REPORT

OF THE

COMMISSION FOR AGRICULTURAL

COSTS AND PRICES

ON

PRICE POLICY FOR SUGARCANE

FOR THE

2006-2007 SEASON

DEPARTMENT OF AGRICULTURE AND COOPERATION
MINISTRY OF AGRICULTURE
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COMMISSION FOR AGRICULTURAL COSTS AND PRICES

Report on Price Policy for Sugarcane for the 2006-07 Sugar Season

In this report, the Commission for Agricultural Costs and Prices presents its views on the price policy for sugarcane for 2006-07 sugar season. The Commission recommends that: -

(i) ***the Statutory Minimum Price (SMP) of sugarcane payable by sugar factories for 2006-07 sugar season be fixed at Rs. 79.80 per quintal for a basic recovery rate of 9 per cent subject to a premium of Rs. 0.90 for every 0.1 percentage point increase in the recovery above that level. At the All-India average recovery rate of 10.17 per cent achieved in 2003-04 season, the SMP recommended comes to Rs. 90.33 per quintal;*** (Para 33)

(ii) ***the Government should invariably declare the SMP of sugarcane before start of the sowing season rather than at the beginning of crushing season. Also, the Government should take decisions on the non-price recommendations of the Commission;*** (Para 2)

(iii) ***the Government should examine the cost effectiveness and scope of greater outreach of tissue culture technique, as developed by VSI, Pune for improving sugarcane productivity as well as reducing the cost of production;*** (Para 4)

(iv) ***there should be a ceiling of 7 percent on the rate of interest to be charged on the loans advanced to farmers by commercial banks as well as cooperatives and the rate of interest should be simple and not compound;*** (Para 5)

(v) ***the Directorate of Sugar should carefully calculate the recovery rate of all those sugar factories which produced sugar by mixing raw sugar with sugarcane juice;*** (Para 7)

(vi) ***the Government should dispense with the regulated release mechanism for free sale sugar while continuing with the levy obligation of 10 percent for supply of sugar through the PDS to protect the interest of the vulnerable section of society;*** (Para 11)

(vii) ***the sub-Clause (1)(a) of Clause 6 of the Sugarcane (Control) Order, 1966 may be amended to make provision for reservation of cane area, inter-alia, on the basis of recovery rate of a factory;*** (Para 16)

(viii) ***the reservation of cane area should be on long-term basis at least for a period of ten years subject to periodical review by the Government for mid way corrections especially keeping in view the need to maintain production efficiency at the factory level and a suitable provision in this regard may be made in the Sugarcane (Control) Order, 1966;*** (Para 17)

(ix) ***the minimum distance between the existing sugar factory and new sugar factory may be increased from 15 km to 25 km and a suitable provision in this regard may be made in the Sugarcane (Control) Order, 1966;*** (Para 18)

(x) ***the Government should declare the L factor within three months of the close of a sugar season. Also, the Government should take necessary steps to declare the L factor for 2003-04 sugar season without any further delay. Further, the Government may get the suggestion of the Government of Tamil Nadu examined to delegate the power to declare L factor to the State Governments;*** (Para 19)

(xi) ***the Government should formulate a long-term policy for sugar trade to promote exports of sugar on regular, albeit sustainable basis;*** (Para 24)

(xii) ***the Central Government should provide a package to the state of Bihar to help the State Government in setting up of new sugar mills and for revival of viable closed sugar mills as well as modernization of existing sugar mills. Also, adequate funds should be made available to the Sugarcane Research Centre, Pusa for development of new high yielding and high sucrose rich varieties in collaboration with other public and private research institutions in the country;*** (Para 25)

2. The Commission submitted its report on price policy for sugarcane for 2005-06 sugar season on 8th September, 2004, recommending the Statutory Minimum Price (SMP) of Rs 79.50 per quintal linked to a basic recovery rate of 9 percent subject to a premium of Rs 0.88 for every percentage point increase in the recovery above the level. Ten months have already elapsed since the submission of the report, but the Government is yet to declare the SMP for 2005-06 season. The announcement of the SMP for 2005-06 sugar season has been considerably delayed. There was also delay in the announcement of SMP for 2004-05 sugar season and the Government notified the SMP on 18th December, 2004, fifteen months after the submission of the report. It has become customary for the Government to announce the SMP at around the beginning of crushing season though the Commission submits its report well in advance of the sowing season to enable the Government to announce the SMP before the start of the sowing season. The purpose is to give the right price signal to sugarcane growers before they take a decision to grow sugarcane crop or other alternate crops. The delay in the announcement of SMP defeats the said purpose. The Commission in its earlier reports has also urged the Government to declare the SMP before the start of the sowing season. In addition to the price recommendations, the Commission also suggests non-price measures to improve the sugar economy. However, these non-price recommendations are not

often attended to by the Government. The Commission, therefore, recommends that ***the Government should invariably declare the SMP of sugarcane before start of the sowing season rather than at the beginning of crushing season. Also, the Government should take decisions on the non-price recommendations of the Commission*****.**

