

---

## Minimum Support Prices and Its Impact on Agricultural Economy

**G. Sudhakar (Ph.D) & Mr. Zeleke Wale**

Department of Business Management

Wolaita Sodo University, Ethiopia

[gsudhakar9309@gmail.com](mailto:gsudhakar9309@gmail.com), [zelewaw@gmail.com](mailto:zelewaw@gmail.com)

---

### **Abstract**

*Minimum Support Price (MSP) Policy has been one of the supportive mechanisms which were put in place during the wee years of formation of the Agricultural Price Policy. The four decades experience is significant enough to have a close review of the policy. Agricultural Price Policy and price support system have come under academic scrutiny due to the recent changes towards liberalization of the Indian economy. In a true sense, agricultural sector remained far from liberalized despite the fact that agriculture itself is a private activity. In the factor market, the farmer is at receiving end, as the factor prices are largely dictated by the suppliers of the factors of production. At the same time, in the product market, the farmers remain at the receiving end again wherein the prices are decided and dictated by the middlemen or the purchasers. The effectiveness of minimum support price (MSP) for paddy has been examined in different regions of India and its role and contribution towards production in surplus states like Punjab have been studied. Being at the cross roads from both sides and taking the worst part of the market on either side, agriculture remains at the mercy of the operators in these two markets. The study is designed with an objective to explore the effectiveness of MSP and to ascertain if the intended benefits have reached the farmers after such a long period of implementation. The constraints faced in the implementation of MSP have also been analyzed.*

---

**Keywords:** *Agricultural, Economy, Liberalization, Price, Policy, Support.*

---

### **1. INTRODUCTION**

Agricultural Price Policy plays an important role in achieving growth and equity in the Indian economy in general, and the agriculture sector in particular. The major underlying objective of the Government's Price Policy is to protect both producers and consumers. Achieving food security at both the national and household levels is one of the major challenges in India today. Currently, the Food Security System and Price Policy basically consist of three instruments: Procurement Prices/Minimum Support Prices (MSPs), Buffer Stocks and the Public Distribution System (PDS). Agricultural Price Policy is one of the important instruments in achieving food security by improving production, employment and incomes of the farmers. There is a need to provide remunerative prices for farmers in order to maintain food security and increase the incomes of farmers.

In India, the agriculture price policies and allied instruments were evolved in the pre Independence era. The procurement and distribution of major food grains were started and statutory maximum prices were fixed, but were not strictly enforced. In the post-Independence era, the objective of achieving food security was linked with environment sustainability. The objective of the Government's price policy for agri-produce is to set remunerative prices with a view to encourage higher investment and production. Though the Government decided to purchase food grains at fixed prices, if market prices fell precipitously, but till 1954 there was no sharp decline in food prices.

The demand for food grains particularly rice and wheat was on the increase from year to year as a result of growing population and rising incomes. Thus a trend had developed towards increased level of consumption as well as substitution of coarse grains like maize, jawar, etc. by wheat and rice. Consequently shortages even of a marginal nature used to persist and there was a steady upward trend in price levels to bring demand and supply into balance.

Based on the secondary data spanning from 1980-81 to 2006-07, the deviations of farm harvest prices from the MSP have been used as a measure of ineffectiveness and the impact of prices and technology on rice productivity has been examined by using the simultaneous equation model. While the MSP policy has been very effective in surplus producing states like Punjab and Andhra Pradesh, it has not been so effective in the deficit states. In Punjab, the effective implementation of the price policy has helped in improving the production and productivity of rice. Non-price factors such as use of improved varieties, availability of assured irrigation at subsidized rates and high fertilizer-use have been found to be significant determinants of growth in rice production. The study has suggested that without losing sight of the environmental concerns, the Punjab model can be used for increasing the production of rice in other potential areas of the country.

### **1.1 MINIMUM SUPPORT PRICE (MSP)**

The Commission for Agricultural Costs and Prices (CACP) recommends Minimum Support Price (MSP) for 25 agricultural crops, the most important of which are paddy, wheat, cotton, oilseeds and pulses. The MSP policy has been a matter of contention since its inception, with a general feeling that MSP favours only the food surplus regions like Punjab and Haryana states from where large stocks of grains are procured for Public Distribution System (PDS) (Chand, 2003). Also, the price policy is considered to have favoured food crops more than the other crops (Singh et al., 2002). As a result, a large chunk of good quality land was shifted from pulses, oilseeds and other important crops to paddy and wheat crops, creating a serious imbalance in the demand and supply of several other agricultural commodities (Chand, 2003). In other regions of the country, the price policy is considered to be ineffective as the government has less interest in procurement operations due to small marketable surpluses. It is therefore, argued that the market prices for wheat and paddy rule lower than the MSP in these areas during post-harvest period and shoot up during the lean periods, which is usually not the case in the surplus producing regions (ADRT, 2003).

