Chapter 6
Summary and Conclusions

6.1 Summary
6.2 Conclusions
6.3 Policy Implications
6.1 Summary

There has been a substantial body of literature which throws light on the market based models of Contract Farming in India and other countries. Though these studies report varied degree of success of the process with respect to its efficiency, many of them concur that risk sharing by the farmer and the contracting firm may be theoretically one of the redeeming aspects of the Contract Farming model but in practice the risk is borne unevenly by farmers. Although, in the short run, individual farmers might have benefited, but in the long run, the Contract Farming benefits the contracting companies more due to their greater bargaining power. Much of the body of research work suggests that the market driven model needs to be mediated through the Government to ensure that it does not become exploitative. However, there is a lack of studies analysing a model of Contract Farming where Government acts as a regulator as well as a facilitator, trying to ensure that Contract Farming has a strong developmental component which works over and above a narrow profit maximising objective.

The Punjab model presents a case in point where the state Government recognised an impending agrarian crisis, emerging out of a scenario of fast-depleting ground water table which was the lifeline of the most common cropping cycle of wheat-paddy in the state. Reasons for continuation of this cropping cycle were rooted in a combination of factors, within which Government policies were probably the most stark and significant. The wheat-paddy cropping cycle became the most desirable option for the farmers because of Central Government procurement price policy, which eliminated price risk as well as the State Government power subsidy for electricity, which resulted in artificially depressing the costs of cultivation. It was in this context that the Punjab Government introduced a Contract Farming system with a well defined objective of crop diversification where the Government was an active player, along with farmers and contracting/service providing private firms.

This study attempts to fill in the gap present in the literature, touching upon several aspects of this Government supported model, that ranges from analysing policy details of the model, perspective of the contracting firm, impact on farmers, and finally its implication for regional development by identifying factors responsible for selection of micro-regions (villages) for the process.
The analysis in the study reveals that penetration of the Contract Farming programme launched by the Punjab Government for crop diversification has been far from satisfactory. Only 62.4 percent and 24.5 percent of the acreage target for Crop Diversification was achieved in 2003 and 2004 respectively. Other than basmati, no other crop has elicited widespread interest amongst the private players. In order to protect the interests of the farmers and encourage private sector participation, PAFC has devised several mechanisms like ‘comfort price’ and paying the service providers on the basis of acreage brought under Contract Farming. Highly protective mechanism devised by PAFC seems to be the extension of Minimum Support Price system which reduces the bargaining power of the private firms’. Middle level institutional structure (service provider) seeks to substitute the role of other government agencies and has been quite controversial. In the initial phase several cases of corruption and wilful overstatement of the Contract Farming area by service providers were recorded. While mentioning several reasons to introduce Contract Farming, other than the primary one of crop diversification, PAFC has also listed compliance with WTO norms as one of the reasons to introduce Contract Farming. This demonstrates that by giving greater operational space to private players PAFC wants to make Punjab agriculture more investor friendly. Some of the facilitating steps taken by PAFC include setting up mandis and warehousing facilities for procurement of produce from the contract farmers. In order to make the procurement of agri-produce very competitive for the processors, the state government has reduced taxes and levies like market fees and rural development cess from 2.0 to 0.25 percent each, thus leading to a reduction by 3.5 percent in the aggregate.

With the emergence of new opportunities in agriculture several agri-business ventures have come up. These ventures include not only food processing industries but also agri-input industries. Most of these ventures operate on the basis of service centre model and consider Contract Farming as a client-building preposition, useful for backward chain consolidation and an instrument for rural penetration. These ventures do not take into account agricultural specificity and cultural variability of the Indian agrarian operations. Instead of adopting the wide area reach approach, they try to reach some of the best and most capable farmers, which will not only fulfil the requirements...
for agricultural operations but will also, minimize transaction cost. These agri-business ventures have adopted ‘consumer differentiation’ model for maximizing returns. All the firms engaged in the Contract Farming programme were highly appreciative of the programme and believed that it can help in improving the competitiveness of Indian agriculture in the world market. Firms believed that Contract Farming has a great potential not only to increase India’s export income but also for the expansion of the food business. Traditional rice exporters viewed Contract Farming as a major institutional intervention to make India’s export competitive in the world market. They believed that through Contract Farming, they can not only achieve substantial cost reduction in their input sourcing operations but can also secure reliable supply chain through it. All the companies agreed that Contract Farming has a beneficial impact on agriculture and farmers should participate actively. Main reasons given by the companies for the farmers to adopt Contract Farming are as under-

- Protection from price fluctuations
- Availability of fixed buyer in the market
- Availability of modern farm inputs at reasonable prices
- Easy availability of loans
- Facilitation in the adoption of eco-friendly practices

Firms considered Contract Farming as a platform which can be used as a launch pad for new technology and machinery. With the contract farmers as their secured client, they can minimise on the advertisement cost and can get some base customers for development of the technology. Most important factors considered by the firms while selecting the villages were existing cropping pattern in the village, infrastructure availability and agro-climatic suitability of the crop. Among infrastructure, main factors considered by the Contracting firms were-

