

Subject: Press Note – FAI Annual Seminar – 2019 on New Approach to Fertilizer Sector

1. Background

- 1.1. India will surpass China as the world's most populous country by 2027 and by 2050, India will have a population of 170 crore (1.7 billion). Requirement of food grains by 2050 will be 400 million tonnes against the current production of 285 million tonnes. Thus, food security of the ever-expanding population will remain an important national agenda for our country.
- 1.2. Requirement of total fertilizer nutrients is estimated to be around 60 million tonnes by 2050 (comprising of 45 million tonnes of chemical fertilizers and 15 million tonnes of organic and bio-fertilizers) as against the current nutrient consumption of 34 million tonnes (containing 27 million tonnes of chemical fertilizers and 7 million tonnes of organic and bio-fertilizers).
- 1.3. In view of huge requirement of nutrients, the total nutrient needs of Indian soils cannot be met only through organic and bio sources. This is particularly true in view of inadequate availability of organic manures and very low levels of nutrient content in the organic fertilizers. Chemical fertilizers will thus continue to play a major role. But, carbon content supplied by the organic fertilizers is important for physical, chemical and biological properties of the soil. In fact, use efficiency of chemical fertilizers increases when used in combination with organic manure.

2. Issues faced by domestic fertilizer industry

2.1. Urea:

- 2.1.1. The fixed cost of urea units continues to be reimbursed on the basis of 2002-03 cost data. Since then, there has been steep increase in these cost elements, which remain unrecognized and unpaid under the existing policies.
- 2.1.2. Modified NPS-III policy notified in 2014 allowed a nominal increase of Rs.350 per MT of urea, minimum fixed cost of Rs. 2300 per tonne and special compensation of Rs. 150 per tonne to gas based plants more than 30 years old. But, this amount is yet to be paid even after a lapse of 5 years. Non-payment of dues as per Modified NPS-III policy has a cumulative impact of Rs.5600 crore for the past five years. There has been further increase in fixed cost elements which remains un-recognised under the policy.
- 2.1.3. Energy consumption norms have been reduced 4 times after implementation of NPS policy in 2003. It started with 2004 (NPS-II), followed by 2006 (NPS-III) and again under New Urea Policy (NUP) in 2015 and 2018. This has been done without recognising investments made for achieving such energy efficiency. The mopping up of energy norms is against the NPS policy that assured that neither capital expenditure would be recognised, nor efficiency improvements would be mopped up.

2.1.4. Impact of energy reduction from 2004 till 2018 is Rs.4300 crore per annum based on current energy prices. Further reduction in energy norms is proposed *w.e.f.* 1st April 2020 which would have further negative impact of Rs.2300 crore per annum.

2.1.5. Share of domestic gas in total gas supply to the fertilizer companies has declined from 76% in 2012-13 to around 30% currently.

2.1.6. New investment including revival of 5 closed units of FCI and HFC are in progress with an investment of more than Rs. 40,000 crore. This would make India self-sufficient in urea production, provided production from existing units continues. Restoring health of existing urea plants makes strong economic and commercial sense for the country, as these plants are supplying urea at much lower cost than the new plants and are also cheaper than imports.

3. P&K Fertilizers

3.1. Domestic manufacturing in P&K fertilizers is suffering due to unfavourable and inverted tax structure for raw materials/intermediates *vis-à-vis* finished fertilizers. Customs duty on phosphoric acid and ammonia is 5% which is same as on finished fertilizers. Customs duty on rock phosphate and sulphur is 2.5%. Import duties on raw materials/ intermediates increases the cost of domestic manufacturing making them uncompetitive compared to imports. Similarly, inverted GST rate on ammonia and sulphuric acid at 18% compared to 5% on fertilizers increases the cost of domestic production. Subsidy rate is same for domestic and imported P & K fertilizers, providing no incentive for domestic value addition.

4. Payment related issues

4.1. Implementation of DBT assured weekly payment of subsidy. However, this assurance is not kept due to persistent budget constraints. Implementation of DBT has postponed subsidy payment by another 6 months because now it is linked to sale of fertilizers through POS machines. Earlier it used to be paid on receipt of material in the district. This has increased working capital requirement and interest cost. The fertilizer companies were also assured of clearing the pending backlogs of subsidy dues before implementation of the DBT model. This assurance has also not been honoured as large amounts of dues continue to remain pending outside the DBT system.