In recent years, the MSP policy has been criticized by both farmers and proponents of free trade. Farmers always demand a substantial hike in MSP, whereas profree agricultural trade thinkers feel that, most of the times, MSP is not in line with the international prices as well as domestic demand and supply situation. This brings distortions and inefficiencies in the production patterns. Agricultural price policy has been argued to have widened the farm income inequalities also (Singh et al., 1986). It is further contended that the MSP has outlived its utility and is being used more as a political tool than an economic instrument. It therefore becomes imperative to examine the effectiveness of MSP in different regions of the country as well as its contribution towards growth. The present study has investigated these issues for the paddy crop, which is the most important cereal crop from both production and consumption points of view in the country. Since MSP policy is considered to have favoured mostly the surplus states, its role and contribution towards production was examined for the Punjab state as a case study.

### **1.2 MAKING OF THE AGRICULTURAL PRICE POLICY**

Agricultural Price Policy in India strongly emerged in the context of food scarcity and price fluctuations provoked by drought of mid-sixties and a war with Pakistan. The policy was to be framed keeping in view three different angles viz.,

- (i) Providing food grains for the Public Distribution System,
- (ii) Ensuring reasonable (affordable to consumers) prices for foodgrains, and
- (iii) Inducing adoption of the new technology.

In a specific theoretical term, the Agricultural Price Policy ensured the impact of various economic factors on the rate of growth as well as quality of growth and provoked the most desired crop-mix. This incidentally ensured allocation of resources, capital formation and inter-sectoral terms of trade. All these together formed a theoretical base for the price policy. Initially, on the recommendation of the Jha Committee, the Agricultural Prices Commission was constituted and a set of terms of reference were drafted for the Agricultural Prices Commission viz.

- (i) To provide incentive to the producer for adopting technology and for maximising production;
- (ii) To ensure rational utilization of land and other production resources;
- (iii) To keep in view the likely effect of the price policy on the rest of the economy, particularly on the cost of living, level of wages, industrial cost structure, etc.;
- (iv) To recommend from time to time, in respect of different commodities, measures necessary to make the price policy effective;
- (v) To examine, where necessary, the prevailing methods and cost of marketing of agricultural commodities in different regions, suggest measures to reduce costs of marketing and recommend fair price margins for different stages of marketing;
- (vi) To keep under review the developing price situation and to make appropriate recommendations, as and when necessary, within the framework of the overall price policy;
- (vii) To keep under review studies relating to the price policy and arrangements for collection of information regarding agricultural prices and other related data and suggest improvements in the same;
- (viii) To advise on any problems relating to agricultural prices and production that may be referred to it by Government from time to time”.

The specific steps through which these functions were to be operationalized included:

- (i) Announcement of Minimum Support Prices for major food grains;
  - (ii) Procurement prices for purchasing surplus from the cultivators;
  - (iii) Of Public Distribution System and building proper buffer stocks for the purchasers;
  - (iv) Zonal restrictions for movement of food-grains to manage the supply and demand.
- Thus began the operations of the price policy through its instruments.

The Agricultural Prices Commission during sixties and in the first half of seventies followed the cost of production approach to arrive at the MSP and procurement prices They kept under consideration nine important factors while fixing the MSP, levy prices and procurement prices, viz.

- (i) Cost of production,
- (ii) Risk under cultivation,
- (iii) Changes in the input prices,
- (iv) Trends in the market prices,
- (v) Demand and supply of the commodities,
- (vi) Cost of living index and general price index,
- (vii) Fluctuations of prices in international market,
- (viii) Price parity between crops input and output across sectors, and
- (ix) Trends in the market prices.