- Accessibility of the village,
- Education and general awareness level in the villages (presence of school and colleges in the village or in nearby area),
- Nearness to urban area,
- Quality of perennial irrigation
Firms did not choose farmers at random and followed certain basic criteria for selection of the farmers. While selecting the farmer their overriding concern was success of the crop therefore they wanted to adopt most efficient, better endowed farmers. The major criteria followed by firms while selecting farmers for the contract were:

- Previous experience of the crop (Avoid Experimentation),
- Size of operational land holdings of the farmer (Big Farmer),
- Previous record of the yield (Efficient Farmer),
- Ownership of mechanical implements and irrigation infrastructure (Access to Capital),
- Educational level of the farmer (Awareness of the Farmer),
- Socio-economic strength reflected in the debt status of the farmer (Freedom From Arhatiya) and
- Non-farm income of the farmer household (Degree of reliance on agriculture as a means of livelihood).

Contracting firms were also facing challenges at several fronts including government pricing policy, local level middleman (Arhatiyas) and absence of legally binding contract. These factors were related to both structural and institutional set up, as well as the cultural web of rural areas.

Firms’ preference to the better endowed farmers was reflected in the domination of rural elite in the Contract Farming programme. Average operational land holding of contract farmer was 20.3 acres while that of the non-contract farmer was 15.6 acres. Besides having higher operational land holding, contract farmers had greater linkages with the rural political structure. Although contract farmers showed higher crop diversification index on account of higher acreage devoted to the Contract Farming crops, they practised highly intensive agriculture resulting in greater usage of water than the non-contract farmers in many cases. Contract farmers have been able to obtain higher yield than the non-contract farmers; however they were not able to obtain similar yields outside Contract Farming, which means, that technology and knowledge diffusion, one of the stated externality of the process of Contract Farming, appears to be absent till now. The profitability of crop has been the most important consideration for
cultivation of any crop in the state, and even within the framework of Contract Farming, this continues to remain as the primary reason. In other words, other benefits like assured price and market, which Contract Farming provides the farmers are, at best, of marginal consequence for land allocation decisions. There has been a noticeable increase in the contracted area of sunflower, but only because it fitted in with the existing cropping pattern that was the most profitable crop combination (paddy-potato-sunflower). In other words, if smooth marketing channel and input supply is ensured, farmers would cultivate the crop even outside the framework of Contract Farming. A non-profitable but environment-friendly crop like maize is adopted only if the farmers cannot opt for the stable and otherwise profitable conventional crop cycle of wheat-paddy. Thus maize had been adopted by the farmers only in locations where they have faced higher water depletion and didn’t have better alternatives.

One of the issues that were examined in this study was the implication of the Contract Farming process on balanced regional development at the micro level. The hypothesis that we started with was that private firms, to the extent they can exercise their choice, would opt for regions having better infrastructure, to maximise their profits. Contrary to the expectations, general infrastructure was not an important determinant in adoption of Contract Farming at the village level. This might be due to three reasons. Firstly, in Punjab the general level of agricultural infrastructure is well-developed and at the village level, differences are less significant compared to rest of India. Secondly, from the analysis of the role of the Government in Contract Farming, it emerges that the Government also has a role to play in selecting the region (micro) of operation of the firms. Thirdly, though the firms may opt for regions with better infrastructure, the existence of highly profitable cropping pattern makes the farmers of the region unwilling to adopt any changes. In fact, better levels of irrigation at the village level actually reduced the chances of a village adopting the Contract Farming system. It needs to be noted that these villages would have incorporated stable and profitable cycle of wheat-paddy in a manner that would be more sustainable compared to villages with relatively lower levels of irrigation.

Though level of infrastructure does not seem to affect probability of adoption of Contract Farming at the village level, detailed insight does give an indication, that, the
nature of contract farming adopted in the better-connected and relatively remote areas, is qualitatively different. For example, cluster-2, which had better connectivity and a nodal position had a higher concentration of contract farmers compared to cluster 1, which was relatively cut-off and located further away from an urban centre. Secondly, the crop that was adopted through Contract Farming in cluster 2 lead to more profitable income of the adopter farmers as compared to cluster 1. This indicates that in a developed region, farmers have a better bargaining power, ensuing from the more favourable region that they are located in. Amongst the locational factors that influenced the probability of adoption of Contract Farming at the village level, variables associated with awareness were found to have significant influence with highest predictive power. Higher non-farm employment opportunities were found to have a negative relation with the probability of adoption of Contract Farming. In other words, if there are alternative opportunities outside agriculture, the probability of Contract Farming adoption would reduce significantly.

