UNIT 71 – UPSC - Issues related to direct and indirect farm subsidies and minimum support prices

Any country's growth depends on agriculture advancement. It plays an important role in the economic development of nation. Almost all the activities spin around agriculture. It offers employment to around 60 per cent of the total workforce in the country (Swaminathan, 2009). In India, since many years, government provides subsidies to agriculture sector in direct and indirect form. For encouraging agriculture production and attaining self-sufficiency, the government provides various incentives together with price supporting schemes. Among the agriculture production incentives, subsidies are considered to be the most dominant device to quicken the growth of agricultural production. Most of the subsidies provided are designed to recompense the high cost of production and to stimulate the use of modern inputs. The subsidy is very important for progression of farmers in India.

It has been observed that Agriculture subsidies are one of debatable issue in world. Since many decades, every county provide huge subsidies to agriculture sector for development of agriculture sector. These actions have definitely improved the agriculture sector. But now every country tries to reduce the level of agriculture subsidies to reduce the burden on economy. Economics, expert & governments have different opinions regarding impact of agriculture subsidies. According to economics, it is detrimental to economy and it wants to reduce. Agriculture expert argued that Agriculture subsidies are really beneficial for growth of agriculture sector.

It was documented in studies that a subsidy was developed broadly in the EU and USA across the two World Wars and the Great Depression to shield domestic food production, but presently it remains important across the world. A subsidy (also recognized as a subvention) is a system of financial assistance paid to an individual, a business or an economic sector in order to accomplish certain policy objectives. This entails that any fiscal exchange which is not directly connected to paying for a service can be defined as a subsidy. Financial assistance in the form of a subsidy may come from one's national or local government, but the term subsidy may also refer to assistance granted by others, such as individuals or non-governmental institutions, although these would be more commonly described as charity.

There are two major categories of agriculture subsidies, first one is direct and another is indirect. Agricultural subsidies are funding to farmers to support their operations. Subsidies may be provided directly, in the form of cash payments, or they may take the form of indirect support. A government might offer low-cost crop insurance, for example, keep prices at an artificial level, or assist farmers in other ways.

Whenever a subsidy takes the form of a cash payment or grant to a recipient, it is characteristically considered a direct subsidy. Any non-cash benefit that a recipient receives that helps it operate or compete is regarded as an indirect subsidy. The benefit is considered to be indirect because its primary purpose may be unrelated to the recipient or not designed for the recipient alone, but provides a significant benefit to the recipient tangentially. A popular type of indirect subsidy is a change to the tax code. Governments can device tax policies that considerably decrease the tax burden for anyone who qualifies. A lawmaker may have a particular industry or constituency in mind when the law is crafted but, typically, the benefit is neutral. Governments construct tax exemptions, credits and deferrals of taxes that can affect a company's bottom line. For example, the establishment of a business empowerment zone is a type of indirect subsidy that gives businesses located in a designated low-income geographical area special tax benefits to spur the local economy. Subsidies are a feature of many government budgets, and it is a debatable matter in some regions of the world. In the case of a positive subsidy, a farmer is remunerated for growing a crop, with the money usually being based on the amount of crop being grown or the amount of the harvest. While antagonists argued that farmers are motivated not to produce a particular crop or product. For example, if milk production is extremely high, farmers might be paid subsidies not to raise dairy cows, to reduce the amount of dairy on the open market.

Basically, there are several types of Federal Farm Subsidies:

1. Direct payments. “Direct” payments are cash subsidies for producers of selected crops like wheat, corn, sorghum, barley, oats, cotton, rice, soybeans, minor oilseeds, and peanuts. Direct payments are based on a historical measure of a farm’s acreage used for production, but some payments go to owners of land that is no longer even used for farming.
2. Marketing loans. The marketing loan program is a price support program that began in the New Deal era. The program encourages overproduction by setting a price floor for crops and by reducing the price variability that would otherwise face producers in the free market. The marketing loan program covers the same crops as the direct subsidy program.
3. Insurance. When viewed internationally, the Risk Management Agency runs the USDA’s farm insurance programs, which are available to farmers to protect against adverse weather, pests, and low market prices.
4. Disaster aid. In federal system, the government operates various crop insurance and disaster assistance programs for farmers. In addition, Congress frequently declare “disasters” whenever the slightest adverse event occurs, and often distributes special payments to farmers regardless of whether they sustained substantial damage.

