Madras Institute of Development Studies

MIDS Occasional Policy Paper 15
Covid-19 Series
July 2020

Reforms out of Ordinances

Agriculture Markets

P.G. Babu,* A. Ganesh-Kumar,† and Chandan Kumar‡

Three recent ordinances[1] have been passed by the Government of India to spearhead agricultural market reforms to increase productivity through better price realisation and to encourage farmers to adopt contract farming for a stable income. It was a long-awaited reform in agricultural marketing, moving from oligopsony to free market, where the farmers can sell their produce anywhere to anyone. The concept of 'One Nation, One Market' is opening new opportunities to the states but throwing new challenges too. These opportunities, if capitalised in the right time, will not only help Tamil Nadu to overcome the recessionary state of the economy, but will also benefit it, in the long run, to rise as a leader in the agricultural market and as an export hub for agro-products. However, that aspiration needs to be balanced against deep-rooted organisational and regulatory challenges.

[1] Essential Commodities (Amendment) Ordinance, 2020; Farmers' Produce Trade and Commerce (Promotion and Facilitation) Ordinance, 2020; Farmers (Empowerment and Protection) Agreement on Price Assurance and Farm Services Ordinance, 2020.

Opportunities: Oligopsony to a competitive market

Turning an oligopsony (many sellers and few buyers) market to a competitive (many sellers and many buyers) market will allow many players and investors to enter the market, who have, so far, been restricted due to limited permits and licences and several restrictions of regulatory nature. It will not only help farmers to realise better prices for their produce but can also take the agro-industry to the next level, if implemented with the right set of policies, regulation, and institutional support. We can, therefore, expect changes in the current market mechanism or market strategies driven by innovative ideas that can lead the market towards

* Madras Institute of Development Studies, Chennai > babu@mids.ac.in
† Indira Gandhi Institute of Development Research, Mumbai > agk@igidr.ac.in
‡ Indira Gandhi Institute of Development Research, Mumbai > chandan.igidr@gmail.com

efficiency. The origins of these changes would stem from the multilayers of competition.

Multilayers of Competition

Traditional *mandi*s vs open markets and new players

The first layer of competition will be between traditional *mandi*s (i.e., Agricultural Produce Market Committees [APMCs]) and new players or open mandis. The traditional mandis will be forced to be more efficient to survive in the business by sharing the deserved benefits with farmers. This competition can help farmers to realise better prices for their produce.

Competition among businesses and Investors

The next level of competition would be among businesses (such as large aggregators, processors, and organised retailers), investors (including local and foreign players) and others, to either enter into this market or increase their market share. This competition, with proper regulation, can help the agro-industry, food processing industry, and other allied sectors to flourish. It can also help to develop requisite infrastructure, like cold storage, storehouses, and logistics. Players can choose their field or subsector as per their expertise or business plans. It can also strengthen the interlinkages between agricultural markets and other sectors. E-platforms or innovative information technology (IT) solutions can further speed up the process of integrating or unifying the markets and sectors.

Competition among states

To harness these two levels of competition, in the 'One Nation, One Market' scenario, the next level of competition will be among states to extract the maximum benefits for their farmers and to the state economy at large. It is up to state policies to attract new regional and national market players, especially the formal sector that can improve the linkage between farmers and consumers. States will have the responsibility of enacting policies that create a level playing field for all players, including existing and potential entrants. Another important responsibility with the state would be to provide the requisite infrastructure in terms of better connectivity to farms through quality roads and land. Ease of doing business through less documentation, and fewer permissions and approvals, can smoothen and speed up the entry of new players. States would need to pay special attention to competition policies to promote healthy competition and to avoid any market capture or dominance.

First-mover advantage

Considering the nation as a single market,[2] the first-moving states can reap extra benefits by gaining a larger market share. The competition will be to attract more players to invest in the state; therefore, to gain first-mover advantage, states would need to be proactive to set the policies or framework to open and allow the market to function with market principles and the right set of regulatory policies to safeguard all stakeholders. The best part of this competition would be the limited, state fiscal commitments. It is likely to turn the competition into one of showcasing political willpower and capabilities of states rather than their fiscal strengths.

