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Economic freedom in agriculture

The boom and bust of agriculture will be solved when we shift from state domination to individual freedom

The market for food is bedevilled with difficulties in India. The recent announcements are an important beginning in solving these problems. It is important to focus on the three big decisions of private persons — what to sow, how much to invest, and what to store — and think of the incentive environment for better decisions. The way forward involves much less government involvement, warehousing, futures markets, international trade and national trade.

Paul Samuelson told a fable about agriculture, which is called “the cobweb model”. A good harvest is followed by a price crash, and then sowing goes down, which gives a surge of prices, and then sowing goes up, and the cycle of pain continues. There is more than a whiff of this problem in India; we have seen these cycles of boom and bust play out repeatedly.

How does the market economy solve these problems? It is important to focus on the three big decisions made by private persons: What to sow, how much money to invest in inputs, and what to store. When these decisions are made well, the food market works well, and vice versa. What is the environment through which these decisions can be made well by private persons? Four elements are required.

A market-based warehousing system is required, to replace the existing world of Public Distribution System (PDS) / Central Warehousing Corporation (CWC). Private persons will peer into the future, forecast future shortages, and stock up goods in response.

This is an area where the policy agenda, in the main, is that of ending government involvement.

How will private persons forecast future shortages? How will farmers decide how much land should be sown, and what crops should be sown? The most important input into this is the futures market. The futures market encourages private persons to study the food economy, and make forecasts of future prices. With a well functioning futures market, private persons will benefit by looking at

the futures price, and sowing and storage will shift in favour of goods where future shortages are visible. This is an area which requires the removal of heavy-handed restrictions into futures trading, the integration of India with global futures markets, and the normal agenda of getting India up to well functioning financial markets.

International trade is a good source of stability. When there is a glut in India, and prices crash, it is in India’s interest to export a lot. When

there is a shortage in India, and prices boom, it is in India’s interest to import a lot. Here also, the actions of private persons must determine whether to import or export. There are vast opportunities for India to engage in labour-intensive and high value agricultural exports (http://www.mayin.org/ajayshah/MEDIA/2019/agri_intnl_trade.html), which requires simultaneously shifting land away from capital-intensive products like wheat or rice.

It is important to see that integration into the world market requires the development of organi-

sational capabilities in private firms. When a government coerces people in unpredictable ways, with bans and unbans, such organisational capability does not develop. The policy agenda is one of government stepping away, as it has in (say) the market for nickel.

The fourth element is trade within India. India is vast and heterogeneous; we are like the European Union. Trade within India is also a great source of stability. This requires removing all interference by the government in intra-India trade. There should be full freedom for buyers and sellers to travel anywhere and trade anywhere, as there is in (say) the market for nickel.

With these four elements in shape (warehousing, futures trading, domestic trade, and international trade), the incentives will be in place for private persons to make the three decisions (what to sow, how much to invest, what to store) properly. The boom and bust, and persistent low income, of Indian agriculture will be solved when we shift from state domination to individual freedom.

The recent announcements focus on problems of warehousing and the national market. The announcements are in the right direction. Rapid and technically sound implementation is now the need of the hour. The present maze of interventions is a complex legal minefield, featuring reductions of freedom through Parliamentary laws and through laws enacted by state legislatures. Careful legal analysis is required, of this minefield, to develop the legal strategy for the Parliament to enact new law which creates freedom in warehousing and in the national market.

A key idea lies in utilising Article 301 of the Constitution of India, which states that trade and commerce throughout India shall be free. This creates interesting possibilities for the Union government to play a role in creating an integrated national market, and by creating institutional mechanisms to continuously identify and review administrative barriers to trade in the food market. A paper by Anirudh Burman, Ila Patnaik, Shubho Roy and myself, “*Diagnosing and overcoming sustained food price volatility: Enabling a National Market for Food* (<https://bit.ly/BPRSfood>),” has this legal analysis.

The market for food has a maze of restrictions which interfere with the three big decisions of private people. In the short run, the full market-based mechanism will not be in play, as many reform actions are required. In the short run, policy initiatives will often generate some unpleasant partial equilibrium effects. It is useful to think in general equilibrium, and undertake the long-range work required to fully graduate to a market-based food system, and then reap the full gains.

The food market is a nice demonstration of the failures of traditional Indian development thinking. The path to policy failure is paved with good intentions. The developmental state, the central planning instinct, the almost casual crushing of human freedom, delivers bad results. At every step of the way, our faulty intellectual framework led to policy actions that kicked off unintended consequences. The way out of mass poverty in India lies in questioning these foundations, in food and in other areas.

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