

## AIREA MSP Note for CACP-Kharif 2013-14

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AIREA's primary mandate is to represent the interests of the Indian Rice Export Industry; our 110+ members account for 90% of India's rice exports. The farmer's CoP, the subsequent MSP set by the government and the consequent volatility in the Mandi prices affects export prices of Indian non-basmati rice, and, as such, the matter is of great significance to the rice export industry.

We gather CACP's primary concern is to maintain remunerativeness of the agricultural sector, to encourage farmers to adopt advanced farming practices and modern technology, and thereby increase productivity and overall production. We are therefore writing to highlight some issues which we hope CACP takes into consideration for the benefit of the rice industry & the wider agricultural economy.

### **Increasing the MSP would lead to over-cultivation and hence oversupply of rice.**

AIREA's key point is that the country over the next 10 years will face a different sort of agri-policy challenge – **a surplus in grains** (both rice and wheat). In this regard, the CACP also made the following observation in its previous report on Kharif Crops 2012:

“the Commission feels that if rainfall remains somewhat closer to normal in four out of five years, the chances are that India will remain surplus in cereal production during the Twelfth Plan. The challenge, therefore, is going to be more on the marketing side of it, domestic as well as exports.”

The data from last few years shows that **area under rice cultivation** has been steadily increasing, although production has in some years marginally decreased due to erratic weather conditions. From 2011 record high of 104m tonnes, India has produced around a 101m tonnes of rice in 2012-2013 and exports are expected to reach 10 million tonnes this year. **There is clearly an oversupply of rice both in the world and domestic market** and this is expected to continue in 2013, unless there is a sudden calamity due to unforeseen circumstances. At a time when we're facing an oversupply, a higher MSP would encourage more rice cultivation despite limited land and water resources, further discouraging crop diversification.

**Diversification:** If the aim is to diversify into high-yielding crops and agribusiness, government should offer MSPs for other products and maintain MSP for rice. If MSP is not enough to promote other crops then focus should be on increasing yields to make cultivation of those crops profitable and also sustainable (large quantities).

Latest supply and consumption data available from the UDSA is given below.

World Rice Production Consumption and Stocks

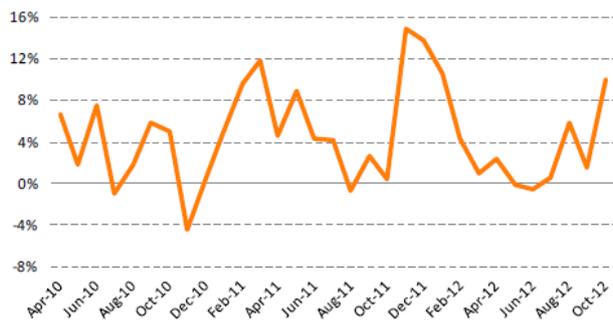
	2008/09	2009/10	2010/11	2011/12	2012/13Oct	2012/13Nov
<b>Milled Production</b>						
Bangladesh	31200	31000	31700	33700	34100	33800
Brazil	8570	7929	9300	7888	7820	7820
Burma	11200	11642	10528	10816	10750	10750
Cambodia	3992	4056	4233	4268	4500	4500
China	134330	136570	137000	140700	143000	143000
Egypt	4673	4564	3100	4250	4700	4700
India	99180	89090	95980	104320	99000	99000
Indonesia	38310	36370	35500	36500	36900	36900
Japan	8029	7711	7720	7646	7500	7500
Korea South	4843	4916	4295	4224	4300	4100
Nepal	2850	2900	2900	2900	2900	2900
Pakistan	6900	6800	5000	6500	6700	6700
Philippines	10755	9772	10539	10700	11000	11000
Thailand	19850	20260	20262	20460	21050	20500
Vietnam	24393	24993	26371	26870	26875	27100
Others	33080	35693	37280	37175	37667	37713
Subtotal	442155	434266	441708	458917	458762	457983
United States	6546	7133	7593	5868	6337	6327
World Total	448701	441399	449301	464785	465099	464310