The methodology of arriving at the MSP was questioned and doubts were raised about the use of data, certain concepts and inclusion/exclusion of imputed cost of various items of farm operations. Similarly, rent of the self-owned land, premium for risk, price parity and cost towards managerial input also came for discussion among the analysts of price policy. In order to reconsider the prevailing structure of the Agricultural Prices Commission and review its methodology a Committee under the Chairmanship of Dr S R Sen was appointed in 1979. The Committee was to examine the methods in arriving at cost of cultivation, and suggest required modifications. Sen Committee in its report gave a number of recommendations towards this (GoI, 1980). Following this, the nomenclature as well as the focus of the Agricultural Prices Commission was changed. The Commission was named as Commission on Agricultural Costs and Prices (CACP) with completely changed terms of reference.

### **1.3 NEED FOR REVISITING MSP**

Initial emphasis of the Agricultural Prices Commission (APC) was on reducing the fluctuations in food-grain prices in order to insulate the consumers against the price increase, providing price incentives to the producers and inducing the producers to adopt new technology. As seen earlier, during mid-eighties, the emphasis of the price policy however, transformed substantially due to the subsequent changes in the agricultural economy. These changes brought forth modifications in the objectives of price policy as well as its emphasis. Consequently, the focus of analytical issues also changed during this period. MSP is now viewed as a form of market intervention on the part of the State and also as one of the supportive measures (safety nets) to the agricultural producers. Even though it is perfectly WTO compatible eyebrows are raised about its continuance and effectiveness to deal with the objectives set by its architects. The issues that dominate the current debate include reasons for continuation of the price support scheme; its effectiveness in terms of the objectives set forth in the 1986 document and support price vis-à-vis remunerative price approach. More pertinent problem relates to the effectiveness of the implementation of the policy of MSP. In sum, the context of price policy has changed substantially over the years and so also the direction and effectiveness of price policy as a tool to influence the agricultural economy. This provoked many social scientists to argue for a fresh look at MSP as an instrument for interacting with some of the important parameters of the agricultural economy. Initially its role was perceived more from the viewpoint of incentivizing farmers to adopt the new seed-water-fertilizer technology. The initial role of MSP as an incentive to adopt technology comes out very clearly in the writing of Professor Dantwala, who was one of the founding architects of India's price policy. He stated that "Though no rigid formula has been accepted to determine the levels of floor prices, the criterion followed is that progressive farmers should find these levels adequate to encourage enterprise and investment to augment production through the adoption of improved technology with all its risk and uncertainty (emphasis added)" (Dantwala, 1996, Pp 213 originally published in 1967). After an experience of a quarter of century, in the implementation of the market intervention scheme Prof Dantwala wrote again during early nineties clearly recognising the changing role of MSP and the interventions. He wrote, "Likewise, intervention has to be selective. Its need must be clearly established and its effectiveness should be constantly under review (emphasis added). The real problem is not simply to establish the legitimacy of intervention, but that of ensuring its effective and judicious implementation" (Dantwala, 1996, Pp292, originally published in 1993). That possibly makes it clear that there is a need to have a fresh look at the MSP and such review must consider its operational efficiency as the main objective.

Among the major objectives of the Price Policy (as reflected from the 1986 policy statement), the incentives to adopt new technology, rational utilization of land and other resources, the

effect of prices on the cost of living that includes agricultural wages as well as wages in the other sectors of the economy, have together assumed greater importance. In the wake of liberalization, MSP assumes a different but a significant role in the form of state intervention in the agricultural product markets as well as a component of the safety-net measure. This also has strong linkage to the factor market. In this situation two important aspects deserve attention viz.

- (i) Insulating the farm producers against the unwarranted sudden fluctuations in prices, provoked by the international price variations (Nair and Sen, 1994) and
- (ii) Creation of an incentive structure for the farm producers in order to direct the allocation of resources towards growth/export oriented crops.

The focus should essentially be towards creation of value addition for the cultivators. Therefore, it becomes necessary to review the implementation process and effectiveness of MSP as an instrument on this background.

After a review, the Committee on Long Term Grain Policy has recommended continuation of the Minimum Support Prices but at the same time also provided other instruments for achieving similar results as that of MSP. Among the alternatives discussed by the Committee insurance against income loss caused by depressed prices below the Minimum Support Price has been one such effective instrument. The scheme should provide insurance coverage to the farmers in the event of price collapse by allowing indemnity to the extent of loss incurred due to price of yield loss (the difference between yield and price received as compared to average yield and price of the last three years). However, such scheme may have implementation bottlenecks. Apart from that, it will be a difficult instrument to be operated by private insurance firms without State support. The problems of moral hazard and the siphoning out the money to the undeserving groups will emerge significantly.