4.2. As per the information provided by 25 fertilizer companies, a total of Rs. 33,691 crore dues are pending as on 1st November, 2019. Out of this, Rs. 20,853 crore is under DBT and balance Rs. 12,838 crore is other than DBT. Rs. 20,434 crore dues are pending for which bills have been generated but not paid and the balance Rs. 13,257 crore are pending for which fertilizer companies are not able to generate bills. The carry forward subsidy dues since 2015-16 are:

Year	Amount (Rs. Crore)
2015-16	43,356.23 [#]
2016-17	39,057.11 [#]
2017-18	32,053.21 [*]
2018-19	39,053.21 [@]
2019-20	60,000 ^{@@}
As on 1.11.2019	33,691 ^{&}

Source: # = Department of Fertilizers

*= Compiled at FAI based on data of 23 fertilizer companies

@ = Compiled at FAI based on data of 28 fertilizer companies

@@ = Estimated

& = Compiled at FAI based on data of 25 fertilizer companies

= Interest cost is estimated based on 10% annual interest and assuming that unpaid subsidy dues remain pending for 6 months in a year.

4.3. Subsidy comprises 78% of cost of urea. Increase in working capital requirement and consequent increase in interest cost due to implementation of DBT is yet to be recognised in the urea policy. Urea units cannot recover this cost from farmers through increased MRP because MRP is fixed by government.

5. Direct Benefit Transfer (DBT)

5.1. The present model of DBT for the fertilizer sector is not a true DBT, as fertilizer subsidy still continues to be routed through the industry. There is no road map at present to take it to its logical conclusion i.e. transfer of subsidy into farmers' accounts.

6. Impact of prevailing policies on stakeholders

6.1. Impact on domestic urea industry

6.1.1. Policies and their implementation have badly impacted viability of Indian urea plants. 50% of operating units are already running under losses. Rest of the plants are running at wafer thin margins and are likely to run into red unless corrective measures are taken immediately. The industry as a whole is having a negative margin on net worth as shown in the table below. Undue delay in payment of subsidy and resultant cash crunch has already forced two major urea plants to suspend/reduce production.

Table: Negative Return from Urea Manufacturing activities

Particulars	2014-15	2015-16	2016-17	2017-18	2018-19
Profit After Tax (PAT)-excluding provisions of Modified NPS-III Policy (Rs. Crore)	-684.28	-213.27	-108.53	-841.80	-736.69
Profit After Tax (PAT)-including provisions of Modified NPS-III Policy (Rs. Crore)	49.33	629.39	761.04	-4.82	71.46
PAT as % of Net-worth – excluding provisions of Modified NPS-III Policy	-4.43%	-1.44%	-0.73%	-6.14%	-5.43%
PAT as % of Net-worth – including provisions of Modified NPS-III Policy	0.28%	3.51%	4.23%	-0.03%	0.43%
Note: Based on the data received from 25 urea units. Fertilizer Policy envisaged Post Tax return of 12% on Net-worth.					

6.2. Impact on P&K fertilizer industry

6.2.1. Due to unfavourable taxation regime, the capacity utilisation of domestic phosphatic (P_2O_5) fertilizers has been declining from 72% in 2010-11 to 65% in 2018-19. There have been only marginal capacity additions of 5 lakh tonnes in this sector in the past five years.

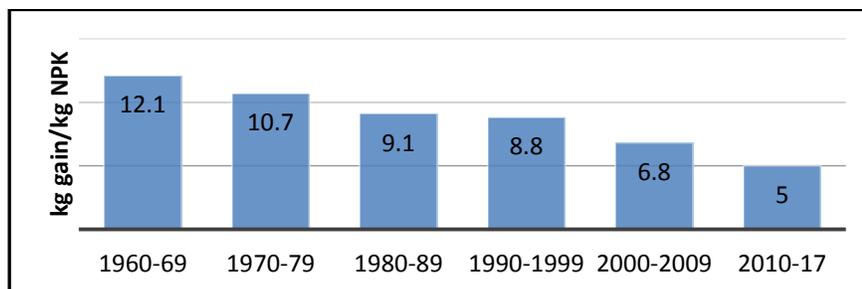
6.3. Impact on agriculture & farmers

6.3.1. The ratio of MRP of DAP to urea changed from 1.9:1 in 2009-10 to 4.1 :1 currently. Similarly, ratio of MRP of MOP to urea changed from 0.9:1 to 3.2:1 during the same period. This has led to excessive use of highly subsidized urea in comparison to P&K fertilizers.

6.3.2. The NPK use ratio widened from 4.7:2.3:1 in 2010-11 to 6.6:2.6:1 in 2018-19. Retail price of urea in India is among the lowest in the world.