Consumption and Residual

Bangladesh	31200	31600	32400	34300	34800	34500
Brazil	8400	8477	8200	8050	8050	8050
Burma	10800	10890	10100	10190	10380	10380
Cambodia	3220	3270	3370	3450	3590	3590
China	133000	134320	135000	139500	143500	144000
Egypt	4270	3940	3300	3620	3900	3900
India	91090	85508	90206	92320	95250	95250
Indonesia	37100	38000	39000	39550	40000	40000
Iran	3100	3150	3250	3400	3500	3500
Japan	8326	8200	8200	8050	8050	8050
Korea South	4789	4701	5175	4977	4800	4800
Nigeria	4220	4580	5030	5200	5400	5500
Philippines	13100	13125	12900	12850	12950	12950
Thailand	9500	10200	10300	10400	10600	10600
Vietnam	19000	19150	19400	19850	20100	20100
Others	50313	52561	53539	55529	56247	56432
Subtotal	433065	434606	441498	454160	464542	463831
United States	4082	4016	4317	3472	4039	4039

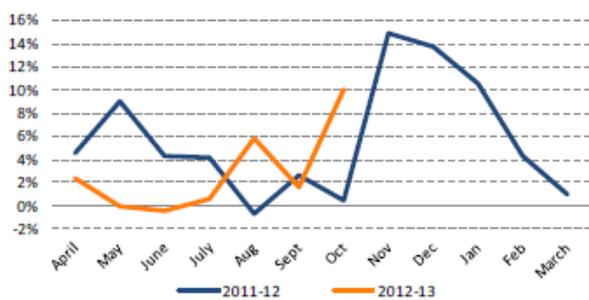
Latest economic indicators are also very encouraging. According to the **latest IIP data** for October 2012, consumer non durables (includes rice) showed robust growth at 10.1% (graphs below). **Rice has a 0.66% share in the IIP index and grew at 24.7%.**

## Year on Year Growth of consumer non-durables



Source: CSO; ICRA Analysis

Chart 6: Growth of Consumer Non-Durables



Source: CSO, ICRA Analysis

The central stocks for this quarter also exceed the buffer norms and strategic requirements as shown below. One can't stress enough on the need for adequate storage facilities. India is targeting total rice procurement of 40 million tons of rice in the year 2012-13 (October to September), up about 14.3% from around 35 million tons procured in 2011-12.

Rice stocks in the central pool as of December 1, 2012 stood at around 30.6 million tons, the highest in at least a decade and up about 13% from 27 million tons of rice in stocks during this time last year. Rice stocks at the beginning of the crop year 2012-13 in October stood at around 23.4 million tons, up about 15% than stocks of around 20.4 million tons on October 1, 2011, and about three times higher than buffer and strategic norms of 7.2 million tons for that time of the year.

### **BUFFER NORMS** w.e.f. 20.04.2005.

As on	Buffer Norms			Strategic Reserve		Grand Total
	Rice	Wheat	Total	Rice	Wheat	
1st April	122	40	162	20	30	212
1st July	98	171	269	20	30	319
1st October	52	110	162	20	30	212
1st January	118	82	200	20	30	250

As on 1.12.2012, FCI's total stocks in the central pool are as follows:

(Figs. in lakh MT)

	IN STORAGE	IN TRANSIT	TOTAL
RICE	303.30	2.77	306.07

Prepared on  
07.12.2012

**MSP & Procurement:** A study by Gahia and Kulkarni (2005) made an interesting point that MSPs have a significant positive effect on rice procurement. And with higher MSPs, off-takes will be lower as the gap between market and subsidized prices narrows down. Consequently, rice stocks will grow at an unmanageable rate putting even more pressure on our **limited storage capacity**. Further to this, lower off-takes won't be able to stop the inflationary effects of higher MSPs in rice; higher the MSP, higher the WFPI (Wholesale Food Price Index). WFPI, in turn, raises the CPIAL (Consumer Price Index for Agricultural Labour). Short-term gain to the farmer may be politically necessary but has immediate consequences for poverty and, in the long-term, distorts the market.

