Chapter VIII

CONCLUSION: POLITICAL ECONOMY OF AGRICULTURAL PRICE FIXATION
1. Price Policy and Agrarian Change

Even though State intervention in the market for foodgrains was initially resorted to in India as early as the Second World War, the nature of the intervention from that period until the mid-sixties was such that, as we explained in chapter I, there was no systematic attempt on a continuing basis to achieve the declared objective of the State policy. In the mid-sixties, the Government decided to enter the market for foodgrains on a regular basis and started a dual market, i.e., it procured a portion of the foodgrain marketed every season and supplementing with import, if any, sold it through the public distribution system, in addition to creating a bufferstock; that portion of the marketed output which is not procured by the Government is sold out by the private trade through the open market. This dual market in foodgrains has to be seen in the context of the changes that have taken place in the agrarian economy over the years.
If we examine the pattern of foodgrain output growth since independence, it would be seen that the highest rate of growth was already achieved somewhere around the earlier half of 1950s, as indicated by the compound growth rate of foodgrain output from 1949-50 to 1955-56 at 4.4 per cent per annum. From 1955-56 to 1961-62, the rate of growth of foodgrain output was of the order of 3.8 per cent per annum. As regards the relative contribution of area and productivity to the growth of output during the entire period from 1949-50 to 1961-62, the productivity remained constant at 1.3 per cent per annum. Therefore, whatever increase in foodgrains took place was to come from the expansion of net sown area. From the fact that the growth of foodgrain output had slowed down by the early 1960s, it appeared that the net sown area as a source of growth had already exhausted. Many observers, in this period,

1. See, C.S. Hanumantha Rao, "Agricultural Growth and Stagnation in India", Economic Weekly, February 27, 1965. The growth rates given in this paragraph are taken from Table I of this article.

2. Ibid.
were thus talking about finding new sources for increasing the growth of yield. At the same time Government was itself trying to find out some measures for increasing the foodgrain output.

We had indicated in chapter I, that the land reform legislations introduced in India in the early fifties could not reduce much of the concentration of landed property in the hands of a few, despite the fact that the per centage of area owned by the top stratum of the households with holdings above 50 acres had decreased from 15.6 per cent of the total ownership area in 1953-54 to 12.4 per cent in 1961-62. This slight reduction in the ownership area of the top stratum of


the peasantry was mainly due to the pushing out of some of the large absentee landlords. With this marginal reduction in land concentration to the extent of about 3 per cent or so, the upper stratum of the peasant households became a more or less homogeneous class. This class of prosperous farmers were found to be more responsive to the new methods of cultivation introduced by the Government from time to time. Thus, from the Community Development Programme of the early fifties and then the IADP and IAAP of the sixties, about which we had explained in detail in chapter I, these farmers made use of the advanced inputs and other methods of cultivation, and adopted commercial farming. In addition, these selected areas, where IADP etc. were introduced, could receive during the course of its implementation certain facilities, like, assured irrigation, a network of cooperative societies which would offer credit, marketing services etc. to the farmers, for the adoption of more scientific methods of cultivation. In short, by the early sixties, conditions were already created for the so called Green Revolution that took place since the mid-sixties.
However, in 1962–63, when there was a general crop failure, which resulted in a reduction of total cereals output from about 71 million tonnes in 1961–62 to 68.6 million tonnes in 1962–63, the prices of foodgrains started rising rapidly; and this rising trend in prices had not reversed, even in 1964–65 when there was a bumper harvest of about 77 million tonnes of cereals. The index number of wholesale prices of cereals (1970–71=100) at 50.1 in 1961–62 rose within three years to 67.3 per cent, i.e., by more than 35 per cent, in 1964–65. With the continuous rise in the prices of foodgrains, which are the most important wage-goods, Government felt that, if these prices were not controlled, the whole programme of industrial development that it started especially from the Second Five Year Plan would be jeopardised.\textsuperscript{5}