#### **1.4 OBJECTIVES**

- To analyze the effectiveness of the price policy in the context of the objectives set forth by the Commission on Agricultural Costs and Prices.
- To analyze the overall relevance and effectiveness of MSP in the case of major crops grown in individual states.
- To assess the impact of MSP on adoption of improved technology and their relative contribution in increasing the production and productivity of the specified crops.

#### **1.5 METHODOLOGY**

This is a consolidated study covering the research reports prepared in the 11 states in the country. The states include Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Maharashtra, Madhya Pradesh, Punjab, Tamil Nadu, Uttar Pradesh and West Bengal. A common research proposal was prepared for all the states and the agro economic research centres of each of the states were asked to submit the report on the effectiveness of Minimum Support Prices. Alternatives to the present scheme of Minimum Support Prices were also important components of this study.

The macro level analysis included in this study is based on time series data of Minimum Support Prices and other prices collected from secondary sources at state level from 2011-12 to 2014-15. We have also attempted an overall analysis of the price situation in the state with the help of the data on Wholesale Prices and Farm Harvest Prices at state level. Availability of markets and other infrastructure, market arrivals, procurement of food grains, the operations of public distribution system, use of inputs and changes in input prices, changes in the cropping pattern also forms important components of this report wherever needed. In addition to this, our analysis is also supported with the primary data collected from a micro-

level survey conducted in three distinct regions of these states. These regions represent i. commercial crop region, ii. High growth food crop region and iii. Coarse cereals-pulses dominated slow growth region. The field survey covered the information on the markets in these regions in addition to a household survey of the cultivators. The study is also supported by a well-designed PRA exercise carried out at three locations in each of the States. The study is confined to the major crops of the selected States.

## 1.6 LIMITATIONS

- The policy of price intervention scheme was drafted in a totally different agrarian situation than that is prevailing today.
- The present context relevance is difficult, even at hypothetical level.
- The scale and coverage is too large.
- The analysis is limited to a few crops and these are the most important crops from the viewpoint of MSP in the State.

## 2. DATA ANALYSIS & INTERPRETATION

Minimum Support Prices (MSPs) for major agricultural commodities have been raised by the Government in the last few years in order to ensure remunerative prices to the growers and thereby enhancing the production of agricultural crops. There were substantial hikes in MSPs in 2011-12 & 2012-13 as compared to the previous years. However, in 2013-14 & 2014-15 MSPs were increased moderately, as shown in the table below:

Commodity	(Rs per quintal)				% Change		
	2011-12	2012-13	2013-14	2014-15	2012-13	2013-14	2014-15
					2011-12	2012-13	2013-14
Paddy common	1080	1250	1310	1360	15.74	4.8	3.82
Paddy (F)	1110	1280	1345	1400	15.32	5.08	4.09
Jowar-Hybrid	980	1500	1500	1530	53.06	0	2
Jowar-Maldandi	1000	1520	1520	1550	52	0	1.97
Bajra	980	1175	1250	1250	19.9	6.38	0
Ragi	1050	1500	1500	1550	42.86	0	3.33
Maize	980	1175	1310	1310	19.9	11.49	0
Tur (Arhar)	3700	9850	4300	4350	4.05	11.69	1.16
Moong	4000	4400	4500	4600	10	2.27	2.22
Urad	3800	4300	4300	4350	13.16	0	1.16
Groundnut	2700	3700	4000	4000	37.04	8.11	0
Sunflower Seed	2800	3700	3700	3750	32.14	0	1.35
Soyabean (Black)	1650	2200	2500	2500	33.33	13.64	0
Soyabean (Yellow)	1690	2240	2560	2560	32.54	14.29	0
Sesamum	3400	4200	4500	4600	23.53	7.14	2.22
Nigerseed	2900	3500	3500	3600	20.69	0	2.86
Cotton(Medium)	2800	3600	3700	3750	28.57	2.78	1.35
Cotton(Long)	3300	3900	4000	4050	18.18	2.56	1.25
Wheat	1285	1350	1400	1450	5.06	3.7	3.57