6.2 Conclusions

Contract Farming represents a paradigm shift in the Indian policy making. Engagement of corporate players to bring about crop diversification and achievement of more sustainable agricultural practices has been a novel experiment, unparalleled in the history of independent India. ‘Multipartite’ model of Contract Farming adopted by PAFC is highly protective and risk minimising both for private players and farmers and in a sense, extension of MSP approach. This represents an unusual marriage of socialistic developmental thought and profit maximising capitalistic view. The state seeks to promote as well as keep in check the inherent marginalising tendencies of private capital. Although good in intentions, the policy faces certain deficiencies and lack of clear focus. For example, the commitment to distributive justice is defeated by the Government policy of paying service providers on the basis of acreage brought under Contract Farming and not on the basis of number of farmers brought under the fold of crop diversification programme. Contracting firms cannot be faulted for having inherent bias in the favour of most efficient and well endowed farmers as they work for maximising profit. Though some of the features of this Government supported model
promote farmers’ interest, this is certainly not at the cost of the interest of the contracting firms. Besides private players, local and international operations may help in increasing farm incomes and broaden acreage of the export crops, but to expect that they would bring about crop diversification in non-export and non-cash crops, will be a misplaced hope. When targeting international markets, the highly imperfect and volatile nature of these markets should not be forgotten. Besides, a great deal of caution is required while preparing a platform for the international players. While they can help in increasing the earning and bringing in foreign markets within the reach of farmers, it will be far fetched to hope that they will continue with the Contract Farming programme when international markets become unremunerative, or a shift in consumption pattern takes place.

One of the reasons for many of the contract farming crops, that offer a water saving option, not being too successful in replacing the rice-wheat cycle is that, there is no price risk in this water intensive crop cycle in the state, due to certainty of the procurement price mechanism. One of the benefits that contract farming offers is precisely the same facility of minimising price risk. Thus, the competition between existing cropping system and Contract Farming crops is in terms of profitability and not secure market channels. Contract Farming needs to offer more attractive options, if it as to make a significant shift away from the water intensive wheat-paddy cycle.

What is needed is not just the involvement of few corporate players in outsourcing of farm activities to farmers, but the total overhaul of agriculture and food policies as well. Continuous upward revision of MSP in case of wheat and paddy poses a severe restrain to the spread of Contract Farming in oilseeds and pulses, which has to be taken care of while formulating a grandeur programme such as crop diversification. Also non-take off of Contract Farming in vegetables and other crops indicate that crop diversification is a complex phenomenon and cannot be achieved by simplistic crop-specific models. Horticultural crops not only offer a profitable option, but generally save on precious water resources. The risk of horticultural crops emerges from speculative prices and lack of cold storage facilities. While contracting firms can take
care of the former problem, the state Government can invest in crop-oriented infrastructure facility.

Again, higher crop-diversification does not necessarily entail better cropping practices and lower input use. A single crop proposed for diversification might use lesser inputs than the crop it seeks to replace but in a crop combination cycle it might worsen the input use. Therefore, it is not only desirable but also imperative to work out a right mix of the proposed crops for diversification.

Farmers’ adoption of any new system is the result of complex interplay of various mediating factors. Farmers’ educational status, factor endowments, socio-economic and political networking and availability of alternatives etc. play an important role in decision making. So Contract Farming might appeal to a farmer who perceives that the alternative offered through contract is better than presently available to them. Therefore, a farmer facing water stress might respond more favourably to Contract Farming in maize offering a price and buyer stability than a farmer having little resource constraint. As a result the spread of Contract Farming or for that matter any other new policy initiative will depend upon the choices made by the players.

From the example of Contract Farming in Punjab, it is quite clear that, socially egalitarian and environment friendly objectives are difficult to achieve through a market-driven measure even when government actively intervenes on behalf of the farmers. Besides, there cannot be any single measure and model but a series of alternatives as no single model is suitable for all conditions. Revitalisation of the cooperatives is expressly desired as any market measure in the absence of a strong cooperative and farmer organisation would end up in marginalising socio-economically weaker farmers.

Experiences of PAFC show that Indian institutions are in the process of evolution and Contract Farming can be considered only a step in the evolution of competitive marketing system and not the only option for it. Importance of vigilant and proactive regulatory institutions will further increase in the era of liberalized economy to guide the market forces in order to achieve various goals.
6.3 Policy Implications

Lacunae and loop holes revealed in the policy formulation of Contract Farming suggest that there is a need to broaden the crop diversification programme. The present model has a limited impact as it works at cross-purpose with MSP and policy of free electricity.

The current crop-specific model has to be planned out in a more holistic manner keeping in view the possible complementary crops that can be cultivated with the crop that is being promoted. The exclusion of horticultural crops as an explicit focus point in the strategy is a case in point.

Importance of State in protecting the interests of small and marginal farmers has increased all the more, as even in private-public mode of partnerships exclusion of socio-economically deprived groups is quite rampant.

Crop insurance and legal backing which has been missing in the case of Contract Farming also needs to be restored, as without any legal sanctions contracts put farmers (especially small) in an unequal bargaining position.