[2] We can consider the export market too for the competition among states.

Challenges

If the past is any guide, one should draw lessons from history. The success of the green revolution in India hinged on its integrated and comprehensive support from various walks of public policy, such as focused research and technology development, irrigation expansion, proper information dissemination, and requisite rural infrastructure development. Similarly, harnessing this opportunity and taking the first-mover advantage will hinge on a state's multidimensional actions. A state is likely to face three major challenges while designing plans and the policy framework—right incentives, appropriate regulations, and robust support system.

Comprehensive plan to targeted incentives

To attract investors, states would need to design incentive schemes. The challenge is to design targeted incentives that match with its objectives or plan for the sector. For instance, if the objective is to fetch maximum investment into a particular sector or region, then the progressive incentive scheme would be appropriate, where larger the investment, greater the incentive. But if the objective is to bring investment into a specific subsector or region, then the incentives can be targeted towards that subsector or region to fulfil the objective. It, therefore, is necessary to draw a long-term plan and strategy to develop the market, and accordingly design incentives aligned with the comprehensive plan.

Regulatory framework for markets, information, contract farming, environment, and food safety

Formulating an appropriate regulatory framework is a challenging task, where a lot of careful deliberations over conflicting ambitions are needed to articulate suitable and transparent regulations for society.

Markets

The key to market regulation is to encourage competition, with level playing field for both new and existing players, including state agricultural agencies and marketing boards that currently are instruments of state intervention in agricultural markets for specific commodities. As part of bringing in a level playing field, it is critical to stop, or at least limit, the preferential treatment that state agencies and marketing boards receive, such as easy access to cheaper credit and the right to procure at government-announced prices (in contrast to market determined prices). Bringing in reforms in this would be challenging due to, among others, political economy considerations—the organised and unionised workforce in the state agencies would resist these changes that erode their privileged position.

Regulation should not only promote competition but also allow the enterprises to achieve economies of scale to scale up the operations in order to compete in the national market as well as sustain their exports to the world market. Competition without appropriate regulation, however, can take a distorted form, which may not be ideal for society. Another serious challenge for regulatory framework would be to avoid, or at least limit, the corporatisation of agriculture, where a few large corporations can influence the market in their favour at the cost of farmers.

A plausible perspective that might fit Covid-19 scenario can be gleaned from Edmund Phelps' (2013) work on 'mass flourishing'. Among the many ideas that he puts forth, two stand out starkly—corporatism and flourishing. He argues that 'modern corporatism' is founded on the idea that national governments ought to provide benefits in the form of tax exemptions or grants or merely free service to groups that are better able to organise themselves, such as corporations, unions, or select consumer groups (Phelps, 2016). This further aggravates the initial lack of inclusion of the less advantaged who have limited access to jobs that provide them 'self-respect' in terms of the nature and dignity of work and pay.

Edmund S. Phelps. 2013. *Mass flourishing: How grassroots innovation created jobs, challenge, and change.* Princeton University Press.

Edmund S. Phelps. 2016. What is wrong with the West's economies? *Homo Oeconomicus, 33*(1–2), 3–10.

Flourishing too has a philosophical origin in the notion of 'good life' which, according to Phelps, is an experience that deeply involves employing one's imagination and creativity in finding new ways to produce or new things to produce. In short, it is 'the experience of using one's mind' irrespective of social class. Green revolution in India is, perhaps, an example of mass flourishing that created 'a "good-enough" economy' with 'high-enough wages, low-enough unemployment and wide-enough access to engaging work' (Phelps, 2016, p. 6), which the proposed agricultural reforms could aspire to.