3. The production of sugarcane suffered serious setback in 2003-04 and 2004-05 sugar seasons. After reaching a peak level of 299.32 million tonnes in 1999-2000, the production of sugarcane has been declining. It declined to 295.96 million tonnes, 287.38 million tonnes and 237.31 in 2000-01, 2002-03 and 2003-04 respectively. The area under sugarcane, which was 42.20 lakh hectares in 1999-2000, increased to 43.16 lakh hectares in 2000-01 and to 45.20 lakh hectares in 2002-03 but decreased to 40.23 lakh hectares in 2003-04. The average productivity also showed a mixed trend. In a state like Maharashtra, the productivity declined from 90.07 tonnes per hectare in 1999-2000 to 74.37 tonnes per hectares in 2002-03 and sharply to 51.30 tonnes per hectares in 2003-04 mainly under the impact of drought and incidence of while wooly aphid in some areas. In Gujarat and Tamil Nadu, area and production declined in 2003-04, but productivity improved a little. Uttar Pradesh is the largest producer of sugarcane in the country where area and production increased from 20.11 lakh hectares and 115.42 million tonnes in 1999-2000 to 21.49 lakh hectares and 120.95 million tonnes in 2002-03 respectively, but both area and production declined to 20.3 lakh hectares and 112.75 million tonnes in 2003-04 respectively. The fourth advance estimates released by the Directorate of Economics and Statistics on 6th July, 2005 place production of sugarcane in 2004-05 at 232.32 million tonnes which is less by 4.99 million tonnes than the previous season.

(Table 1)

4. The Commission is seriously concerned with the fall in production and productivity of sugarcane. Ways and means must be devised to increase production through increase in productivity of sugarcane, as there are limitations in bringing additional area under sugarcane. The Commission visited the Vasantdata Sugar Institute (VSI), Pune and acknowledged its work and

achievements. The tissue culture laboratory of the institute was engaged in multiplication of selected varieties of sugarcane using tissue culture technique. The Commission was apprised that the plantlets produced through this technique are absolutely disease free and true to their original type and are being supplied to the sugar factories and sugarcane growers for raising breeder's seed nursery in three-tier system of seed multiplication. When the seed nursery was raised using tissue culture plantlets, the seed multiplication ratio of 1:25-30 was obtained as against 1:10 planted using conventional method. The increase in the yield of crop was approximately 20-25 percent. The institute was providing tissue-cultured plantlets at no loss no profit basis (Rs. 4 per piece). The Government of Haryana has informed that the cost of seed raised through tissue culture remains high at about Rs. 18000 per acre as against Rs. 4000 per acre in the conventional method of cane planting. The Commission recommends that ***the Government should examine the cost effectiveness and scope of greater outreach of tissue culture technique, as developed by VSI, Pune for improving sugarcane productivity as well as reducing the cost of production.***

5. The timely availability of credit at reasonable rate of interest to farmers is crucial. It helps them to purchase the required inputs like seed, insecticides etc. and pay for other charges. The sugarcane growers brought it to the notice of Commission that the rate of interest being charged by the cooperative banks is in the range of 11-12 per cent. The representative of the sugarcane growers from Punjab told the Commission that they obtained a loan of Rs. 200 crores from the State Bank of India at 7 percent rate of interest. The Commission is of the view that there should be a ceiling of 7 percent on the rate of interest to be charged on the loans advanced to farmers and the rate of interest should be simple and not compound. Accordingly the Commission recommends that ***there should be a ceiling of 7 percent on the rate of interest to be charged on the loans advanced to farmers by commercial banks as well as cooperatives and the rate of interest should be simple and not compound*****.**

6. The production of sugar is directly related to sugarcane production. In the years of high sugarcane production, sugar produced was also higher and vice versa. The sugar production was 201.32 lakh tonnes in 2002-03 season when the country produced 287.38 million tonnes of sugarcane in the season. With the fall in sugarcane production by 50.07 million tonnes in 2003-04, sugar production decreased by 61.74 lakh tonnes to 139.58 lakh tonnes in 2003-04. The sugarcane production has decreased further by 2.63 million tonnes in 2004-05. Sugar production upto April, 2005 was 129.89 lakh tonnes (including sugar produced by processing imported raw sugar). Because of the shortage of cane, there would hardly be any crushing in the remaining months of the season though processing of raw sugar might continue. Directorate of Sugar has estimated production of sugar in the current season at 130 lakh tonnes as against the estimated internal consumption of 185 lakh tonnes. As a result of fall in the sugar production in 2003-04 and 2004-05 sugar seasons, the closing stocks are estimated at 42.00 lakh tonnes at the end of 2004-05, which would be less than the normative requirement of keeping three months stocks. As per preliminary estimates of State Governments, the sugar industry and the Department of Food & Public Distribution, the sugar production would be about 180 lakh tonnes in 2005-06 sugar season. (Tables 1 & 2)

7. In order to augment domestic supplies and stocks of sugar, the Government liberalized the Advance Licensing Scheme for import of raw sugar to be processed and sold in the domestic market and to fulfill the export obligation in 24 months, which has now been increased to 36 months. This decision of the Government to go for raw sugar import rather than importing refined sugar was a prudent decision especially the phased flow of imported sugar, as there was no abnormal increase in international price when Indian sugar factories contracted for import of raw sugar. Further, the value addition took place in the country. Also, it was possible for sugar factories importing raw sugar to extend the crushing season, which otherwise would have been shorter due to shortage of cane. Since the imported raw sugar was being mixed with sugarcane juice for processing, it might create confusion in determining the exact recovery rate. The scientists at VSI Pune told the Commission that a formula did exist for

determining the recovery rate in such cases. Since the SMP of sugarcane is linked to the recovery rate, the recovery rate of raw sugar importing sugar factories should be carefully calculated. Accordingly, the Commission recommends that ***the Directorate of Sugar should carefully calculate the recovery rate of all those sugar factories which produced sugar by mixing raw sugar with sugarcane juice*.**

