Contract Farming: Recipe for crisis

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The UPA government's touching faith in the power of private corporate activity appear to be undiminished despite large and indeed growing evidence to the contrary. As in so much else relating to the productive sectors of the economy, the central government appears to believe that most problems in agriculture can be solved not through active public intervention but simply by letting large private corporations handle things. The National Agriculture Policy declares that "Private sector participation will be promoted through contract farming and land leasing arrangements to allow accelerated technology transfer, capital inflow and assured market for crop production, especially of oilseeds, cotton and horticultural crops".

Contract farming is a system of cultivation and supply of agricultural goods that is based on forward contracts between producers/suppliers and buyers. The essence of such an arrangement is the commitment of the cultivator to provide a certain quantity of a crop to a committed buyer (typically a large company). The contract usually requires the farmer to plant a specific crop on his or her land, and to harvest and deliver to the contractor a certain amount of produce, based upon anticipated yield and contracted acreage. This could be at a pre-agreed price, but need not always be so.

Quite often, the contractor supplies the farmer with selected inputs and technical advice. The typical contract is one in which the contractor supplies all the material inputs required for cultivation, while the farmer supplies land and labour. However, the terms and nature of the contract differ according to variations in the nature of crops to be grown, the agencies or companies concerned, types of farmers, and technologies and the context in which they are practised.

This system has old historical roots. There are those who will find obvious analogies with the system of what became known as "forced commercialisation" under the aegis of the East India Company in the 18th and early 19th centuries, when indigo and opium cultivation was introduced by European planters into Bengal. However, modern contract farming been developed in the United States, where corporate penetration of agriculture is now the most advanced as multinational companies have come to dominate the entire chain of agricultural production and distribution.

The recent spate of contract farming in India effectively began with the case of Pepsi Foods Ltd (hereafter PepsiCo) which entered India in 1989 by installing a tomato processing plant at Zahura in Hoshiarpur district of Punjab. The company intended to produce aseptically packed tomato pastes and purees for the international market. However, before long, the company decided that the investment in agro-processing plants would not be viable unless the company also had greater control over the yields and quality of the tomatoes produced locally. In consequence PepsiCo followed the contract farming method described earlier, whereby the cultivator plants the company's crops on his land, and the company provides selected inputs like seeds/saplings, agricultural practices, and regular inspection of the crop and advisory services on crop management.

As it happened, subsequently PepsiCo abandoned tomato procurement, and since then its contract farming model had been focussed on potatoes for making processed potato chips. It currently has contracts with around 24,000 farmers, mainly in Punjab, but also in other states like West Bengal, Gujarat, Uttar Pradesh, Maharashtra, Karnataka and Bihar.

However, PepsiCo's involvement with contract farming has gone through many ups and downs. After an initial phase of much excitement when its model of contract farming was considered a success in terms of diversifying cultivation in Punjab and improving the incomes of farmers, there was a lull and even decline in the 2000s. This reflected growing dissatisfaction among the farming community affected by these contracts, especially when lower market prices led the company to effectively reduce the output prices through a variety of means such as quality control.

More recently there has been a revival once again, with the amount of potato procurement by PepsiCo doubling to 240,000 tonnes in the past five years. Further, the company has once again declared ambitious plans for expansion and extension to other crops like food grains (basmati rice and oats), spices (chillies) and oilseeds (groundnut) as well, apart from other vegetable crops. However, the recent statements sound almost identical to promises made nearly a decade ago by earlier Company representatives that subsequently did not materialise, so the past performance may not be an optimistic predictor of the possible future.

One major problem that has been evident in the past is the reneging of contracts by parties depending on market conditions. Thus when market prices are low, companies (not just PepsiCo but others) have rejected produce on quality grounds, forcing farmers to sell at lower prices to them or other buyers. It is also true that there have been instance of side-selling by farmers when market prices have been higher than those contracted.

It has been observed that the private companies that were to provide extension services in the contracted areas, did not do their job properly. (This is after all a labour intensive and expensive service to provide, with many positive externalities, which suggests that it would typically be underprovided by private suppliers in any case.) Issues like proper agronomic practices, regular visits to farmers and emphasising the quality norms were inadequately addressed. In the non-traditional basmati areas which were under contract farming, cultivators resorted to large-scale use of harvesting machines which resulted in high percentages of broken grains. Contractors wanted to pay lower prices for such grain, which the farmers were not willing to accept.

