, while much more is needed to address the genuine fears of farmers

The eruption of massive farmers' protests across India against the Farm Acts has shocked those in the seat of power in Delhi. According to the government, many private markets will be established, middlemen would disappear, farmers would be free to sell to any buyer and farmgate prices would rise. But the protesting farmers do not accept these claims. They believe that farmgate prices would fall with the intensification of a corporate presence in agricultural markets. They also believe that the government, ultimately, wants to phase out the Minimum Support Price (MSP) system.

Let us look at the major claims and their merits. Due to space constraints, the focus here will only be on the Farmers' Produce Trade and Commerce (Promotion and Facilitation) Act, 2020 (FPTC Act).

MORE MANDIS NEEDED

An important assumption behind the FPTC Act is that mandis controlled by Agricultural Produce Marketing Committees (APMC) are monopsonies in rural areas. This assumption itself is specious. First, official data show that even for paddy and wheat, respectively, only 29% and 44% of the harvest is sold in a mandi, while 49% and 36% is sold to either a local private trader or an input dealer. In other words, de facto, a large proportion of Indian harvest is not directly sold in a mandi.

Farmers are forced to sell outside the mandis for two reasons. The first is that there are not enough mandis. In 1976, there were 4,145 large markets in India, with the average area served at 775 km2. The National Commission on Agriculture (NCA) had recommended that every Indian farmer should be able to reach a mandi in one hour by a cart. . Thus, the average area served by a mandi was to be reduced to 80 km2. For this, the number of mandis was to increase to at least 41,000. But there were only 6,630 mandis in 2019 with an average area served of 463 km2. Using another set of criteria, a government committee in 2017 had recommended that India should have at least 10,130 mandis. So, by all counts, India needs not less but more mandis.

The second reason is that most small and marginal farmers, given their small marketable surplus, do not find it economical to bear the transport costs to take their harvests to mandis. Thus, they end up selling their harvest to a village trader even if at a lower price. Even if private markets replace mandis, small and marginal farmers will continue to sell to traders in the village itself. The situation will change only if economies of scale rise substantially at the farm level.

Second, de jure too, the freedom to sell outside mandis already exists in many States. Already, 18 States have allowed the establishment of private markets outside the APMC; 19 States have allowed the direct purchase of agricultural produce from farmers; and 13 States have allowed the establishment of farmer's markets outside the APMC. Despite such legislative changes, no significant private investment has flowed in to establish private markets in these States. Private markets have emerged in some pockets for some crops, but these are by no means widespread. The reason for poor private investment in markets is the presence of high transaction costs in produce collection and aggregation. When private players try to take over the role of mandis and the village trader, they incur considerable costs in opening collection centres and for salaries, grading, storage and transport. The more the number of small and marginal farmers are, the higher will these costs be. Corporate retail chains face additional costs in urban sales and storage, as well as the risk of perishability. This is why many retail chains prefer purchasing bulk quantities of fruits and vegetables from mandis rather than directly from farmers.

TRANSACTION COSTS

Even if private markets emerge, the size of transaction costs are likely to offset any decline in mandi taxes. As a result, there is no assurance that farmers would receive a higher price in private markets. In the existing private markets too, there is no evidence of farmers receiving higher prices than in the mandis. In fact, if transaction costs exceed mandi taxes, the costs would be transferred to the farmers as a lower price. This, then, would imply a stronger squeeze on the farmer than at present Many commentaries treat taxes in mandis as wasteful. This assertion is not fully true. First, much of the mandi taxes are reinvested by APMCs to improve market infrastructure. A fall in mandi taxes would reduce the surplus available with APMCs for such investment.

Second, in States such as Punjab, the government charges a market committee fee and a rural development fee. The Punjab Mandi Board uses these revenues to construct rural roads, run medical and veterinary dispensaries, supply drinking water, improve sanitation, expand rural electrification and provide relief to farmers during calamities. Such rural investments will also be adversely affected if mandis are weakened.

THE FATE OF MSPs

Without doubt, MSPs would continue to survive on paper as the government will have to procure to maintain a minimum buffer stock. However, many policy signals point to a strategic design to weaken the MSPs.

First, input and labour costs are rising sharply in agriculture. This necessitates a regular upward revision of MSPs to keep pace with costs of living. However, MSPs are rising at a far slower rate over the past five to six years than in the past. Second, the government has not yet agreed to fix MSPs at 50% above the C2 cost of production. As a result, farmers continue to suffer a price loss of Rs 200 to Rs 500 per quintal in many crops. Third, the Commission for Agricultural Costs and Prices (CACP) has been recommending to the government that openended procurement of food grains should end. These policy stances have set alarm bells ringing among farmers.

In Punjab, Haryana and western Uttar Pradesh, most crop sales are at the MSP through procurement centres including the mandis. The farmers in these regions legitimately feel that they have been dealt a double whammy. If mandis weaken and private markets with no commitment to MSPs expand, they fear a gradual erosion of their entitlement to a remunerative price. If mandis weaken and private markets do not sufficiently replace them, they fear that the void would be filled by unscrupulous and unregulated traders. As Barbara Harriss White, a scholar of India’s agricultural markets once observed, “deregulated imperfect markets may become more, not less, imperfect than regulated imperfect markets”.

STEPS TO BE TAKEN

Discussions between the government and the farmers can be structured using a broad framework based on two focus points.

First, India needs an increase in the density of mandis, expansion of investment in mandi infrastructure and a spread of the MSP system to more regions and crops. This should happen hand in hand with a universalisation of the Public Distribution System as an affordable source of food for the poor.

Second, we need not just more mandis, but also better mandis. APMCs need internal reform to ease the entry of new players, reduce trader collusion and link them up with national retrading platforms. The introduction of unified national licences for traders and a single point levy of market fees are also steps in the right direction.

However, if we go by the Union Finance Minister's statement in November 2019, the government thinks that the APMC system has "served its purpose" and the States should "reject" and "dismantle" mandis. Such statements betray the real intent of the government, which has not missed the attention of the protesting farmers. Further, the branding of protesters as "antinational" and "Khalistanis" has only helped to further alienate the farmers from the government. The government's legislative adventurism with the Farm Bills was misplaced to begin with. . But it is never too late to rethink. Unconditional talks with farmers would be an appropriate starting point.

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