8. The "High Powered Committee on Sugar Industry" (Mahajan Committee) in its report submitted to the Government in April, 1998 recommended decontrol of sugar. By decontrol of sugar, the Committee meant only removing levy obligation on sugar factories as it recommended continuance of regulated release mechanism. The Committee also recommended that supply of sugar through Public Distribution System (PDS) should be discontinued and if the Government wished to continue sugar supply under PDS, then the required quantity should be purchased from industry/trade by tendering or at fixed prices. The Government did not accept these recommendations of the Committee and decided to go for complete decontrol of sugar in a phased manner and after setting up of the future markets so as to avoid destabilization of sugar industry. As a step towards decontrol of sugar, the levy obligation on sugar factories was gradually reduced from 40 percent to 30 percent with effect from1st January, 2000 and then to 15 percent and 10 percent with effect from 1st February, 2001 and 1st March, 2002 respectively. The Government announced in February, 2002 that sugar would be completely decontrolled in 2002-03 i.e. by 31st March, 2003. Following this decision of the Government, the millers apprehended that sugar prices would crash on decontrol of sugar as they were carrying large stocks of sugar exceeding 11 million tonnes. They approached courts and obtained release orders for sale of sugar circumventing the release mechanism. This move of the millers upset the market and the market prices of free sale sugar declined by about Rs. 200 per quintal which constrained the capacity of factories to pay cane price to sugarcane growers. Ultimately, the Government had to defer its decision to decontrol sugar by two years and to review the position in February, 2005. The Government also amended the Essential Commodities Act, 1955 in May 2003 to undo the effect of an order of the Allahabad High Court

handed down in March, 2002 wherein the High Court held that the Government had no authority to impose restrictions on the sale of free sale sugar. No doubt, the said amendment restored the authority of the Government to make orders for releases of free sale sugar but the sugar factories have again succeeded in obtaining Court Orders for sale of extra free sale sugar over and above the quota released by the Government. It appears that the sanctity of release mechanism has been completely lost.

9. The setting up of futures markets in sugar was one of the conditionality before decontrol of sugar. The Government allowed futures trading in sugar in May, 2001 and has given recognition to four exchanges viz. National Multi Commodity Exchange Ltd. Ahmedabad with effect from 06.02.2003, M/s e-sugar India Ltd. Mumbai with effect from 25.07.2003, National Commodity and Derivative Exchange Ltd. Mumbai with effect from 27.07.2004, and Multi-commodity Exchange Ltd. Mumbai with effect from 07.02.2005. The futures trading in sugar has already commenced in these four exchanges. Thus, the condition to do away with the release mechanism has already been met.

10. With the lowering of levy obligation on sugar factories, the Government restructured the Public Distribution System in sugar. When the levy obligation was lowered to 30 per cent in January, 2001, the income tax assesses were excluded from the purview of PDS sugar with effect from July, 2001. On further reduction of the levy obligation to 15 per cent in February, 2002, the supply of levy sugar through the PDS was restricted only to BPL families in the country except the north-eastern states, hilly states and island territories where universal coverage was allowed due to their geographical locations and logistics constraints. With restructuring of PDS, the requirement for PDS sugar dropped from about 50 lakh tonnes to about 26 lakh tonnes. Sugar is an essential commodity. It is the duty and responsibility of the Government to ensure availability of a reasonable quantity of sugar to the vulnerable section of the society at a reasonable price. Hence, there is a need to continue with the supply of PDS sugar to targeted groups. The Committee on ‘Revitalization of Sugar Industry’ (Tuteja Committee) in its report submitted to the Government in

December, 2004 has suggested scrapping up of the release mechanism for free sale sugar with effect from 1st October, 2005 but retention of levy obligation of ten percent.

11. During the Commission's interaction with the various stakeholders, a view was expressed that the sugar price would abnormally increase within a few months after decontrol of sugar. They cited the earlier experience when the Government decontrolled sugar in 1978. In the first few months of decontrol, sugar prices declined but skyrocketed thereafter. They were apprehensive that history would repeat itself, therefore they were of the view that the Government should continue to carry with the release mechanism. Their fear is unfounded. The situation was different in 1978. At that time, imports of sugar were restricted and the country faced severe shortage of foreign exchange. Now, imports of sugar are on OGL and the country is having comfortable foreign exchange reserves. In case of any abnormal increase in the sugar prices, sugar imports will flow into the country and lower the domestic prices. The import duty could always be used to regulate imports of sugar. The domestic prices have to be consistent with the international prices. Further, the stock of sugar at close of 2004-05 sugar season would be about 42 lakh tonnes, just enough to meet two and half months requirement. Therefore, it is the right time to dismantle the release mechanism. Accordingly, the Commission recommends that ***the Government should dispense with the regulated release mechanism for free sale sugar while continuing with the levy obligation of 10 percent for supply of sugar through the PDS to protect the interest of the vulnerable section of society*.**

12. As indicated above, the futures trading in sugar has commenced in four exchanges. The futures markets are supposed to perform twin functions of hedging and price discovery. The hedgers reduce their price risk from potential price movements in future. The main participants in sugar contracts in futures are: the sugar mills, traders, commission agents, speculators and processed food manufactures. They have their own perceptions of futures prices and take position accordingly. In the process, the futures price of sugar is discovered.