As a result, the state government agency that had designed the contract farming programme in the first place (Punjab Agro Foodgrains Corporation) has on several occasions been forced to step in and buy basmati rice that was being rejected by the contracting companies. The PAFC has become the guarantor of last resort for buyers and farmers in case the transaction does not go off smoothly, which is increasingly the case.

In Punjab, successive state governments have argued that contract farming is the best means of crop diversification, in a region where there is a real question of ecological survival and sustaining natural resources like water and soil in a reasonably healthy state. Traditional crops like wheat and the more recent paddy are seen as excessively reliant on water, so reduction in acreage of these crops by around 30 per cent is suggested by agronomists. However, since contract farming is based on private corporate interests that are inherently profit-driven, there is no reason why these should coincide with the ecological requirements of the region. Indeed, much of the recent corporate interest in Punjab agriculture has been in basmati farming, which is one of the great water-guzzlers. Crop diversification can be more effectively encouraged through a system relative pricing policy accompanied by a supportive system of public agricultural extension services. It is the decline of such public services which has instead laid open the field for private corporations to enter.

The Punjab government apparently feels that shifting to contract farming will ease the pressure on state finances by eliminating both subsidies and farm support prices. But it is likely to do so only at the more significant medium term cost of corporatisation of agriculture and marginalisation of farmers. Already, around 100,000 acres are under contract farming in the state, with both multinationals and domestic companies involved. The system that is increasingly in vogue involves a tie-up of a marketing company with an input producer with a bank that agrees to provide credit.

The state government of Punjab is not alone in encouraging this greater corporate activity in agriculture. A 2006 study by Sukhpal Singh describes how governments in Gujarat, Madhya Pradesh, Andhra Pradesh, Karnataka, and Maharashtra have allowed agribusiness firms to buy and operate large land holdings for R&D, and export-oriented production purposes. Sometimes the explicit purpose is to encourage cultivation on wastelands. Thus, state governments of Maharashtra and Gujarat have also enacted laws to allow corporate farming on government wastelands by providing large tracts of these lands (up to 2000 acres each) to agribusiness companies on a long term (20 year) leases. The Chhattisgarh State Government has made available about 20 lakh hectares of land for jatropha (biofuel) cultivation. The government of Gujarat has offered wastelands up to 2000 acres for horticulture and biofuel for 20 year lease to big corporate houses and resourceful farmers at the rate of Rs. 500 per acre interest free security deposit.

Quite apart from various concerns about the rights over waste lands and the denial of such rights to local dwellers, including women, there are also concerns about common lands and pastures being classified as waste lands and handed over to corporations on that basis. An even bigger concern may relate to water rights. Since ground water in India is effectively privatised (in that whoever can dig the deeper well can appropriate more of the ground water) there are dangers of corporations taking the lions' share of water resources, affecting neighbouring cultivators and adversely impacting the water table in the area.

Various studies of other experiments with contract farming (such as the famous "Kuppam" project that was implemented in Chittoor district in the electoral constituency of the then-Chief Minister Chandrababu Naidu in the 1990s, and other instances in states like Madhya Pradesh) have indicated that such schemes have at best very mixed results and that they also led over time to displacement of small farmers. Several problems relating to sustainability of that pattern of production and unsuitable ecological practices associated with such contracts have been noted.

A study by Venkateshwarlu and Corta (2001) of contract farming of hybrid cottonseed in three districts of Andhra Pradesh, found large-scale use of the labour of young girls, at the expense of employment of adults. Most of the cross-pollination work - which accounted for nearly 90 per cent of the labour time – was being done by young girls who worked daily from July to February. Generally, 10-15 children were hired for 100-150 days per acre of cottonseed production. Children as young as six years old worked from 8.30 am to 6-7 pm. The cottonseed production calendar was standardised by companies for seed certification and marketing. This resulted in the regimentation of children's work schedules, so that they were continuously employed for six to nine months a year. Girls were preferred in cottonseed production because their wages were lower than those of adults, they worked longer hours and more intensively, and were generally easier to control. It was reported that one girl could do the work of three adults. Though the agreements typically obliged these female children to work for only one season (six to nine months), in practice they tended to work for several years for the same contractor.