Barley	980	980	1100	1150	0	12.24	4.55
Gram	2800	3000	3100	3175	7.14	3.33	2.42
Lentil(Masur)	2800	2900	2950	3075	3.57	1.72	4.24
Rapeseed/mustard	2500	3000	3050	3100	20	1.67	1.64
Safflower	2500	2800	3000	3050	12	7.14	1.67
Jute(TD5)	2200	2300	2400	2400	4.55	4.35	0
Sugarcane (FRP)	170	210	220	230	23.53	4.76	4.55
Copra @ Milling	5100	5250	5250	5550	2.94	0	5.71
Copra @ Ball	5350	5500	5500	5830	2.8	0	6

Table No. 1

Source: Commission for Agricultural Costs and Prices

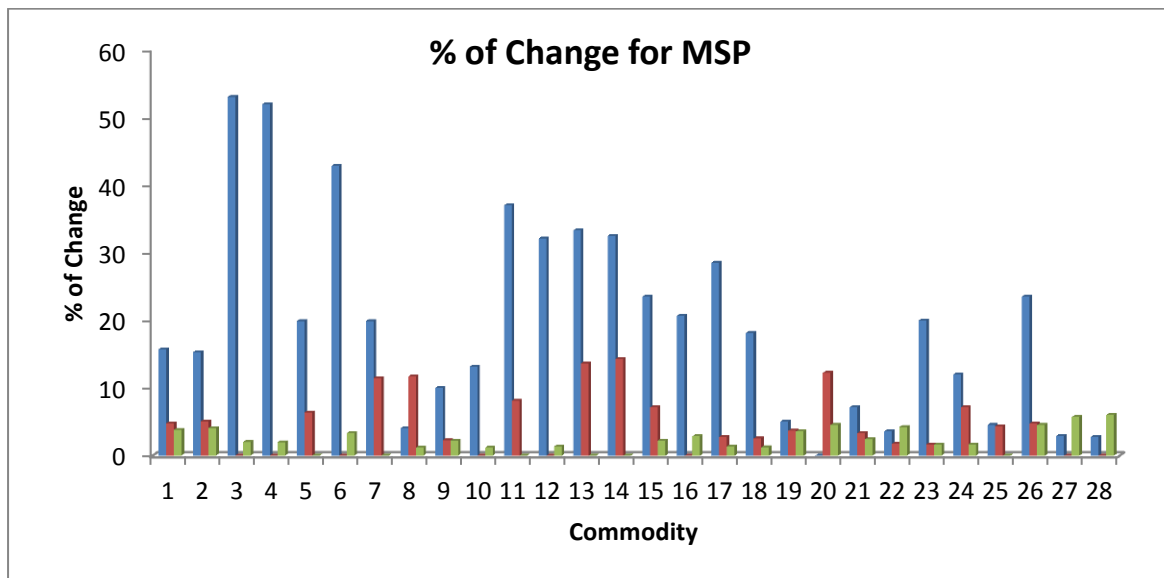


Fig. No. 1

## INDUSTRIAL PRODUCTION

The Index of Industrial Production (IIP) based industrial growth during 2014-2015 (April-January), was 2.5 per cent as compared to 0.1 per cent growth achieved during the corresponding period of the previous year. Out of the three broad sectors, the electricity sector has recorded the highest growth. During this reference period, the electricity sector grew at 9.3 per cent as compared to 5.7 per cent achieved during the same period of the previous year. However, the manufacturing and mining sectors grew at 1.7 per cent and 1.3 per cent respectively against the corresponding figures of (-) 0.3 per cent and (-) 1.1 per cent of the previous year.

Industry Group	Weight	Jan-14	Jan-15	April-January	
				2013-14	2014-15
Mining	141.57	2.7	-2.8	-1.1	1.3
Manufacturing	755.27	0.3	3.3	-0.3	1.7
Electricity	103.16	6.5	2.7	5.7	9.3
<b>Growth by use-based industrial group</b>					
Basic Goods	456.82	2.8	4.5	1.6	7.4

Capital Goods	88.25	-3.9	12.8	-0.8	5.7
Intermediate Goods	156.86	4.3	-0.8	3.2	1.5
Consumer Goods	298.08	-0.5	-1.9	-2.7	-4.7
Durables	84.6	-8.3	-5.3	-12.5	-14.2
Non-durables	213.47	4.5	-0.1	5.7	1.9
<b>General Index</b>	1000	<b>1.1</b>	<b>2.6</b>	<b>0.1</b>	<b>2.5</b>

