# 25 years of tinkering in agriculture – Ashok Gulati

Part first –

**<u>1990s set of reforms and its effect on agriculture</u>**

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**Course – GE Hons.**

**Subject : INDIAN ECONOMY –II**

# Reforms

1990 was the time when our fiscal deficits was 10% , current account deficits was more than 3% , reserves was less than $1 billion and inflation rate was around 17% annually  . In view of situation of that time Indian economy went onto adopting a comprehensive reform agenda.

The 1991 policy package that ushered in economic reforms comprised primary of three components

1. Correction of exchange rate
2. Reduction in industrial tariff
3. Delicensing of a large number of industries

# Agriculture neglect

- It is notable that agriculture was never a part of this comprehensive reform agenda. In this part we will look at how the reform that was largely adopted to secure financial stability or in other words macroeconomic stability ended up providing some benefits to agriculture nevertheless.
- But before marching forward first we need to ask , how the policies prior to reforms were effecting agriculture ?
- In that context it can be said that despite significant successes like green revolution and white revolution , overarching trade and marketing policies remained restrictive and antifarmer.

# Effect of overvalued exchange rate and heavy protection to industry

- On the one hand , the country’s overvalued exchanged rate taxed its otherwise globally competitive agriculture sector , and o the other, the exceptionally high import duties on industrial commodities discriminated against the farm sector.
- According to Pursell and Gulati , on an average agriculture was discriminated against to the tune of about 20-30 percent of the value of Agri output.
- This was equivalent to an implicit tax imposed on agriculture due to overvalued exchanged rate and heavy protection to industry.

# Hypothesis

For assessing how far these reforms benefited agriculture , first we need to formulate three hypothesis which are as follows:

- One with major exchange rate adjustments agriculture must have emerged as an exportable sector and if export of agriculture gradually opened up ,though with hiccups it should reflect in improved Agri-export performance over time.
- Two , with falling tariff on industrial products , relative prices between agriculture and manufacturing sector should turn in favour of agriculture
- Third , private sector investment in agriculture if they respond to relative price should increase and improve agriculture growth rate

# Agricultural exports and imports

India’s share in global Agri exports went up from 1 percent in 1990s to 2.6 percent by 2013-14.

Overall Agri trade (export plus imports ) which was less than 5 percent of agricultural GDP (AGDP) in 1990-91 stood at almost 20 percent by 2013.

There has been some moderation in trade-in recent years of on account of two factors :Falling domestic supplies due to two consecutive droughts in 2014 and 2015 and plummeting global prices affecting India’s global competitiveness.

Despite these, country's Agri trade was still at 17.6 percent of its AGDP in FY 2016.

- Not surprisingly , India, despite being a net importer on ts overall trade account for all commodities is a net exporter of agriculture to the rest of the world.
- Overall , Indian Agri exports in FY 2014 crossed $42 billion as against imports of about $ 16 billion, giving a net trade surplus of about $26 billion. This is the highest ever trade surplus that Indian Agri trade has generated.
- In this regard , it is interesting to note the findings from Balassa index of revealed comparative advantage (RCA) which suggest that Indian agriculture outshines other sectors on a global platform.

- With higher index value of agriculture compared to manfacutring and commercial services , agriculture sector has been gaining greater competitiveness relative to other two sectors.
- For example , between 2011-2014, the RCA for M&CS was around 1.05 but for agriculture it improved from 1.06 to 1.24.
- Also in 2014 , RCA for agriculture was 1.24 wilte it for manufacturing it was 0.8 and for combined M&CS it was 1.05.
- Considering above mention changes it can be said that agriculture is gaining both across time and even within a year over other sectors in export sector.

- Back in 1990s , cereals had a share of 9% percent in Agri exports and in FY 2015 , the share of rice alone was around 20% percent.
- About 60% percent of exports in FY 2015 was comprised of rice, meat, marine products, spices and cotton.

# Relative term of trade for Indian agriculture

- Relative price index between agriculture and manufacturing sector has witnessed a secular upward trend. The index touched a low of 89 in 1993. however it has improved since then, reaching 157 by 2014-15.
- A major part of this improvement started from 2004 onward when the new government decided to reduce the gap between low domestic prices and high global agriculture prices.
- Increases in the MSPs of wheat and rice , along with several other crops became one of the conduits for this, particularly after 2007.

- The year coincided with the launch of NFSM domestically and onset of food price eruption globally.
- Thus to achieve its target of increasing domestic production by 20 MMT in next five years under NFSM and to draw parity between domestic and international prices which shot up due to global food crises of 2007-08, the government increased MSPs strategically to catch up with world prices over a three to four year period.
- This led many to ascertain aggressive hike in MSPs of wheat and rice to be behind double digit food inflation between FY 2009 & FY 2013.

- Assertion like this don’t hold much ground if we look at the historical trends in domestic prices that have over time followed their global counterparts.
- Second even after hike in MSPs of wheat and rice , Indian support prices are much lower than our global competitors such as Thailand , Philippines , china , Indonesia , Bangladesh in case of rice and china and Pakistan in case of wheat.
- Quantitative analysis done by author suggests the much of inflation can be explained due to hike in fiscal deficits , rise in real wages and rise in global prices

# Private investment in agriculture

- Capital formation in agriculture by the private sector (mainly farmers) responds , inter alia, to two things : relative incentive structure as captured in relative prices and to public sector investments in agriculture under the complementarity hypothesis.
- Year wise trends of gross capital formation in agriculture points towards two structural changes :
- One , the share private investment in overall agricultural investment increased from 50% in 1980s to 85% in 2014.
- Second , driven by private investment overall investment in agriculture went up from 10% in 1990s to 20% in 2013-2014.

# Performance of agriculture GDP

It seems that hypothesis formulated in the beginning about the effect of these indirect set of reforms turn out to be correct and positive for agriculture. Nevertheless , any discussion about the positive effect on agriculture can't be completed without looking at its effect on overall agriculture growth.

- Impact of all these factors on AGDP growth has been mixed. It grew by 4.1 percent per annum from 2007-11 up from 2.5 percent preceding ten years , 1998-2007.this period of growth maps with period that witnessed fastest reduction in poverty in the country. Not coincidently , this growth period was also precisely he time when relative prices moved inn favour of agriculture.
- This is important considering the fact that still about 53 percent of grossed area is still rainfed , which often causes higher uncertainty depending upon monsoon rains.

- Quantitative analysis done by authors suggest that around 90% variation in Agricultural GDP could be explained in three components - monsoon rainfall index , technology augmentation , relative prices for agriculture where's relative prices has the largest effect on Agricultural growth rate.
- In conclusion we can say that reforms indeed helped agriculture in promoting trade and receiving private investment but it seems that for improving growth rate of agricultural GDP strategic use of price factors has a more role to play.