Information

The smooth functioning of a market relies on seamless availability of information, that is, symmetric information. Any constraints to information sharing or availability can result in market failures that, in turn, can lead to market abuse by the players who possess the information, that is, a case of asymmetric information. The success of green revolution in India can partially be credited to the comprehensive strategy of information dissemination (through various communication channels, such as television, radio, and local media) among the stakeholders, particularly the farmers (Varshney, 1995). On the other hand, failures in information diffusion of the expected benefits and potential pitfalls of Bt cotton variety became problematic in Maharashtra and Andhra Pradesh (including parts of current Telangana) (Sahai, 2002), where several farmers, under pressure of huge credit burdens and heavy losses due to ill-informed decisions about the Bt cotton crop, were left with no choice but to end their lives (Gruère & Sengupta, 2011; Stone 2011). The proponents of Bt cotton, however, argued that spurious seeds sold in the black market (that has grown rapidly due to initial high prices of Bt cotton seeds) were responsible for crop failure; insufficient information about the increasing number of seed varieties further confused the farmers (Gruère & Sengupta, 2011; Herring, 2007). The Bt cotton saga highlights the crucial role of information for successful policy implementation.

Ashutosh Varshney. 1995. *Democracy, development, and the countryside: Urban-rural struggles in India*. Cambridge University Press.

Suman Sahai. 2002. Bt cotton: Confusion prevails. *Economic and Political Weekly*, *37*(21), 1973–1974.

Guillaume Gruère & Debdatta Sengupta. 2011. Bt cotton and farmer suicides in India: An evidence-based assessment. *The Journal of Development Studies*, *47*(2), 316–337.

Glenn Davis Stone. 2011. Field versus farm in Warangal: Bt cotton, higher yields, and larger questions. *World Development*, *39*(3), 387–398.

Ronald J. Herring. 2007. Stealth seeds: Bioproperty, biosafety, biopolitics. *The Journal of Development Studies*, *43*(1), 130–157.

Moreover, any market transaction involves information search, which is a part of transaction costs; hence ease of information accessibility is key to reduce transaction costs. If farmers can access information at the least cost, it will help them to reap more benefits, by minimising their transaction cost. Therefore, the state government needs to put extra efforts to create regulatory institutions to make information available easily and cost-effectively. E-platforms, e-markets, and other innovative IT solutions could be instrumental to fill this gap in the digital era, with the penetration of mobile telephony increasing among farmers. Information through digital platforms, if unchecked, however, can also result in mushrooming of information providers that, in turn, will bring the problem of plenty. Therefore, a heeding regulation or supervision by the state would be necessary to maintain the balance between information providers and seekers and to have a set of credible sources of information.

Contract farming

The current reforms through the third ordinance legalises and stresses contract farming. The regulation of contract farming through a state-level authority would be the state government's responsibility. The contracting agencies are usually organised and large entities, whereas the farmers are engaged in individual capacity with limited knowledge, human resources, and contracting experience; hence, it is difficult for the farmers—both individually and collectively—to match the bargaining power of the larger contracting agencies. Moreover, if unchecked, there is a possibility of cartelisation of formal or bigger players, which can distort and skew the distribution of benefits, against the contracting farmers. Therefore, the government needs to put extra effort into contract farming regulation to encourage balance on both sides.

Studies on contract farming in India highlight the success in terms of risk-free farming and stable income for farmers, where the contracting company (for instance, Pepsico, which procures potatoes through contract farming) buys the final produce at predetermined prices and procures at the farm gate, along with providing additional services, such as farm and crop inputs, technology and knowledge transfer, credit facility, and insurance for the crop (Dutta, Dutta, & Sengupta, 2016). The literature, however, cautions about these positive outcomes based on overlooked or missing aspects of contract farming. Evidence suggests that contract farming has, so far, mostly remained restricted to medium and large farms in India; the majority of the farming community—small and marginal farmers—have not been able to take advantage of contract farming (Singh, 2002). It also highlights the complex nature of power equations within rural society, which exacerbates the inequality within the farming community, through the unequal distribution of benefits of contract farming (Vicol, 2017). These issues need to be addressed through a thoughtful regulation framework in order to have larger economic and social impact.