Table No. 02

**Source:** Commission for Agricultural Costs and Prices

From the above table among the use-based industry groups, basic goods, capital goods, intermediate goods and consumer non-durables sector recorded positive growth during 2014-15 (April-January). Over the same period, the consumer goods sector including consumer durables recorded negative growth, both during 2014-15 as well as 2013-14. At the same time Intermediate goods sector showed a growth of 1.5 per cent during 2014-15 (April-January) as compared to the corresponding figure of 3.2 percent of the previous year. For the basic goods sector, the growth rate for this period during the current year is 7.4 per cent as against 1.6 per cent recorded for the last year. In the consumer durables sector, the growth rate was (-)14.2 per cent during 2014-15 (April-January) as compared to (-)12.5 per cent of the previous year. In contrast, consumer nondurables sector recorded a growth rate of 1.9 per cent in 2014-15 (April-January) as against 5.7 per cent achieved during the corresponding period of the previous year. At the disaggregated level, 5 out of the 22 two-digit industrial groups viz., publishing, printing & reproduction of recorded media, chemicals and chemical products, office accounting and computing machinery, radio, TV and communication equipment & apparatus and medical, precision & optical instruments recorded negative growth during 2014-15 (April-January). Of the remaining 17 industry groups, two i.e. basic metals, and electrical machinery & apparatus recorded above 10 per cent growth; another three groups, namely, food products & beverages, luggage, handbags & leather products and other transport equipment recorded growth rates between 5 to 10 per cent, while twelve groups, namely, tobacco products, textiles, wearing apparel; dressing and dyeing of fur, wood and products of wood, paper and paper products, coke, refined petroleum products & nuclear fuel, rubber and plastic products, other non-metallic mineral products, fabricated metal products, except machinery & equipment and machinery and equipment, motor vehicles, trailers & semi-trailers and furniture manufacturing recorded growth rates below 5 per cent.

### 3. FINDINGS AND CONCLUSIONS

- The Government's Price Policy for agricultural produce seeks to ensure remunerative prices to growers for their produce with a view to encourage higher investment and production as well as safeguarding the interests of consumers by making available supplies at reasonable prices.
- The price policy also seeks to evolve a balanced and integrated price structure in the perspective of the overall needs of the economy.
- To achieve this end, the Government in each season announces Minimum Support Prices (MSPs) for major agricultural commodities and organizes purchase operations, wherever required, through public, cooperative, and other designated agencies to ensure that prices do not fall below that level.
- It decides on the support prices for various agricultural commodities taking into account the recommendations of the CACP, the views of State Governments and Central Ministries as well as such other relevant factors as are considered important for fixation of support prices.



- The MSP being uniform throughout the country, the Commission had to arrive at an all-India weighted average cost as an input to price policy formulation. Since price policy was a resultant of informed judgment of various factors, there could not be any mechanical formula of how much weight was to be given to each factor in the exercise of price policy formulation.
- The margin of MSP over the cost of production varied widely and no norms had been prescribed for fixing the margin over the cost of production. Thus, there is a need for greater transparency in the method of arriving at MSP over the cost of production.

#### **4. BIBLIOGRAPHY**

- <http://finmin.nic.in/reports/AnnualReport2014-15.pdf>
- <http://ageconsearch.umn.edu/bitstream/137357/2/5-SZ-Ali.pdf>
- <http://www.isec.ac.in/40%20Impact%20of%20MSP%20on%20Agr.%20Eco%20Conso%20Rep.pdf>
- [http://niti.gov.in/writereaddata/files/writereaddata/files/document\\_publication/MSP-report.pdf](http://niti.gov.in/writereaddata/files/writereaddata/files/document_publication/MSP-report.pdf)
- [http://planningcommission.nic.in/reports/sereport/ser/ser\\_msp.pdf](http://planningcommission.nic.in/reports/sereport/ser/ser_msp.pdf)
- <http://finmin.nic.in/reports/AnnualReport2014-15.pdf>
- <http://164.100.47.134/intranet/AgricultureProducePricingPolicy.pdf>
- <http://finmin.nic.in/workingpaper/Foodgrain.pdf>
- <http://www.iimahd.ernet.in/assets/snippets/workingpaperpdf/3497670192013-01-01.pdf>