5. Export subsidies. The USDA operates a range of programs to aid farmers and food companies with their foreign sales.
6. Agricultural research and statistics. Most American industries fund their own research and development programs.

India has made extraordinary advances on the agricultural front during the last decades. For huge success, credit should go to the several million small farming families that form the support of Indian agriculture and economy. Policy support, production strategies, public investment in infrastructure, research and extension for crop, livestock and fisheries have considerably helped to increase food production and its availability.

The objective of subsidies, by means of creating a wedge between consumer prices and producer costs, lead to changes in demand/ supply decisions. The forms of subsidies are a cash payment to producers/consumers is an easily recognizable form of a subsidy. However, it also has many imperceptible forms. Thus, it may be hidden in reduced tax-liability, low interest government loans or government equity participation. If the government procures goods, such as food grains, at higher than market prices or if it sells as lower than market prices, subsidies are implied.

Agricultural subsidies in India:

In India, major items of agricultural subsidies are food, fertilizer, irrigation, power and credit. While food and fertilizer subsidies are borne by the Centre, power and irrigation subsidies are borne by the respective state government. Credit subsidies are given through the banking system.

Food subsidy is the difference between the price at which the Food Corporation of India (FCI) procures from farmers and sells through the Public Distribution System (PDS). The food subsidy in India was Rs.12060 crores in 2000-01 and it increased to Rs.56002 crores in 2009-10.

For fertilizer inputs, subsidy is the difference between the price paid to fertilizer manufacturers and price received from the farmers. For other inputs, it is the difference between economic cost of input and issue price to the farmers, which is paid by the government.

Credit subsidy is relevant for short term loans provided for production purpose for a period of one year. It is the difference between cost of credit and the actual interest paid by the farmers. Credit subsidy includes interest subvention and interest subsidy. In the case of Nationalised Banks interest subvention is only applicable and it is provided by the Government of India through the RBI. For the Co-operative Banks both the interest subvention and the interest subsidy is applicable and it is given through the NABARD.

To enhance the agricultural production, the Government of India is providing some other subsidies to the farmers, through the Farmers' Co-operative Societies in the form of seeds, development of oil seeds, pulses, cotton, rice, maize, crop insurance schemes and price support schemes.

In a debate, subsidies are often disparaged for their financial load. Some academics assert to the extent that these should be withdrawn in a phased manner, such a step will reduce the fiscal deficit, improve the efficiency of resources use, funds for public investment in agriculture. On the other hand, there is a fear that agriculture production and income of farmers would decline if subsidies are curtailed. These are very important issues, which need serious investigation. There are numerous issues for farm subsidies. Farm subsidies redistribute wealth. Farm subsidies transfer the earnings of taxpayers to a small group of fairly well-off farm businesses and landowners.

Farm subsidies may weaken the economy. In most industries, market prices balance supply and demand, profit levels signal investment opportunities, and entrepreneurs modernise to provide better products at lower prices. Those market mechanisms are blunted in U.S. agricultural markets. Farm programs variously result in overproduction, misuse of marginal farmland, less efficient planting, excess borrowing by farmers, inadequate attention to cost control, and less market innovation.

Farm programs are prone to scandal. Farm programs are subject to bureaucratic inefficiencies, recipient fraud, and pork-barrel politics.

It can be assessed that the agriculture subsidies are fundamental part of the farmers in India. The agriculture subsidies contribute greatly in agriculture sector in every county. Every year, government of India spends lot of money in various agriculture subsidies for growth of agriculture sector.

Minimum Support Price:

To define, minimum Support Price is the price at which government purchases crops from the farmers, whatever may be the price for the crops. Minimum Support Price is integral part of India's agricultural price policy. The minimum support prices are announced by the Government of India at the beginning of the sowing season for certain crops on the basis of the recommendations of the Commission for Agricultural Costs and Prices (CACP). Support prices normally affect farmers' decisions indirectly, regarding land allocation to crops, quantity of the crops to be produced etc. In this way, the MSP becomes a big incentive for the farmers to produce more quantity. It is reported that Based on the recommendations of the Commission for Agricultural Costs and Prices (CACP), the Department of Agriculture and Co-operation, Government of India, declares Minimum Support Price (MSP) for 24 crops under 5 groups viz. Kharif Crops, Ragi crops, Sugarcane, raw jute and copra.