Aloy Dutta, Avijan Dutta, & Suchismitaa Sengupta. 2016. A case study of Pepsico contract Farming for potatoes. *IOSR Journal of Business and Management*, 75–85.

Sukhpal Singh. 2002. Contracting out solutions: Political economy of contract farming in the Indian Punjab. *World Development*, *30*(9), 1621–1638.

Mark Vicol. 2017. Is contract farming an inclusive alternative to land grabbing? The case of potato contract farming in Maharashtra, India. *Geoforum*, *85*(Oct), 157–166.

A diverse support system would need to be devised covering various aspects related to contract farming. Contract farming may be a new concept for many farmers; hence, they may be reluctant to adopt it even if it could be more remunerative and provide them stable income. A helpline or authority could help to prepare farmers to understand contract farming and their obligations to honour the contracts as well as comply with routine procedures of inspection, completion formalities, and so on. Also, such neutral agencies should help farmers to learn how to choose the right partner among many options. To enhance awareness—about the benefits and pitfalls of contract farming—among farmers (and even traders), the state may follow a mission or campaign mode for wider dissemination.

Once contract farming is in practice, the next challenge would be efficient and effective contract enforcement. The role of a third party in contract enforcement is widely acknowledged in contract theory literature. A government organisation or authority can play the role of third party to verify or standardise quality parameters for easy authentication or verification of quality and other parameters in order to reduce the likelihood of disputes. For instance, invoking the clause of force majeure due to untimely rain or pest attack would need verification or certification from the third party. Therefore, a well-trained, resourceful, and adequately powerful, independent third-party institution would be needed.

Even with the well-engineered contract enforcement system, disputes arising out of contracts are difficult to avoid. It leads to the challenge of creating a robust dispute resolution system that can resolve disputes within a stipulated period and with cost-economising effort. The proximity of such redressal system to the farmers and other stakeholders can create long-term benefits.

Environmental safeguards

While increased competition can bring several advantages to farmers and consumers, unbridled and unregulated competition can play havoc on natural resources if traders, private processors, and farmers aggressively pursue short-run profits at the cost of long-run resource sustainable farm practices. The experience of aquaculture cultivation in parts of Tamil Nadu and Andhra Pradesh is a pointer in this regard (Kagoo & Rajalakshmi, 2002). Indeed, government policies of subsidising inputs, such as chemical fertilisers, water, and electricity, can also have similar adverse effects on the natural resource base required for agriculture, as seen in many of the north-west states of the country (International Food Policy Research Institute, 2007). An appropriate regulatory framework for natural resource management based on local conditions, including state input subsidy policies, should be devised by state governments to strike a balance between short-term livelihood necessities and long-run sustainability of agriculture.

I. Emerson Kagoo & N. Rajalakshmi. 2002. Environmental and social conflicts of aquaculture in Tamilnadu and Andhra Pradesh. *Journal of Social and Economic Development*, *4*(1), 13–26.

International Food Policy Research Institute. 2007, March. Withering Punjab agriculture: Can it regain its leadership? (Report).

Food safety standards and sanitary and phytosanitary measures

The discovery of the Covid-19 virus in largely unregulated food markets in Wuhan (China) as well as Tamil Nadu's experience with the Koyambedu agricultural market becoming a hotspot for the spread of the virus, bring out the importance of food safety standards, and sanitary and phytosanitary (SPS) measures. Such standards and measures cover not only the products themselves and the inputs used in their production, but also the entire food supply chain, in terms of handling, storage, processing, and transporting the product from the farm to the final consumer. India, in general, like many developing countries in south Asia and elsewhere in the world, does not have a strong regulatory framework on food safety and associated SPS measures. It is time that the country pays attention to this, as failures in this regard can have large economic costs as the pandemic and the consequent lockdown measures have shown. Tamil Nadu, which experienced this issue in one of its large agricultural markets, can take a lead and integrate food safety and SPS regulations into its framework for encouraging private sector investments in agriculture. Implementing such regulations would involve some fiscal costs, including in investments in appropriately-trained human resources, laboratories for testing, and certification of products. Such investments, however, will yield large benefits for the society at large—better health status of its citizens, and products that are in demand because they are certified to be safe both in terms of the inputs used and of handling, storage, processing, and transportation. These benefits would easily outweigh the fiscal costs involved in implementing the food safety standards and SPS measures.