Initially, the volume in trading in sugar was small but picked up recently. The volumes increased despite uncertainty caused by the mechanism of sugar releases. The Indian Sugar Mills Association informed the Commission that the increase in volume was more as a result of excessive speculative activities and that futures prices were manipulative. The future prices generally converge to or remain in the narrow range of spot prices when the future contract expires. When speculation takes place, the gap between spot and futures price widens. In such a situation, the futures markets fail to perform the function of price discovery. The Commission was informed by the Department of Consumers Affairs and NCDEx that it has been decided that the physical settlement of outstanding positions would be made mandatory on the expiry of future contract, which would curb speculations. It is possible that the volumes may go down with such stipulations but this would be beneficial for all participants as the future price would not be the result of speculative activities. The Commission has already recommended dismantling of release mechanism for free sale sugar. The Commission believes that with the dismantling of release mechanism, there would be substantial increase in volumes in futures trading in sugar.

13. Some of the sugarcane growers argued that when the Government was considering to free the sugar industry from regulated release mechanism, then the Government should also consider allowing sugarcane growers to supply sugarcane to any sugar factory of their choice. Their argument was that the SMP factory-wise varied from factory to factory depending upon recovery rate of the individual factories. The sugarcane growers in the reserved area of a low recovery rate factory received lesser price notwithstanding the quality of sugarcane supplied not being inferior to that of their neighbour sugarcane growers supplying cane to a high recovery rate sugar factory. They suffered for no fault of theirs, therefore they should be allowed to supply cane to sugar factories having higher recovery rate. The Commission appreciates the viewpoint of the sugarcane growers.

14. Sub-clause (1)(a) of clause 6 of the Sugarcane (Control) Order, 1966 provides that the Central Government may, by order notified in the official

gazette, reserve any cane area where sugarcane is grown for a sugar factory having regard to the crushing capacity of the factory, the availability of sugarcane in the reserved area and the need for production of sugar with a view to enabling the factory to purchase the quantity of sugarcane required by it. The Central Government has delegated these powers to the State Governments. The cane Commissioners issue cane area reservation orders allotting cane area to each sugar factory. Sugar factories can draw cane from the allotted area only. The sugarcane growers enter into agreements with the sugar factories concerned either directly or through their cooperative societies for supply of a specified quantity of sugarcane. Sugarcane growers are thus restricted to supply cane to any factory outside the reserved area.

15. The Mahajan Committee looked into the issue of cane area reservation and favoured continuation of the present system of cane area reservation on the following grounds:

(a) *In the absence of system of cane reservation, it will be difficult for sugar factories to regulate the supply of cane by the farmers according to the crushing capacity available on each day.*

(b) *The system of cane reservation enables permanent linkage between the mill and the cane growers which provide the necessary incentive to the mills to undertake the cane development work in its reserved area.*

(c) *In the absence of cane area reservation, a factory would not be sure that the additional cane or cane of better quality produced as a result of its development efforts would not go to another factory thus depriving it of any benefits of its investment in cane development.*

(d) *The system of reservation also helps the cane development work by ensuring that the credit that may be advanced by the mill or by a bank on the guarantee of the mill would get recovered from the cane price at the time of supply of cane to the mill and thus helps the flow of credit to sugarcane growers.*

16. There is a merit in the arguments of Mahajan Committee, but at the same time the above said viewpoint of the sugarcane growers can also not be ignored. At present, the cane area is being reserved for a sugar factory mainly on the basis of its crushing capacity. No regard is paid to the recovery rate of the

factory. On the other hand, the Statutory Minimum Price of sugarcane is linked to the recovery rate. The sugarcane growers of high recovery sugar factories get higher SMP and vice versa. There is a need to encourage sugar factories to improve their recovery rates so that sugarcane growers get higher cane price. It is unfortunate that many sugar factories continue to have recovery rates even below 8.5 percent mainly due to their obsolete plant and machinery. They have not gone for upgradation/modernization despite availability of liberal assistance from SDF. Further, they have done hardly any cane development work in their allotted area. One of the ways in which the sugar factories can be encouraged to improve their recovery rates is to make cane reservation area, inter-alia, on the basis of recovery rate of the factory. Other things being equal, a factory having high recovery rate should get proportionately more cane area than the factory whose recovery rate is less. Such a move would stimulate the factories to go for modernization/upgradation of their plant and machinery and to undertake cane development area resulting in higher recovery rate. Accordingly, the Commission recommends that ***the sub-Clause (1)(a) of Clause 6 of the Sugarcane (Control) Order, 1966 may be amended to make provision for reservation of cane area, inter-alia, on the basis of recovery rate of a factory***. (Table 7)

17. In some states, the cane area reservation is done on year-to-year basis with the result that sugar factories in these states do not take full interest in cane development work in the area allotted to them. The Mahajan Committee recommended that the reservation of cane area should be made on a permanent basis so that mills take keen interest in developing cane in their areas. The Government considered this recommendation of the Committee and decided that the cane area of sugar factories should be on long-term basis for a period of 10 years subject to a review by the State Governments. The basis of such a review could be, inter-alia, capacities of the factories concerned, average crushing rate during the period under review, status of cane price dues, expansion of capacities, establishment of new mills within the permitted radial distance etc. The Commission is in full agreement with the views of the Government on recommendation of the Mahajan Committee and suggests that a provision in this

regard may be made in the Sugarcane (Control) Order, 1966. Accordingly, the Commission recommends that ***the reservation of cane area should be on long-term basis at least for a period of ten years subject to periodical review by the Government for mid way corrections especially keeping in view the need to maintain production efficiency at the factory level and a suitable provision in this regard may be made in the Sugarcane (Control) Order, 1966*****.**