The MSP was declared used first time in 1965 as a mechanism for agricultural price policy to fulfil the various objectives. Since then, the MSP performs an important function in realizing the various objectives related to agricultural price policy. MSP originally was began for the safety of farmers through a guarantee that if there produce is left unsold in the market, will be bought by the government. Another purpose was to incentivize farmer to produce more crops so as to ensure food security in India. It shields farmers from the unjustified fluctuation in prices caused by the variation in supply (largely influenced by the monsoon), lack of market integration, information asymmetry and other elements of market imperfection plaguing the agricultural markets. The guaranteed price and assured market are expected to encourage higher investment and in adoption of modern technologies in agricultural activities. Additionally, with globalization resulting in freer trade in agricultural commodities, it is important to protect farmers from the unwarranted fluctuation in prices, provoked by the international level price variations.

The MSP helps to incentivize the framers and thus ensures adequate food grains production in the country. It gives sufficient remuneration to the farmers, provides food grains supply to buffer stocks and supports the food security programme through PDS and other programmes. Support prices generally affect farmers' decisions indirectly, regarding land allocation to crops, quantity of the crops to be produced etc. the MSP becomes a big incentive for the farmers to produce more quantity.

Table: Crops covered by Minimum Support Price

Kharif Crops		**Rabi Crops**	
1	Paddy	15	Wheat
2	Jowar	16	Barley
3	Bajra	17	Gram
4	Maize	18	Masur(lentil)
5	Ragi	19	Rapeseed/Mustard
6	Arahar(Toor)	20	Safflower
7	Moong	21	Toria
8	Urad	**Other Crops**	
9	Cotton	22	Copra
10	Groundnut	23	De-husked Coconut
11	Sunflower seed	24	Jute
12	Soyabeen Black	25	Sugarcane
13	Sesamum		
14	Nigerseed		

Objectives of Minimum Support Price:

Government's agricultural policy has three important mechanisms:

- The MSP
- Buffer Stocks
- Issue of food grains through the PDS

Minimum Support Price helps to procure adequate food grains through FCI, state agencies and cooperatives. The PDS network through the policy of issue price delivers it to the weaker sections.

Minimum Support Price is price fixed by Government of India to protect the farmers against excessive fall in price during bumper production years. The minimum support prices are a guarantee price for their produce from the Government.

The objective of the MSP is to guarantee remunerative prices to the cultivators for encouraging higher investment and production. It also aims to bring a balanced realization of sufficient food production and consumption needs at the same time ensuring adequate and affordable food grains to all the people.

Minimum support price is intended to:

I. Assure remunerative and relatively stable price environment for the farmers by inducing them to increase production and thereby augment the availability of food grains.
II. Improve economic access of food to people.
III. Evolve a production pattern which is in line with overall needs of the economy.

The government decided the support prices for various agricultural commodities after taking into account the following:

- Recommendations of Commission for Agricultural Costs and Prices
- Views of State Governments
- Views of Ministries
- Other relevant factors

Minimum support price is based on economic criteria such as demand and supply situation, trends in domestic and international market prices, cost of production, inter-crop price parity, terms of trade between agriculture and non-agriculture sectors, trade policy in agriculture, effect on general price level, and so on.

The effective application of Minimum support price scheme requires a systematic administrative mechanism that includes personnel, system, infrastructure and scientific mechanism. There has to be pre and post planning for the procurement at every location so that all are aware of the activities planned and there are no delays or gaps in the system. The monitoring is also essential at every phase for the efficiency of the process and accountability of the people involved in its implementation. To have result oriented scheme, the monitoring should be scientific and effective. Every state has devised its own mechanism of monitoring based on the local requirements.

To conclude, The Minimum Support Price is significant policy of the Union Government to determine floor price of major agricultural produces every year for protecting the farmers from the brokers and fluctuating market conditions as it provides them an assured market in addition to a minimum assured return. Minimum support price for major agricultural products is fixed by the Government, each year. Minimum support price is a tool which gives guarantee to the farmers, prior to the sowing season, that a fair amount of price is fixed to their upcoming crop to encourage higher investment and production of agricultural commodities. The Minimum support price is in the nature of an assured market at a minimum guaranteed price offered by the Government.