Way ahead

With the new set of reforms, the oligopsony market is targeted to turn into a free competitive market. The destination of these reforms is clear (free competitive market), but the path is unknown. However, the reforms initiated so far go only halfway towards this destination. A major deterrent for greater investments and participation by private sector in agriculture in the country is the policy of public procurement at administratively announced minimum support prices (MSP), aided and implemented through an elaborate set of institutions and government agencies, both at the union and state levels. Public procurement of specific commodities (rice, wheat, etc.) at administratively-set MSP distorts the risk-return profile of various agricultural products, which in turn affects farmers' production decisions. This can raise the risks faced by potential entrants, which would curtail investments and hence not serve the purpose of ushering in greater competition in agricultural markets. It, therefore, is critical to reform the system of public procurement and MSP as has been pointed out by several studies (see for instance, Ganesh Kumar et al., 2009).

A. Ganesh Kumar, Ashok Gulati, & Ralph Cummings, Jr. 2009. Reforming foodgrains management: Achieving food security with cost-effectiveness. In Surjit Singh & V. Ratna Reddy (Eds.) *Changing contours of Asian agriculture: Essays in honour of Prof. V.S. Vyas* (pp. 475–478). Academic Foundation.

Several states—Andhra Pradesh (Rythu Bazaar), Karnataka, Maharashtra, and Tamil Nadu (Uzhavar Sandhai)—allow direct marketing by farmers of farm products, especially horticultural products, in urban centres, bypassing the APMC. These experiments have had mixed outcomes in different products and in different states. One shortcoming of these farmer markets is that they are subject to several municipality regulations that are not necessarily farmer friendly. They often lack investments, especially in preserving the shelf life of products, thereby resulting in greater wastage, the loss due to which is borne by the farmers. In many instances, these farmer markets also suffer from poor food safety practices. State governments can strengthen these markets by institutionalising them in all urban centres, facilitating easy access to credit, and having programmes to bring greater awareness about food safety standards in these farmer markets.

The evolving nature of the market always responds well to the innovation and openness of adopting new ideas. It also gives freedom to experiment. Hence, states should not hesitate to experiment and implement any idea or policy that has the potential to take the market to its destination—free competitive market. One possible option is to set up private markets, in the form of special economic zones (SEZs), closer to farms.

These SEZs can play multiple roles as an open market, aggregator of players related to agro-industry, and a supply chain logistic. These SEZs will be an alternative to traditional markets (APMCs) and hence promote competition in the market. These SEZs can also house other market players involved in the agro-industry, such as supply-chain logistic players of cold storage, warehousing, packaging, and gamma re-radiation. It will be like a one-stop solution for the agro-industry. It can help to reduce logistic efforts and costs.

Promoting such SEZs can provide deeper and wider infrastructure for the agro-industry and will further strengthen the linkages of agro-industry to other sectors. Therefore, developing a smaller SEZ in each taluk, and a bigger SEZ at district level may achieve maximum outreach to farmers as well as economies of scale for the businesses. Apart from providing basic infrastructure for SEZs, like good quality roads and land, the state will have limited fiscal commitments. The development of these SEZs can mostly be through private financing, with some initial incentives from the government. State governments may modify their policies to attract foreign direct investment and foreign players into this market.

