

## Minimum Support Price

5.37 Keeping in view the interests of the farmers as also the need for self reliance, Government has been announcing Minimum Support Prices (MSP) for 24 major crops: paddy, wheat, jowar, bajra, maize, ragi, pulses, oilseeds, copra, cotton, jute, sugarcane and tobacco (see Box 5.3). Farmers are free to sell their produce in the open market or to the Government at the MSP, depending on what is more advantageous to them. CACP recommends MSP for these agricultural products. (Box 5.4) MSP of wheat and paddy and the increase in the MSP over the years is given in Table 5.11. Keeping in view the hardships suffered by the farmers due to this year's drought, a one time special drought relief of Rs.20 per quintal was announced in the case of paddy over and above the existing MSP for the purpose of procurement.

5.38 Government follows an open ended procurement policy and there is no procurement target. It buys whatever is offered for sale at MSP. Rice and wheat are the two principal commodities where Government's role is most pronounced. Procurement operations for other crops are carried out only when market prices fall below MSP.

5.39 In the past, till 1996-97, MSP recommended by CACP was by and large

adhered to by the Government and there were limited market distortions. Private trade played its role as long as market prices were higher than the MSP. The first major aberration occurred in 1997-98, when CACP recommended price of Rs.405 per quintal for wheat was raised by the Government to Rs.475 per quintal. During the period 1996-97 to 1999-2000, MSP of wheat was raised by Rs.170 per quintal as against the CACP recommended raise of Rs.110 per quintal. The market has not been able to absorb this additional increase of Rs.60 per quintal till today. Consequently market prices of wheat even today are ruling below the MSP (Rs.620) in major producing states.

5.40 State taxes at 11 percent of MSP in major procuring states of Punjab and Haryana push up FCI's economic cost and consequently the food subsidy bill of the Government. Andhra Pradesh levies 10 percent tax on rice MSP.

5.41 Substantial increases in MSP of rice and wheat and the system of open ended procurement have resulted in two problems. Firstly, increases in the MSP much above the cost of production in the efficient states such as Punjab and some regions of Haryana and UP have caused farmers to divert more land for production of rice and wheat from coarse grains, cotton and oilseeds. Consequently,

### Box 5.3 : Minimum Support Prices : A historical perspective

The Price Support Policy of the Government is directed at providing insurance to agricultural producers against any sharp fall in farm prices. The minimum guaranteed prices are fixed to set a floor below which market prices cannot fall. Till the mid 1970s, Government announced two types of administered prices :

- (i) Minimum Support Prices (MSP)
- (ii) Procurement Prices

The MSPs served as the floor prices and were fixed by the Government in the nature of a long-term guarantee for investment decisions of producers, with the assurance that prices of their commodities would not be allowed to fall below the level fixed by the Government, even in the case of a bumper crop.

Procurement prices were the prices of kharif and rabi cereals at which the grain was to be domestically procured by public agencies (like the FCI) for release through PDS. It was announced soon after harvest began. Normally procurement price was lower than the open market price and higher than the MSP.

This policy of two official prices being announced continued with some variation upto 1973-74, in the case of paddy. In the case of wheat it was discontinued in 1969 and then revived in 1974-75 for one year only. Since there were too many demands for stepping up the MSP, in 1975-76, the present system was evolved in which only one set of prices was announced for paddy (and other kharif crops) and wheat being procured for buffer stock operations.

there is little scope for crop diversification, as farmers are less willing to go in for crops for which price support even if given is irrelevant given that market prices for most of the other products are higher. Procurement is done only when market prices fall below MSP.

5.42 Secondly, increased procurement has resulted in the FCI being saddled with large volume of stocks of foodgrains much above

the stipulated buffer stock norms. This has aggravated the problem of rising food subsidies, particularly buffer subsidies, which presently account for over 20 percent of the food subsidy bill. The carrying cost of these stocks is becoming unsustainable. A re-orientation of the foodgrain policy is therefore imperative. There is a need for a re-thinking on the rationale of raising the MSP of rice and wheat every year.

#### **Box 5.4 : CACP's methodology for cost calculation**

The minimum support prices for major agricultural products are announced each year after taking into account the recommendations of the Commission for Agricultural Costs and Prices(CACP). The CACP, while recommending prices takes into account all important factors including cost of production, changes in input prices, input/output price parity, trends in market prices, inter-crop price parity, demand and supply situation, parity between prices paid and prices received by farmers etc. Among these multiple factors that go into the formulation of support price policy, the cost of production is the most significant. Thus, for making the support price policy functionally meaningful, the minimum guaranteed prices ought to cover at least the reasonable cost of production in a normal agricultural season obtained from efficient farming.

The CACP analyses the cost of production data for various States in respect of various commodities in consultation with the States. After a meeting of the State Chief Ministers, the MSP/procurement prices are declared. With costs of production for the same crops varying between regions and also across farms within the same region and for different producers, the level of costs that could be accepted as a norm poses enormous difficulties.

##### **Cost concepts**

In fixing the support prices, CACP relies on the cost concept which covers all items of expenses of cultivation including in that the imputed value of inputs owned by farmers such as rental value of owned land and interest on fixed capital. Some of the important cost concepts used by CACP are the C2 and C3 costs.

##### **C2 cost**

C2 cost includes all actual expenses in cash and kind incurred in production by actual owner plus rent paid for leased land plus imputed value of family labour plus interest on value of owned capital assets (excluding land) plus rental value of owned land (net of land revenue)

##### **C3 cost**

Cost C2 + 10 percent of cost C2 to account for managerial remuneration to the farmer.

Costs of production are calculated both on a per quintal and per hectare basis. Since cost variations are large over States, CACP recommends that MSP should be considered on the basis of C2 cost. However, increases in MSP have been so substantial in case of paddy and wheat, that in most of the States MSPs are way above not only the C2 cost but the C3 cost as well. For instance, weighted average of C3 costs of eight wheat growing states is presently only Rs.532 per quintal while the weighted average of C2 cost is Rs.483 per quintal as against which CACP recommended MSP is Rs.620 per quintal. The producer subsidy at C2 cost is therefore Rs.137 per quintal (MSP minus C2 cost) and Rs.88 per quintal at C3 cost (MSP minus C3 cost).

**Table 5.11 : Minimum support/procurement price of wheat and paddy***(Rs/quintal)*

Crop year	Wheat		Paddy				
	MSP	Percent change	Common	Percent change	Fine	Super fine	Grade'A'
1992-93	330	20.0	270	17.4	280	290	-
1993-94	350	6.1	310	14.8	330	350	-
1994-95	360	2.9	340	9.7	360	380	-
1995-96	380	5.6	360	5.9	375	395	-
1996-97	475	25.0	380	5.6	395	415	-
1997-98*	510	7.4	415	9.2	-	-	455
1998-99	550	7.8	440	6.0	-	-	470
1999-00	580	5.5	490	11.4	-	-	520
2000-01	610	5.2	510	4.1	-	-	540
2001-02	620	1.6	530	3.9	-	-	560
2002-03	-	-	530\$	0.0\$	-	-	560\$

For MSP of Other crops, see Appendix-5.5

\* Effective 1997-98, MSP is fixed for only two varieties of paddy, common and grade-A.

\$ One Time Special Drought Relief of Rs.20/- per quintal has been given in case of paddy this year over and above the existing MSP.

Source : Ministry of Agriculture.