In short, the dual market in foodgrains was started by the Government at a time when it was faced with the problem of (i) raising the growth of foodgrain output

\textsuperscript{5} Francine R. Frankel, "India's Green Revolution : Economic Gains and Political Costs", op.cit., p.5.
through sources other than net area sown which, as we said above, had already exhausted, and (ii) safeguarding the interests of the consumers against rising market prices of foodgrains, which when attained would also help to sustain the growth of industrial production. It was a time when a class of large farmers in certain selected areas could make use of the facilities provided by the Government for advanced methods of farming and, thus, there was a tendency for capitalist agriculture to take place in India.6

2. Operation of the Dual Market System

A fundamental change that was brought about in the foodgrain market of India since the mid-sixties was, as we explained in chapter VI, to stabilise the overall market price of foodgrains through the adjustment of stocks acquired by the State, i.e., when the market price of foodgrains went up, more stocks were to be released through the public distribution system, so that the

pressure on the open market demand for foodgrains decreased and the prices prevented from going up; similarly, when the market supply of foodgrains increased relative to existing demand, say, due to a bumper harvest, the State was to take over the excess supply against a 'cost-determined' price and to build a buffer-stock, so that the producers' prices are prevented from crashing to uneconomic levels. In other words, the State intervention in the market for foodgrains was expected to keep the prices of these foodgrains stable over time, irrespective of the change in the quantity supplied through the season-to-season harvests; the prices, according to this system, was supposed to change only if there occurred a change in the cost of production, due to whatever reason.

In order to see that this particular system of dual market functioned effectively, the State sector designed two sets of producers' prices, namely, the minimum support price and the procurement price, the former to act in bumper harvest years and the latter,
in normal or bad harvest years. Thus, the minimum support price, the procurement price and the stock, in principle should maintain stability in the overall level of prices. There are, however, problems for the dual market to function as expected, principally due to the inability of the Government to divorce the issue price, at which the stock acquired by it is sold through the public distribution system, and the procurement price, at which the output sold by the cultivators is purchased by it.

Firstly, whenever the procurement price is raised, issue price also has to be raised, as the ability of the Government to subsidize the issue price and maintain it at a low level is limited by the budgetary constraints. If the Government is able to raise the budgetary resources, it should have no problem in keeping the issue prices however, even if the procurement price is raised; that is, as and when the procurement price is stepped up and the relatively richer farmers receive more money from the sales of their output, if the Government taxes a portion of that money income from them, it would get the required amount to subsidize the
issue price. In that case an increase in the procurement price would not make much of a problem for the functioning of the dual market. Moreover as we argued in chapter III, such a policy of maintaining the procurement price at a higher level, and at the same time taxing away the excess income accrued to the larger farmers, would help the relatively smaller farmers to obtain a higher return for their output and to apply some better methods of cultivation as also to improve their standard of living. But so far as the richer farmers are not taxed, the other budgetary sources of revenue, for subsidising the issue price, are taxation and deficit financing. Just as Government shows its unwillingness to tax the rural rich, it does not also use the scope of raising the level of direct taxation on the non-farm incomes, particularly of the 'non-fixed income groups' such as industrialists, traders, professionals like doctors, lawyers, chartered accountants etc. Over the years, the direct tax revenue as a percentage of total revenue to the Government had been persistently decreasing or keeping constant, while the share of indirect taxes as percentage of total
revenue had been increasing.\textsuperscript{7} Thus, it is the indirect taxation and deficit financing that the Government has to depend on, for subsidising the foodgrain issue price. However, since the indirect taxes and deficit financing tend to push up the prices of the mass consumption goods and would act as disincentive to growth of the industries which produce them,\textsuperscript{8} the budgetary resources cannot be raised through these sources to any extent (though Government has by and large increased these two items of revenue over the years) with a view to keeping down the level of issue price, whenever the procurement price is raised.\textsuperscript{3}

Secondly, the difficulty arises in the functioning of the dual market because of very nature of this system pushes the market prices upward, i.e., in the years when the supply increases in relation to demand, the prices

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\textsuperscript{7} Sec, S.L. Shetty, "Structural Retrogression in the Indian Economy Since the Mid-Sixties", Economic and Political Weekly, February 1979, (enlarged and updated reprint) Table 41, where it may be seen that direct tax revenue as percentage of total tax revenue has gone down from 35 per cent in 1952-53 to 22 per cent in 1975-76, whereas indirect tax revenue as percentage of total tax revenue has increased from 65 per cent to 78 per cent during the corresponding period.