A new journey for states: Opportunities and a new conundrum

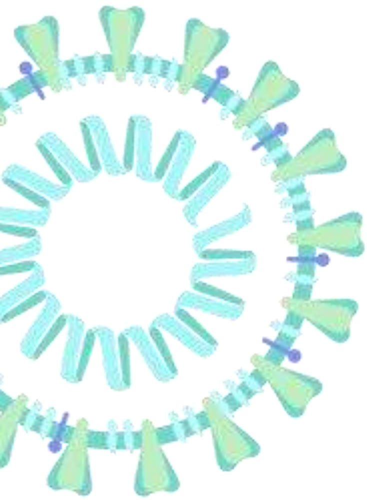
As the recent ordinances open the agricultural market and create opportunities for farmers (to sell to anyone and anywhere), businesses (to enter the market as per their choice and expertise), and the states (to go beyond their geographical boundaries for larger market share), they unleash multilayer competition in the agricultural sector. A state can take the first-mover advantage through proactive measures to benefit its farmers and to the state at large. The best part of this competition would be the limited state fiscal commitments. It is likely to turn the competition into one of showcasing the political willpower and capabilities of states rather than their fiscal strengths.

States, however, will have a new conundrum of creating the policy framework that has multiple challenges. The first challenge is to create a level playing field for all, including existing players and potential entrants. Another important responsibility with the state would be to provide the requisite infrastructure in terms of better connectivity to farms through quality roads and land. The next challenge—the most critical too—is to set the balance between buyers and sellers (i.e., businesses and farmers). The policy framework should boost competition, minimise collusion (and influence of powerful 'within state' entrenched interest groups and cartels), and safeguard the vulnerable (farmers), to minimise the chances of market abuse or market capture.

States would need to put special efforts for the formulation of planning and right incentives, and regulation of markets, information, contract farming, environment, and food safety. Designing incentive structures that match the comprehensive development plan for the sector would be crucial for sector development. Ease of information accessibility to farmers is the key to pass the benefits to farmers and reduce their transaction costs. The presence of e-platforms, e-markets, and other innovative IT solutions could be instrumental to fill this gap in the digital era. However, mushrooming of information providers can bring the problem of plenty. Similarly, contract farming has the potential to provide stable and higher incomes to farmers, but asymmetric power relations between the contracting agency and farmers need to be balanced through proper regulation and a robust support system. Private open markets in the form of SEZs could be a good starting point in the direction of competitive markets. Construction of SEZ infrastructure can generate employment and augment demand in the state economy.

Note

The current reforms are based on the three ordinances and will be valid till either one year or the final act passed by parliament, whichever is earlier. The actual law and acts are yet to be drafted and refined through public and stakeholder consultations and parliamentary scrutiny. The final act may, however, differ in rules and procedures, but it is highly likely to keep the spirit of converting the oligopsony market to a free competitive market. Therefore, opportunities remain open for states and perspective planning can reap first-mover advantages.



COVID-19 SERIES

We are in the midst of a pandemic shock as well as a deep economic recession. It necessitates extraordinary policy action. However, we do not have the luxury of time to carry out a new research plan. The situation calls for immediate reflection and action, based on available data. In the Covid-19 Series of Occasional Policy Papers, MIDS faculty contemplate on diverse issues of importance, contextualise their work to the contemporary challenge, draw attention to linkages with interrelated sectors and issues, and suggest short-to-medium–term policy measures. This series would be a useful input in the design of the state's post-pandemic socio-economic policy.

P.G. Babu

Director, MIDS

MIDS Occasional Policy Paper

No. 15 / July 2020

Covid-19 Series

Image credit: Desiree Ho for the Innovative Genomics Institute.

Madras Institute of Development Studies (MIDS) was founded in 1971 by Malcolm S. Adiseshiah. It studies development problems of India, with a special focus on Tamil Nadu. Since 1977, MIDS is a national institute funded jointly by the Government of India (through Indian Council of Social Science Research) and the Government of Tamil Nadu.

79, Second Main Road, Gandhi Nagar, Adyar,
Chennai INDIA 600020
Phone: +91 44 24411574
email: pub@mids.ac.in
www.mids.ac.in