18. It is needless to mention that Indian sugar industry would have to improve its cost efficiency to participate and benefit from trade in global sugar market. The major factors that constitute the cost of production of sugar are: cost of purchasing sugarcane, duties and taxes, conversion cost, recovery level and economies of scale. Of these, the economies of scale have become a very important factor. Now a days, the production is being planned by all industries on large scale to cut down the fixed costs. In sugar also, the new factories being set up are of higher crushing capacity and the existing factories are also increasing the capacities to reap the benefits of economies of scale. As per present norms, the minimum distance between two sugar factories has to be 15 km. This minimum distance was 40 km in 1987. It was reduced to 25 km in 1989. In 1991, the relaxation in area restriction was allowed to 15 km in cases where cane availability so justified. When sugar industry was delicensed in 1998, the minimum distance in terms of 15 km was retained. The Mahajan Committee considered the issue of minimum distance and the Committee expressed the view that the radial distance from an existing mill for setting up of a new sugar factory should be 25 km. The Tuteja Committee has again considered this issue. The Committee did an exercise to work out the cane availability for different radial distance presuming certain parameters. The Committee worked out the cane availability per day at 1809 tonnes, 3217 tonnes, 5027 tonnes, 7239 tonnes, 9854 tonnes, and 12870 tonnes for distance of 15 km, 20 km, 25 km, 30 km, 35 km and 40 km respectively. The Committee also opined that for expansion of capacity beyond 5000 TCD, the additional requirement of sugarcane should accrue through increased productivity and not by expansion of area under sugarcane. The Commission is of the view that if the industry is to

face competition in the world, it has to produce sugar at competitive rates. In the leading sugar producing countries of the world, the sugar factories are of large capacities ranging between 10,000 TCD to 30,000 TCD whereas in India, the average capacity was 3343 TCD in 2002-03. It is possible to have large capacity sugar factories only if adequate cane becomes available in the cane area allotted to sugar factories. As such, the distance between two sugar factories must be sufficiently large. The Commission, therefore, supports the said recommendation of the Tuteja Committee and recommends that ***the minimum distance between the existing sugar factory and new sugar factory may be increased from 15 km to 25 km and a suitable provision in this regard may be made in the Sugarcane (Control) Order, 1966*****.**

19. Clause 5A of the Sugarcane (Control) Order, 1966 also prescribe a formula for sharing profits earned by a sugar factory which in simple terms is R-L/2 where R is realization from sale of levy and free sale sugar and L is the unit cost of production. The L factor is actual cost of producing one unit of sugar and it is declared, *zone-wise*, by the Directorate of Sugar. Based on the L factor and the accounts of sugar factories, the State Governments determine the liability of each sugar factory to pay the additional cane price. Unfortunately, the Directorate of Sugar could not declare the L factor in time in the past. The L factor for 2002-03 sugar season has been recently declared on 20th July,2005. The delay in declaring the L factor in time deprives the sugarcane growers to receive the full cane price in time. The sugarcane growers of Tamil Nadu were agitated on this issue and they blamed the Central Government for the delay. Directorate of Sugar informed that the delay took place because they did not get the requisite information timely from all sugar factories. To overcome this delay, the Government of Tamil Nadu suggested that the power to declare L factor should be delegated to the State Governments. The Commission discussed this suggestion of the Government of Tamil Nadu with the officers of the Department of Food & Public Distribution and it was concluded that Department of Food & Public Distribution would get this suggestion examined. It may be added here that declaration of L factor was not important in the regime of State Advised Prices because the sugarcane growers were getting cane price higher than SMP

absorbing the additional cane price. With the break down of system of State Advised Price, L factor has assumed a lot of significance. Hence, there is a need to declare the L factor in time. The Commission in its report on price policy for 2005-06 has emphasized the need to declare the L factor within three months of the close of sugar season. Directorate of Sugar should instruct sugar factories to furnish the requisite information within the stipulated time, failing which punitive actions should be taken against defaulting sugar mills under the relevant provisions of the Sugar (Control) Order, 1966. The Commission reiterates its earlier recommendation that ***the Government should declare the L factor within three months of the close of a sugar season. Also, the Government should take necessary steps to declare the L factor for 2003-04 sugar season without any further delay. Further, the Government may get the suggestion of the Government of Tamil Nadu examined to delegate the power to declare L factor to the State Governments*****.**

20. A suggestion was made by the Government of Maharashtra that the Commission should fix a premium over and above normal SMP for sugar rich varieties so as to encourage the sugarcane growers to grow such varieties. It was argued in favour of the suggestion that the State Governments of northern India do give premium on early and late varieties. This was opposed by a few sugar factories on the ground that same variety gives different yield in different fields depending upon the inputs applied and weather conditions and also different recovery at different points of time. The Commission considered the suggestion of Maharashtra and it was of views that unlike the northern India states where the State Governments fix the State Advised Price irrespective of the recovery rate, the SMP of sugarcane is linked to recovery rate. With increase in recovery rate, both the sugar factories and sugarcane growers gain equally. The sugar factories gain by way of higher production whereas sugarcane growers get increased SMP. Since the sugar factories and sugarcane growers gain equally with the increase in recovery rate, the Commission is of the view that the fixation of separate premium for sugar rich varieties is not necessary.