Input prices have been steadily appreciating. Lack of availability of farm labour and farm wages inflation, mainly due to NREGA, has contributed to rising labour costs. Due to rising food prices and sticky non-food inflation, the consumer price index (CPI) rose 9.9% in November 2012 from a year ago, marginally higher than the 9.75% clocked the previous month (October 2012). Rural and urban consumer retail inflation was 9.97% and 9.69%, respectively, in November as compared to 9.9% and 9.46%, respectively, the previous month. Diesel price hike this year has only added to headline inflation. The rupee has been constantly depreciating over the past year and the trend is expected to continue in the medium term. A higher MSP would lead to more money supply in the market continuing the vicious wage-price cycle of rural & agricultural inflation. **The MSP of paddy must take into account current inflationary scenario, while also keeping in mind the drastic cascading effect the final MSP would have on future food inflation.**

**Do Indian rice export prices affect the international market and world food security? Do we have a responsibility to the world's poor? Can we afford to tamper with India's strategic interests and international perception?** In a situation of oversupply, India's internal needs (including the poor) are secured. The larger question then is whether India has a responsibility to the world's poor? India, since last year, has been hailed as the "saviour of the world" due its relatively cheaper exports of non-basmati rice (after the ban was revoked) which halted a potential food crisis.

**Indian export prices must remain competitive to maintain India's position in the world market.** Input costs of millers and exporters will rise by roughly 20% in 2013. There is little to no flexibility in transferring the cost to importers. It is of prime importance to note that non-basmati rice is typically imported by poor and least developing nations. Additionally, the anticipated Thai flooding the market with cheaper rice in 2013-2014 will hit our industry. Our internal data suggests that countries world-over like Indonesia, Iran and Nigeria are stocking up for the next year and therefore we expect a significant drop in demand in 2013-2014. Note that Indonesia is one of the largest non-basmati rice importers. In such a scenario, Indian exporters will not be able to raise prices, and if forced to do so, we will be crowded out of the market.

At a time when India is gaining clout in world trade and geopolitics, we must be careful not to damage her image as a soft yet powerful nation. The government needs to weigh geopolitical and strategic interests before making any price or non-price intervention that would leave an indelible mark in the world food market.

CACP mentions that the price policy is also expected to “encourage rational utilization of land and water resources. In this regard, we feel that instead of levying counterproductive **export bans and inefficient tariffs** on rice millers and export houses the government must check leakages and possibly re-evaluate the efficacy of its subsidy burden. Of course, instant radical reforms via subsidy cuts are economically and politically impractical but there must be constant dialogue on the issue.

**MSP effect on Public Investment:** It is also understood that state intervention in the foodgrain market, via MSPs, leads to higher subsidies which is negatively correlated to public investment in agriculture. Higher support prices are meant to compensate low yield growth (which is incommensurate with population growth) and consequent increase in cost of production that is the result of dwindling non-price interventions through public investments. But this leads to a vicious cycle where higher MSPs (subsidies) in turn lead to dwindling public investment which again leads to higher MSPs!

Therefore, AIREA strongly believes that **non-price interventions** are imperative in the medium to long term to ensure food security for the nation as well as to cement India’s position in world rice trade. Note that India climbed to **the top position in the world market** after the non-basmati export ban was revoked and, this, was at an opportune time when Thai rice market was in doldrums due to their internal policies (rice mortgage programme). It wouldn’t be an overstatement to claim that India saved the world from a potential drought in 2012. This wouldn’t have been possible without government’s non-price policy rethink.

Investing in infrastructure and clearing up supply chain bottlenecks, easy access to rural credit for farmers, removing stocking limits on private trade, lifting unreasonable levies on rice millers, promoting uniformity in levies (Punjab at 14.5% while Madhya Pradesh at a low of 4.5%), expanding agricultural extension by promoting private and NGO involvement, reforming warehouse receipt system, and permanently opening up exports of agricultural products are some **such non-price measures**.

Non-price policy, supported by a reasonable MSP, has a critical role to play in augmenting productivity, and reducing real costs in due course. There is some evidence to show that productivity is inversely related to the cost of production which is directly related to the pricing policy of the government. According to some studies, cost of production of paddy can be brought down by about 2 percent if its yield is improved by 10 (src: CACP Price Policy for Kharif crops 2012). Increasing yields, of course, depends on non-price interventions highlighted above whereas increasing MSP would have absolutely no effect on yields and productivity.

AIREA, therefore, strongly feels that any drastic change in the MSP would be counterproductive for India’s rice exports. We sincerely hope that you consider our industry’s stand in your final recommendation.