\textsuperscript{8} Prabhat Patnaik, "Industrial Development Since Independence", Social Scientist, June 1979, p.6.
do not fall to the extent expected of the rise in supply because of the existence of a support to the price in the market, whereas in years of bad harvests the prices move upward without keeping itself stable as expected in the system of dual market. The reason for this trend, known as 'ratchet effect' in prices, is that while the minimum support price acts to an extent effectively, and prevents the prices from falling, there is no such effective ceiling to the upward movement of prices, which, under the proposed dual market, is expected to be controlled by the stock that the state acquires from the producers. In short, in the past, instead of the dual market acting as a price stabiliser, it only helped to stop the prices of foodgrains from falling but not to prevent it from rising, so that the trend of the overall prices has been on the increase.

Again, under the existing system of dual market, the choice to sell the output either to the Government or to the private trade rests, in the absence of any compulsory levy, with the producers themselves. During bumper harvest years, as there is no other option, the
producers sell their output mostly to the Government. But during bad years, when the market prices tend to move up, the producers hold back their output without selling either to the Government or to the private trade, so that the bufferstock with the Government becomes inadequate to hold the price line. This is advantageous to the producers, as the Government in such a situation is again compelled to adjust the procurement price upward in the hope of attracting some stocks for the public distribution system. Had there been a compulsory levy, as we argued elsewhere, Government need not have to go on increasing the procurement price to attract the output from the producers for the maintenance of the public distribution system; on the contrary, in that case, it could have fixed a procurement price on the basis of a 'cost-plus' formula and obtained from the cultivators an assured amount of foodgrains, which could have been used to stabilize the prices, as is proposed under the dual market. In the absence of a producer levy, the Government's ability to peg the procurement price at a 'cost-plus' level and thus control the market price is limited.
Thirdly, we know that the concept of cost that is used to fix the procurement price is such that it inflates the prices for the richer segments of the cultivators and helps to shift the income distribution in their favour. That is, as we saw in part I, the cost of production estimate includes the rental value of owned land and interest on owned fixed capital in such a way that especially land rent has a built-in capacity to increase along with an increase in the procurement price. In other words, whenever the produce of land fetches a higher procurement price the value of that land goes up. The rental value of owned land for areas where there are no lease system, such as, Haryana, Punjab, etc., is estimated by taking into account the capitalised value of land. Thus, higher the procurement price, higher the capitalised value of land and, therefore, higher the land rent, and so on. Because of this system of procurement price fixation, the return over cost of production of the richer farmers, who could adopt land-augmenting, cost-reducing methods of cultivation, had remained relatively higher from
the mid-sixties almost up to 1974-75, and helped to provide a shift in income distribution in favour of these richer farmers.

Since the Government is unable to divorce the issue price from the procurement price, the higher profit margin included in the procurement price for the richer farmers gets reflected in the issue price. It is well-known that, the public distribution system covers mostly the urban consumers, except in certain states like Kerala where the rural consumers are also brought under the net work of controlled foodgrain distribution. But, wherever there is public distribution system, it only partially fulfills the foodgrain requirements of those who are covered under the system. For the remaining part, these consumers have to depend on the open market where the price is higher than the issue price because, apart from other reasons, issue price is subsidised while the open