21. The price of sugar remained subdued for the past many years. The average wholesale price index of sugar (Base 1993-94=100), which was 145.1 in October, 2000, declined to 136.0 in October, 2001 and to 124.3 in October, 2002. The decline in the average wholesale price index during 2000-01, 2001-02 and 2002-03 seasons was 1.6 percent, 5.22 percent and 9.61 percent respectively. The index touched the lowest level at 115 in April, 2002 when sugar factories sold a large quantity of extra sugar on the strength of court orders. The prices picked up in the middle of 2003-04 but firmed up in 2004-05 season. The increase in wholesale price index during 2003-04 and 2004-05 (upto June, 2005) was 13.63 percent and 15.64 percent respectively. The prices of gur and khandsari moved in tandem with the prices of sugar. Since the excess stocks of sugar have been liquidated and the international prices have also improved, the sugar prices may remain firm in the coming season. Expected buoyancy in the international market in the wake of phasing out of export subsidies by EU may also strengthen border protection. (Table 6)

22. The imports of sugar have been on OGL since 1994. Due to low import duty, considerable imports of sugar took place during 1997-98, 1998-99 and 1999-2000. With the raising of import duty to 60 percent along with the continuance of countervailing duty of Rs. 850 per tonne in February, 2000, the imports of sugar have been checked. The recent imports of raw sugar are under the EXIM Policy of the Government for re-exporting within 36 months and these imports are in no way harmful to sugar industry and sugarcane growers. The present import duty of 60 percent, which is far below the WTO bound rate of 150 percent, safeguards the interest of sugar industry and sugarcane growers, therefore it should continue at the same rate till the domestic prices do not show any abnormal increase.

23. During 1998-99 to 2002-03 sugar seasons, the production of sugar was higher than the consumption with the result that stocks of sugar with sugar factories piled up. The closing stocks at the end of 2002-03 season exceeded 11 million tonnes. In order to liquidate excess stocks of sugar, the Government encouraged export of sugar and gave WTO compatible incentives viz.

reimbursement of internal transport and freight charges w.e.f. 21st June, 2002, neutralization of ocean freight disadvantage w.e.f. 14th February, 2003 and handling and marketing charges w.e.f. 3rd October, 2003. With these incentives, the exports of sugar, which were merely 13 thousand tonnes in 1999-2000 increased to 14.56 lakh tonnes and to 16.62 lakh tonnes in 2001-02 and 2002-03 respectively but decreased to 12 lakh tonnes in 2003-04. The incentives were withdrawn with effect from 21st June, 2004 when the stocks came down considerably due to fall in sugar production in 2003-04 season. The sugar industry represented to the Commission that the claims of many sugar factories on account of exports of sugar have not been settled and paid though the SDF rules provided for settlement of claims within 45 days. The Commission urges to the Government to settle claims of the sugar factories expeditiously and within the time frame allowed under SDF rules. (Table 4)

24. When India exported sugar during 2000-01, 2001-02 and 2002-03, the international prices of sugar were low. The unit value of exports in financial years 2002-03 and 2003-04 was just Rs. 10.64 per kg and Rs. 10.13 per kg respectively, but improved to 13.69 per kg in 2004-05, whereas the unit value of exports in 1997-98 was Rs. 14.11 per kg. It is only recently that the international prices have moved up. The world price of refined sugar (FOB Europe Spot) which was as low as US $ 185 per tonne in October, 2003 increased to US $ 260 per tonnes in July, 2004 and further to US $ 278 per tonnes in June, 2005. One of the reasons for low international prices of sugar was that EU countries flooded the markets with subsidized exports. EU manufactures refined white sugar from sugar beet and had a large export surplus. The subsidized exports from EU affected adversely the exports of sugar from other exporting countries like India, Australia, Thailand and Brazil etc. The sugar industry in these countries approached the WTO against subsidized export of EU sugar and a panel of WTO has ruled in their favour in April, 2005. EU was given 15 months time to comply with the ruling. This was a commendable job done by Indian sugar industry with sugar industry of other exporting countries. The European Commission has recently announced a reform plan for complying with the WTO ruling. The reform plan will reduce the export subsidy to EU sugar producers to a considerable

extent. With reduction in subsidies, EU exports are unlikely to remain competitive because of their higher cost of sugar production and EU countries may have to leave the export market. This would give an opportunity to India and other sugar exporting countries to fill the gap. Unfortunately, Indian sugar factories produce very little refined sugar. They produce plantation white sugar that has limited export markets in neighbouring and Southeast Asian countries. In order to encourage production of raw and refined sugar, the Commission in its report on Price Policy for Sugarcane for 2005-06 Sugar Season recommended that fiscal incentives might be given to sugar factories in the shape of differential excise duty for production of raw and refined sugar. The Government may take decision on this recommendation of the Commission quickly. The Commission feels that the international prices may increase further with the weakening of market presence of EU countries. The rise in international prices will attract the Indian sugar factories to look towards export markets for better price realization. So far, the Government gave export incentives to liquidate excess stocks of sugar and withdrew them when stocks position normalized. This 'off and on' approach does not favour long term strategy for promoting export of sugar. The time has come when the Government should give up its 'off and on' approach and come out with a long-term trade policy. If India is to have its long-term presence felt in the international market, then the export of sugar must be on a sustainable basis. Accordingly, the Commission recommends that ***the Government should formulate a long-term policy for sugar trade to promote exports of sugar on regular, albeit sustainable basis*****.** (Table 5)

