Farm Policy: The political economy of why reforms elude agriculture

India should learn from China and start with liberalisation of rural land, labour and capital markets before attempting bigger things.

Written by Pravesh Sharma | Published:August 18, 2016 2:20 am

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Independence Day has come and gone with its usual mix of celebrations, pride and ruminations on how things could be better. Interestingly, several media commentaries tagged the event with the 25th anniversary of economic reforms, launched in 1991 around the same time of the year. They largely dwelt on the theme of expanding economic freedom to buttress and sustain political freedom, though none – barring a piece by

Ashok Gulati and ShwetaSaini for this newspaper on August 15 (http://goo.gl/L922wj) – focused on agricultural reform.

It is a well-known fact that unlike in the industrial, financial or other services sectors, reforms have mostly bypassed agriculture. The rigid and illiberal policies that continue to exist in agriculture severely restrict its potential to contribute to employment generation and poverty reduction. It, then, raises the question: why does reform elude agriculture?

The answer may lie in the political economy of agriculture, which, in turn, is a product of the interplay of three major forces: a) the situation in the factor markets (land, labour and capital); b) the role of rural commercial capital; and c) globalisation. Let me briefly explain each of these elements — how they mutually clash and generate the friction, slowing down reform in agriculture.

The factor markets in agriculture represent some of the most frozen parts of our economy, where time seems to have stood still since roughly the first decade after Independence. In the case of land, tenancies were abolished along with dismantling of the zamindari system in practically all states by the 1950s. But the result is that informal tenancies flourish and with no legal protection to tenants. There is data showing that the majority of farmers leasing in land now are small and marginal cultivators, who together constitute some 85 per cent of all holdings. The absence of a legal land lease market has hurt these cultivators the most. Lack of tenancy documentation deprives them of access to subsidised formal crop credit, insurance, power and other inputs, while restricting their ability to absorb new productivity-enhancing technologies.

Coming to labour, while this is an area generally seen to be fraught with high risks for reform, the situation of rural labour markets is all the more primitive. While governments have promoted the use of modern technology in seeds and other inputs, they have shied away from unleashing the full power of farm mechanisation. While the underlying motive may be the fear of displacing labour – not borne out on the ground, where the reality is one of growing scarcity and non-availability during the peak agricultural season – the ultimate cost has been farm productivity: Our yields in most crops are around half of China's. Small and marginal cultivators have again been the worst sufferers. They cannot hope to own modern farm equipment and are also unable to access these in the absence of custom hiring centres.

With regard to capital, the Situational Survey of Agriculture for 2013 revealed that only 60 per cent farmers could avail of credit from formal financial institutions, whether banks or cooperative credit societies. In the case of small and marginal farmers, about 85 per cent are still dependent on the village moneylender and informal credit markets, where interest rates start at 24 per cent per annum. No wonder, the survey also showed 52 per cent of all agricultural households in India to be indebted, with Andhra Pradesh (92.9 per cent), Telangana (89.1 per cent) and Tamil Nadu (82.5 per cent) topping the charts.

Linked to these is the role of the other two elements. The stark reality is that rural commercial capital — personified by the large landowner, the moneylender and the mandi commission agent/trader — still dominates the farm credit sector. This form of capital is inherently risk-averse, only seeking to reproduce itself. It courts political patronage to resist any reform or entry of competitors. The entrenched power of rural commercial capital probably explains how even the most tentative and limited of marketing reforms, initiated now and then, have got thwarted in most states.

The impact of globalisation, too, needs to be looked at against this backdrop of rigid factor markets and primitive rural commercial capital. Integration of a few commodities such as cotton, soyabean, rice and high-value fruits and vegetables into global value chains has exposed large number of farm households to price volatility and risks, which they can neither understand nor control. More importantly, the safeguards and instruments available to producers in more developed markets — futures, hedging or even risk insurance — aren't accessible to farmers here. The result can be widespread distress (as in the case of cotton when it went through a global downturn after 2013), fuelling the notion that all reform in agriculture is risky and dangerous.

China's example shows that reforms in the primary sector have to begin with the basic factor markets. The farming community must taste the benefits of reforms first in its immediate neighbourhood — through easier land leasing laws, affordable and timely credit and other financial services, and also access to inputs, mechanisation and transparent markets. That would help build a constituency to support a larger and longer term agenda for reform in agriculture, including rationalisation of subsidies. Policy makers seeking quick solutions through ad hoc, surface-level interventions will only come to grief.

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