9. Some others have argued that when there is an increase in the farmers' income through a price rise for their output, it would result in an overall demand for foodgrains, thus leading to an increase in the foodgrain prices. For example, (i) T.N. Krishnan, "The Marketed Surplus of Foodgrains", Economic Weekly, February, 1965; (ii) Kalpana Bardhan, "A Note on Price Elasticity of Demand for Foodgrains in a Peasant Economy", Oxford Economic Papers, March 1969; and (iii) Sukhanoy Chakravarty, "Reflections on the Growth Process of Indian Economy", in Charan D. Wadhwa (ed.), Some Problems of India's Economic Policy, (New Delhi: MacGraw Hill, 1977).
market price is not. Thus, wherever the procurement price favours the income distribution in favour of the rural rich, it pushes up the issue price, to the extent that it is not subsidised, as also the open market price, and affects the purchasing power of the rural poor and the urban workers and salariat.

3. Macro-distributive Implication of Procurement Prices

Though the procurement price offered by the Government until almost 1974-75 contained a higher profit margin for the rural rich, and shifted the overall income distribution in their favour, the same could not be continued further because of other developments which took place by then. The international oil crisis of 1973, for example, resulted in a very sharp rise in the prices of fertilizers in India from 1974 onwards, as about 40 per cent of the total domestic requirements of these fertilizers is met from imports.
Until then the Government was supplying the chemical fertilizers to the cultivators at subsidised rates, with the intention of helping them to sustain the growth of output that they already achieved. It is well-known that use of fertilizers should be followed by complementary inputs like assured water supply, pesticide and weedicides, and so on and therefore only those cultivators who can afford to use all these complementary inputs are in a position to benefit from the subsidised distribution of fertilizers. ¹⁰ On this basis, we can presume that the fertilizers distributed by the Government at the subsidised pool issue price have mostly helped those farmers who have been provided with a higher profit margin in the procurement price, i.e., the relatively richer farmers.

When the international oil crisis aggravated the domestic fertilizer prices in 1974, the Government could not further reduce the pool issue price of

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fertilizers through additional subsidy and maintain the profit margin to the rural rich in their procurement price because, by then, due to the ranging inflation of the 1972-74, the rural and urban consumers had already been squeezed of their income and purchasing power. A further increase in the latter's economic burden by an attempt to maintain the profit margin of the rural rich would have worsened their position further. Even otherwise, as we mentioned in the previous chapter, by this time, urban unrest against the growing burden of the workers and salariat was already appearing. We cannot go in detail in the limited space of this chapter about these developments, but it would be relevant to mention here that inflation hits first the poorer segment of the economy like the agricultural wage labour, urban workers and the salariat. But the rural labour being generally illiterate and unorganised, do not show their growing economic difficulties through mass movements. It is quite often the vocal sections among the poor, namely, the urban workers and salariat, who show their protests through organised action. It is well-known
that such protests had been taking place in India, coinciding with the international oil crisis, which were indicated by the railway employees' strikes in 1974, the political alienation of the ruling party as evidenced by the results of some state elections, and so on.

Against such growing discontent of the common mass, Government had to lower, from 1975-76 onwards, the level of procurement price (not in absolute terms, but in relative terms, i.e., the procurement price relative to cost of production) which, we saw from our data in chapter VI, remained higher from 1967-68 to almost up to 1974-75, and then gradually declined from 1975-76 until the close of the 1970s, when there appeared a tendency for the profit margin included in procurement price to again rise.

But, from the mid-seventies, when the Government started reducing the profit margin of the rural rich, it has been argued\(^\text{11}\) that, even a portion of the increased

\(^{11}\) K.N. Raj, "Dharm Narain Memorial Lecture", \textit{op.cit}.
costs of production of these farmers had been left uncovered in the procurement price, which, in turn, was ascribed to the relative stagnation of foodgrain production during this period. Further, that was why during the latter half of the seventies there were a large number of farmers' agitations in different parts of the rural countryside against the low prices offered by the Government for their output. These agitations were started essentially by the landlords and capitalist farmers. As the large farmers produce generally for the market, their agitation could be understood in the light of an unremunerative procurement price or the procurement price with reduced margin of profit offered from the mid-seventies.