25. The State Governments also have to be more proactive in taking initiative to benefit from emerging sugar scenario in the international market. The Government of U.P. has already taken the initiative and has announced an attractive Sugar Industry Promotion Policy, 2004. The State Government has informed that under this industrial policy, an investment of Rs. 2800 crores for creation of 1.4 lakh tonnes TCD is in pipeline for 2005-06 and 2006-07 seasons which include 19 new sugar factories and expansion of existing 12 sugar factories. The Commission feels that the adjoining state of Bihar too has equal potential. Bihar has a glorious past history in sugar industry. At one point of time,

there were 32 sugar mills in Bihar whereas now only 10 sugar mills are working. 15 sick sugar factories were taken over by the State Government in 1975 and 1985 with a view to making them viable units and the management of these mills was entrusted to Bihar State Sugar Corporation, an undertaking of the Government of Bihar. Unfortunately, the efforts of the Government did not succeed. Since the liabilities of the Bihar State Sugar Corporation were far greater than its assets, it has gone into liquidation. Another three sugar mills of British India Corporation (BIC), a Central Government undertaking, are also lying closed. The State Government has informed that consultation are going on with the Central Government to set up six new sugar mills in the State. The Central Government has been requested to re-start the three closed sugar mills of BIC group. Bihar is a poor state and it may not be possible for the State Government to revive the closed units or create new capacities without central assistance. Also, the state has poor infrastructure facilities and northern part of Bihar often gets floods due to release of excess water by the neighbouring country Nepal. Another area of concern in Bihar is its low productivity of sugarcane and low recovery rate. The productivity of sugarcane in Bihar was 40.99 tonnes per hectare as against the all-India productivity of 58.99 tonnes per hectare in 2003-04 season. The recovery rate was 9.36 percent as against the all-India recovery rate of 10.17 in 2003-04 season. Therefore, the new high yielding and high sugar rich sugarcane varieties need to be developed according to the soil and weather conditions of Bihar. The State Government is having Sugarcane Research Centre, Pusa which can do useful research in developing and multiplying the new varieties. The Tuteja Committee has recommended that the institute should be allocated adequate funds for developing new sugarcane varieties. The Commission supports the recommendation of the Tuteja Committee. In view of the aforesaid discussions, the Commission recommends that ***the Central Government should provide a package to the state of Bihar to help the State Government in setting up of new sugar mills and for revival of viable closed sugar mills as well as modernization of existing sugar mills. Also, adequate funds should be made available to the Sugarcane Research Centre, Pusa for development of new high yielding and high sucrose rich***

varieties in collaboration with other public and private research institutions in the country.

26. Sugarcane is a labour intensive crop. The cost on account of human labour constitutes a major part of the total variable input cost. As per information available from Labour Bureau, between April 2004 and March 2005 the actual wage rates for agricultural labour have increased marginally or declined in the major sugarcane growing states. While the increases are in the range of 1-1.5 per cent in the states of Punjab, Tamil Nadu and Maharashtra, in Andhra Pradesh, Uttar Pradesh and Karnataka the wage rates have actually declined. The prices of farm inputs, between July 2004 and June 2005, as indicated by Wholesale Price Index are observed to have increased by a low margin of about 3 per cent for fertilizers and 2 per cent for pesticides. The prices of petro-based inputs like high speed diesel (HSD), light diesel oil (LDO) and lubricants have also registered an increase over the previous year. (Tables 8 & 9)

27. After the submission of the Commission's last report on price policy for sugarcane for 2005-06, fresh estimates of cost of cultivation/production of sugarcane generated under the Comprehensive Scheme (CS) by the Directorate of Economics & Statistics pertaining to the year 2003-04 are available for the major growing states of Andhra Pradesh, Haryana, Karnataka, Maharashtra, Tamil Nadu, Uttar Pradesh and Uttaranchal. Between 2002-03 and 2003-04, the estimates of cost of cultivation of sugarcane as measured by A_2+FL and C_2 have increased for Haryana and Karnataka while the same have registered a decline for all the remaining states. The decrease in the C_2 cost of cultivation is about 18 per cent for Uttaranchal, 17 per cent for Andhra Pradesh, 15 per cent for Maharashtra, 11 per cent for Uttar Pradesh and less than one per cent for Tamil Nadu. In Karnataka the C_2 cost of cultivation has increased by about 12 per cent whereas in Haryana it is almost the same as the previous year. The average yield of sugarcane per hectare in respect of sampled units of CS has increased by 26 per cent in Karnataka,16 per cent for Haryana and between 2 to 2.6 per cent for Uttaranchal and Tamil Nadu. However, the average yield has decreased

by about 24 per cent in Maharashtra,8 per cent in Andhra Pradesh and less than one per cent in Uttar Pradesh in the corresponding period. (Tables 10 & 11)

28. The estimates of cost of production of sugarcane of various states have been projected for the ensuing season on the basis of the same methodology adopted by the Commission in the past few years. A variable input price index has been constructed for each state covered by the Comprehensive Scheme on the basis of the actual input price movements observed so far and assuming an expected inflation rate of 5 per cent. As per the present practice, the cost estimates pertaining to the latest three years are projected and then the averages of the projected costs are considered. In the absence of 3 years continuous CS data for Uttaranchal, the state has been kept out of the projection regime. Thus, the C_2 cost of production of sugarcane for 2006-07 is projected to an average of Rs.78.49, Rs.77.77, Rs.68.78, Rs.77.98, Rs.68.76 and Rs.73.63 per quintal respectively for Andhra Pradesh, Haryana, Karnataka, Maharashtra, Tamil Nadu and Uttar Pradesh. The weighted average C_2 cost of production on the basis of production weights for TE 2003-04 then works out to Rs.73.76 per quintal for 2006-07. (Tables 12 & 13)