The case of Andhra Pradesh may deserve some more elaboration, because of the extreme agrarian crisis evident in that state after a period of systematic encouragement of private corporate agriculture and neglect of the conditions of viability of small farmer cultivation. The Commission on Farmer's Welfare that was set up by the state government of Andhra Pradesh in 2004 found that the economic strategy of the previous decade at both central government and state government levels systematically reduced the protection afforded to farmers and exposed them to market volatility and private profiteering without adequate regulation; reduced critical forms of public expenditure; destroyed important public institutions; and did not adequately generate other non-agricultural economic activities. While this was a generalised rural crisis, the burden fell disproportionately on small and marginal farmers, tenant farmers and rural labourers, particularly those in dryer tracts. In these circumstances, farmers' distress was reflected in extreme form in suicides, but also in loss of land by small owner-cultivators, migration and other related tendencies.

The state government in Andhra Pradesh did not play a central role in ensuring the provision of high quality inputs at affordable prices at the right time to all cultivators both by direct intervention as well as by appropriate regulation. Nor did they provide sufficient extension services, such that most knowledge was effectively provided by private input suppliers with clear conflicts of interest. This was one of the reasons why farmers sought contractual relationships with buyers who also promised greater access to agricultural knowledge and inputs.

The Report also found that the marketing of agricultural produce had become one of the critical areas where the farmers were exploited, largely because of inadequate and sometimes faulty forms of public intervention. Thus, marketing infrastructure was found to be inadequate and there were numerous procedural problems in the market yards. This is not an insurmountable problem: it is possible to provide adequate and non-exploitative arrangements in the market yards, especially using new technologies, that would reduce the exploitation of direct cultivators by private buyers. Similarly, timely and adequate procurement operations by central and state government agencies could ensure remunerative prices to cultivators and arrest distress sales. Market Price Stabilisation Funds (along the lines also proposed by the National Farmers' Commission) would prevent excessive volatility of prices faced by cultivators and also reduce their need to enter into contracting arrangements that promised a dubious stability.

It is evident from the cases reported here, as well as other evidence, that contract farming holds numerous problems for agriculture in developing countries like India. It tends to displace labour quite substantially; marginalises the direct cultivators who lose control over the production process and often even over their land; encourages more capital-intensive and less sustainable patterns of cultivation; can result in greater insecurity and lower incomes for farmers because of use of quality measures to lower the effective output price being paid by contractors; can even deny farmers the benefits of higher prices which could be instead absorbed by corporate contractors with local monopsonistic power; propagates monoculture which reduces food security and the possibility of livelihood diversification through livestock; relies excessively on the use of lower paid women workers and child labour; increases and accelerates the process of casualisation of labour. Given these evident problems, it is surprising that contract farming is still being promoted so assiduously by various forces, including the central government in India today.

The case for contract farming has emerged largely because public institutions have failed to provide farmers with the essential protection and support required for viability on a sustained basis. What cultivators in rural India need most of all today is the following combination: a basic price support mechanism that ensures that costs are covered; efficient extension services that provide information about possible crops, new inputs and their implications, new agricultural practices relevant for the particular area, and so on; the availability of reliable and assured credit at reasonable rates of interest. These features were certainly planned for Indian agriculture, and in some regions they were also delivered in some periods. There is also no reason why they cannot be delivered by the public sector.

This necessarily requires a revival of agricultural extension services and the provision of agricultural credit across rural India, as well as a rejuvenation and strengthening of the Minimum Support Price system for important cash crops. There is no reason to expect that private corporate firms will deliver these requirements, since their interest would be to maximise profits in the short-term and they are not necessarily interested in the long-term sustainability of cultivation. Indeed, private corporate involvement is unstable; this generates demands for the renewed involvement of the public institutions.

The argument is often made that the combination of price support, credit provision and extension services is no longer possible for state governments to deliver because of their current fiscal crunch, and that is why they are being forced to encourage contract farming. This argument is specious at best. If private corporations can borrow to undertake these activities, there should be no reason why the government cannot do the same, especially when public involvement is likely to take a more socially desirable form. If state governments are being prevented from undertaking such borrowing, then that is where the battle must be fought, by mobilising all the state governments to challenge these central restraints, rather than succumbing to the pressures and looking for private sector alternatives in an area with high positive externalities such as this.

What is very clear is that relying only on contract framing to solve the current agrarian problems in the country is futile. Instead, if it is not properly controlled and regulated and if it adds to the reneging of responsibility by state acstors, it is likely to intensify such problems.

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