However, it is a well-known fact that, apart from the rural rich who essentially started these agitations, the small and middle farmers also had participated in these agitations. The latter category of farmers are generally known as subsistence farmers. While the output produced by the small farmers would not be sufficient.
enough to meet their round the year requirement, the output produced by the middle peasants, on an average for the good and bad years taken together, would be just sufficient enough for their annual consumption requirement. Even though very little is known about the actual market participating of this section of the peasant households, it is commonly held that they do sell a portion of their output immediately after the harvest and then `buy-back' in the latter part of the season. We have seen in chapter V that these small farmers' costs of production, according to official concept of cost-C, which includes wages imputed at market rates for the use of family labour, remain higher than the average cost of production. We also observed in chapter VI, with the help of FMS costs for some years from 1966-67 to 1969-70, that when the procurement price provided a relatively larger return over average cost of production more than one-third of the households cultivating wheat and about three-fourths of the households cultivating paddy could not obtain their material cost plus subsistence charges from the procurement prices, and that these cultivating households were relatively smaller peasants.
It indicates from this that, from the mid-seventies when the procurement price failed to protect the 'full-cost' of even those rich farmers who generally have less than average costs, the material costs plus subsistence of these small and middle peasants might have further left uncovered in the procurement price. Many observers who have been associated with kisan movements in India for long years have also pointed out about the growing misery of the small peasants which has led them to join these agitation.  

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4. Political Economy of Procurement

Price Fixation

From the above, some important conclusions can be drawn about the political economy of procurement price fixation.

Firstly, maintenance of the growth of foodgrain output in an economy like India is predicted upon the behaviour of a stratum of relatively large farmers.

Their use of productivity-raising inputs like chemical fertilizers depends upon the profitability of the output that they grow on the land. If the State decides to maintain the growth of foodgrain output and thus assures a relatively high profit margin in the produce of the larger farmers, then, the macro-distribution of a given income at any given time implies a shift in this income in favour of these large farmers on the one hand, and a squeeze on the poorer segments of the economy, like, the rural proletariat, urban workers and salariat. If there is a flexible system of taxation which can take away the excess surplus with the larger farmers, then, the squeeze on the consumers could be reduced. So far as such a system of taxation on the rural rich is not in existence, the squeeze on the consumers becomes inevitable to a large extent. That was why at a time when the Government decided to maintain the high profit margin of the rural rich, without supported by taxation, that the private economic surplus in real term rose.

and enabled the rural rich to invest productively or in inventories; and the latter, to the extent that it was resorted to, further added to the squeeze on the consumers.

If the Government decides to maintain foodgrain output growth and provides them a higher profit margin in the procurement prices, but does not tax the rich farmers and, at the same time maintains the standard of consumption of the rural and urban poor, then, the decision to maintain the foodgrain output growth through the provision of higher profit margin should be at the expense of the industrial capitalists, whose profit margin should be squeezed. Even if in the short-run, the industrial capitalists try to maintain their profit by adding their output to the inventories or by expanding the utilised capacities, in the long-run it would mean industrial stagnation.

Secondly, suppose the state is able to work out an acceptable configuration of the macro-distribution and succeeds in reconciling the competing claims of the
different sections in the economy, namely, the industrial capitalists, the workers and salariat, and the rural rich, then, there is the problem of external disturbance, like the oil crisis that led to the fertilizer price hike in India, about which we mentioned earlier. Since the Government has no control over the external economic developments, such disturbances have to be 'domestically' tackled. Thus, suppose the Government decides to contain the 'imported inflation' and, say, for this purpose the profit margin of the industrial capitalists is squeezed; then, industry stagnates; if the profit margin of the rural rich is squeezed, then agriculture stagnates; and, if the workers and salariat are squeezed, then, they protest and it costs the Government politically. In short, whatever way the State attempts to maintain the dual market within the existing framework of the economic system there are possibilities to arise problem for the State.