29. The above projections are based on the average yields of sample holdings for the years 2001-02, 2002-03 and 2003-04 for the concerned states. When adjusted to 9 per cent recovery rate using state specific average recovery rates for the TE 2003-04, the C_2 costs of production for 2006-07 work out to Rs.69.46, Rs.70.20, Rs.60.27, Rs.63.80, Rs.63.15, Rs.70.50 per quintal respectively for these states. On this basis, the weighted average C_2 cost of production adjusted for 9 per cent recovery is projected at Rs.67.33 per quintal.

30. Some State Governments also provide estimates of cost of production/cultivation based on their own surveys. These data are examined at length and compared with the corresponding CS data and also with the subsequent projection made on the basis of this data by the Commission for the ensuing season (2006-07). Despite certain conceptual and methodological differences between the data supplied by the states and those provided by the

DES due to which they may not be strictly comparable, the data provided by the states are found to be useful in many ways. Andhra Pradesh and Tamil Nadu have provided estimates of cost of production of sugarcane for 2003-04 and 2004-05 while Maharashtra has provided the same for 2003-04. The cost of production provided by Andhra Pradesh at Rs.99.30 and Rs. 90.20 per quintal respectively for the years 2004-05 and 2003-04 is inclusive of the transportation charges. After discounting for the transportation charges these estimates work out to Rs.87.91 and Rs 80 per quintal which are on the higher side as compared to the CS estimate for the year 2003-04. The difference may be attributed to the higher input costs considered by the state. Item-wise comparison of inputs is not possible as the format used by Andhra Pradesh is not strictly comparable with CS format. Tamil Nadu has estimated the cost of production at Rs.59.74 per quintal for 2004-05 which is also inclusive of the transportation cost. After making necessary adjustments, the cost of production for Tamil Nadu works out to Rs.55.78. As against this, the CS estimate for the year 2003-04 for the state is Rs 63.71 per quintal and the Commission's projection for the state for the ensuing season is Rs.68.76 per quintal. Haryana and Maharashtra have provided cost projections for 2006-07. The cost projected at Rs. 106.96 per quintal by Haryana is higher than that projected by CACP. Haryana has included additional costs on account of management and transportation charges. After making necessary adjustments, the cost projection works out to be Rs. 93.60 per quintal for the state. This adjusted cost is higher than CACP's projection due to higher charges on account of human labour, seed, insecticides, irrigation etc and also land rent considered by the state. In the case of Maharashtra, the cost projected by the state is Rs. 109.82 per quintal which is inclusive of 15 percent profit to the farmers, transport, market and supervision charges. After adjustment, this works out to Rs 74.74 per quintal. As against this, Commission's projection for the state works to Rs 77.99 per quintal for 2006-07 season. (Table 14)

31. While fixing the SMP, the cost of transportation is be added to the total cost of production. After examining the transportation charges for sugarcane by various modes of transportation received from states, the all India average

transportation cost for the year 2006-07 works out to Rs.12.50 per quintal approximately.

32. Sugarcane farmers have been repeatedly raising issues regarding the valuation of family labour, inclusion of transportation, marketing charges and risk coverage in the cost while formulating the Price Policy recommendations. These issues have been examined in detail by the Alagh Committee and the report of the committee has already been submitted to the Government for consideration.

33. Thus, considering all the relevant factors, namely costs of production, demand-supply situation of both sugarcane and sugar, trends in market prices of sugar in domestic as well as international markets, and having regards for the factors mentioned in Clause 3 (1) of the Sugarcane Control Order, 1966 and the need to encourage sugar industry to reach out to international market on sustainable basis, especially in the wake of diminution of European Union, the Commission recommends that ***the Statutory Minimum Price (SMP) of sugarcane payable by sugar factories for 2006-07 sugar season be fixed at Rs. 79.80 per quintal for a basic recovery rate of 9 per cent subject to a premium of Rs. 0.90 for every 0.1 percentage point increase in the recovery above that level. At the All-India average recovery rate of 10.17 per cent achieved in 2003-04 season, the SMP recommended comes to Rs. 90.33 per quintal***.

(T. Haque)
Chairman

(K. Ponnukannu)	**(M.S. Grewal)**	**(Rajiv Mehta)**
Member (Official)	**Member (Non-Official)**	**Member-Secretary**

August 3, 2005

सत्यमेव जयते

Confidential

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Dated: 12th June, 2006

Dear Shri Verma,

Kindly refer to your D.O. No. 3(1)/2005-SP dated 25.05.2006 regarding the report of CACP for Sugarcane for the sugar season 2006-07 and the affect of increases in the price of diesel on the MSP.

Since the submission of the above mentioned report the diesel prices had undergone two revisions, in September, 2005 and on 6th June, 2006. Consequently the overall cost of production of sugarcane for the season 2006-07 is estimated to be increased by Rs.0.45 per quintal.

With regards,

Yours sincerely,

(Rajiv Mehta)

Shri Abinash Verma,
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