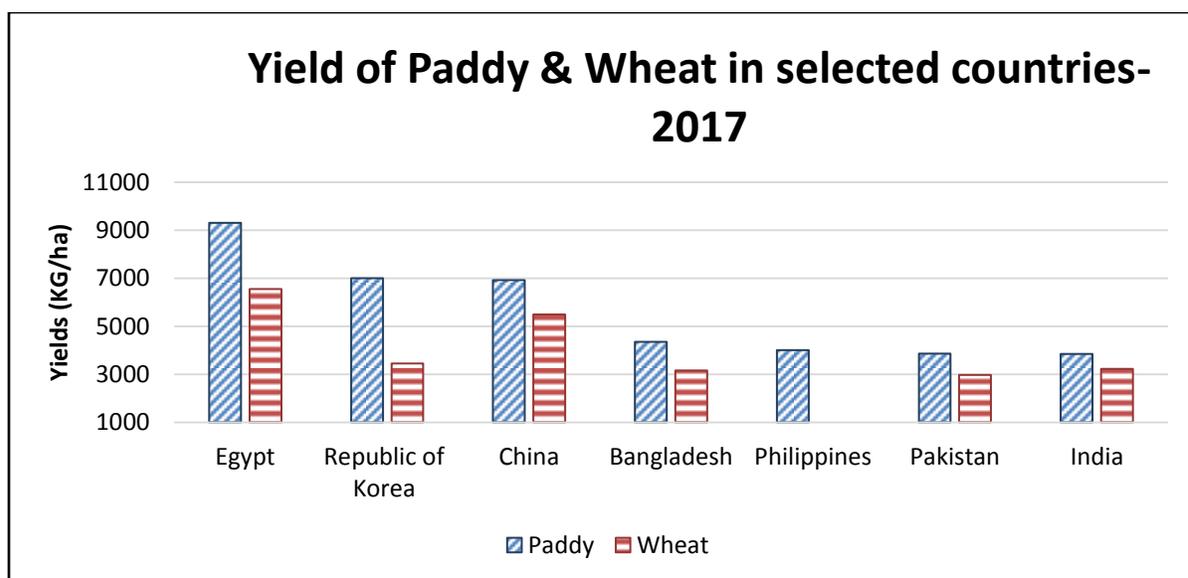
6.3.3. Crop response ratio (kg grain produced/kg NPK applied) has fallen sharply over the decades from 12.1 during 1960-69 to 5 during 2010-17 (see chart below).

Figure 3: Trends in response to NPK (kg grain / kg NPK)



Source: Katyal J.C. (2019) *Indian Journal of Fertilizers* 15(12), pp 1384-1401

6.3.4. This has resulted in stagnant crop yields. Indian crop yield levels are lower than many of the developed countries and even some of our neighbouring countries, as given in the chart below:



Source: (i) www.fao.org (ii) *Fertilizer Statistics 2017-18, FAI*

6.4. Impact on Environment

6.4.1. Imbalanced use of fertilizers nutrients has also given rise to environmental concerns. Particularly, nitrogen management in agriculture has assumed global importance.

7. What is needed

7.1. Measures to restore soil health, improve agricultural productivity and farmers' income

7.1.1. Government has tried to address the issue of imbalanced use of plant nutrients. These include distribution of soil health cards, neem coating of urea, resizing of urea bags from 50 kg to 45 kg. But, these measures have not given desired results. Obviously, price of urea remains an overriding factor in the pattern of farm nutrients.

7.1.2. There is a need for a major course correction. The instrument of subsidy needs to be used in promoting balanced and integrated use of all fertilizer nutrients through all sources including chemical fertilizers, organic manures, bio-fertilizers, secondary and micronutrients.

7.2. Measures needed to restore domestic fertilizer industry

7.2.1. Immediate measures

- Payment of revised fixed cost to urea units as per Modified NPS-III Policy notified in 2014.
- Policy for index based automatic revision in fixed cost beyond 2008-09.
- Extension of existing energy norms till NBS Policy/DBT is implemented for urea.
- Adequate budget allocation to clear all outstanding dues of the past and meet current requirement.
- Addressing unfavourable taxation issues by exempting raw materials/intermediates for P&K fertilizers from customs duty and reducing the rate of GST on ammonia and sulphuric acid at least to 12%.

7.2.2. Medium term measures

- Implementation of NBS Policy for urea. With gas pooling and rationalisation of energy norms reducing the heterogeneity among cost of production of urea units to a large extent, NBS in urea is now practically workable.
- Implementation of DBT in true sense by transferring fertilizer subsidy directly to the bank account of the farmers. Government is already successfully transferring Kisan Samman Nidhi to the bank accounts of farmers. Hence, DBT for fertilizer subsidy is also fully workable now.

8. FAI Annual Seminar

8.1. With the above background, this year's FAI Annual Seminar 2019 has been devoted to the theme 'New Approach to Fertilizer Sector'. It is likely to be attended by more than 1200 delegates including about 150 delegates from abroad. The seminar will be inaugurated on 2nd December, 2019 at Hotel Andaz Delhi, Aerocity, New Delhi, followed by technical sessions in the next two days ending with valedictory session on 4th December, 2019. In all 19 papers will be presented during the seminar by eminent speakers comprising policy makers, industry leaders and experts from national and global institutions.

8.2. We invite you all to participate in this 3-day event including inaugural function on 2nd December, 2019, technical sessions in the next 2-days and the valedictory session on 4th December, 2019.
