Farmer Producer Companies in India

Does Aggregation lead to Prosperity?

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A consultation was held on the above topic on September 13, 2019 at the RGICS. The following is a report on the Consultation:

Introduction

In India, the dependence of a high proportion of population on agriculture has remained even after almost three decades of economic reforms. In 2015-16, 42.5% of the total employed population of the country (in Primary sector, which is mainly agriculture) produced 12% of the value in the economy! This proportion has been in a consistent fall since the early 1980s.

Due to a number of reasons, Indian farm sector has been under distress from many years. "At least 270,940 Indian farmers have taken their lives since 1995, NCRB records show. This occurred at an annual average of 14,462 in six years, from 1995 to 2000. And at a yearly average of 16,743 in 11 years between 2001 and 2011. That is around 46 farmers' suicides each day, on average. Or nearly one every half-hour since 2001" (Sainath 2013).

A survey conducted by Centre for the Study of Developing Societies (CSDS), Lokniti, for Bharat Krishak Samaj in 2013-14 revealed that around 75% of farmers would prefer some other work than farming. It also pointed out that around 60% of farmers want their children to migrate and settle in a city. A huge proportion of these were landless, marginal and small landholders (Mukherjee 2014).

Under the current system, there seems to be a structural flaw. The producers of primary sector, especially farmers, have been divorced form the value addition that undergoes from farm gate to end consumer. In addition, the farm produce and remuneration for small and marginal landholders remains precarious given unpredictability of extreme climate variations, rising input costs, depressed prices, etc.

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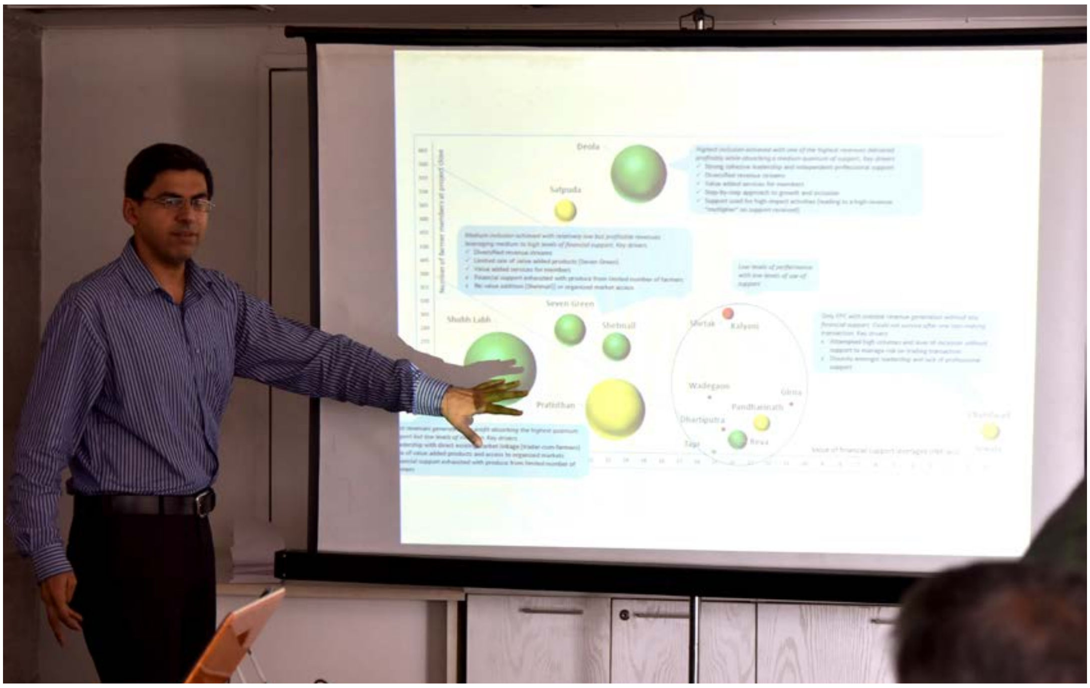

Mr Aman Khanna, Consultant, Asian Development Bank sharing experience of FPCs in Maharashtra

In last four decades, India has become a food surplus country, and there are hardly any food commodities that are not exported from here. Given such circumstances, the current approaches to increase farmers' incomes through increasing productivity and using high yielding varieties, etc., may not be the best way possible. At best, there is a high risk of glut in the market that further depresses prices.

Background

There is a growing need to reposition farmers as owners of complete value chain rather than just producers of raw material for whole of food production system. Farmer Producer Companies or FPCs are one of the institutional solutions devised in India, to do just that. This brief report outlines learnings from a consultation held at Rajiv Gandhi Institute for Contemporary Studies, New Delhi in September 2019. After a brief background to the concept of farmer producer companies, the report is divided into two sections, one describing the experiences from four states viz. Maharashtra, Gujarat, Madhya Pradesh and Uttar Pradesh. The second section explores the feasibility of the concept and deliberates on potential solutions to address bottlenecks hindering the concept from realising its potential.

Cooperatives became the most popular form of institutional mechanism to generate collective action even before independence. A large number of cooperatives were formed oriented towards helping the neediest. After Independence, cooperatives became integral to planned development in India. The concept was widely used to increase agricultural production, and delivered good results during initial years. Over time, the nature of organisational structure and excessive state control led to appropriation of power by a few vested interests. In essence, apart from a few tremendous success stories, largely the cooperatives became den of evil that it was envisioned to counter.

Among small and marginal holdings, a relatively larger proportion of operational holdings are cultivated (92% and 91% respectively) as also relatively higher proportion on them is irrigated (52% and 47% respectively). These two inputs bring to fore that marginal holdings manage relatively superior quality of agricultural lands for higher productivity per acre. This is established through higher cropping intensity in the smaller group of operational holdings in relation to large size holdings.

Post liberalisation, need for a new institutional form was felt to reactivate collectivist idea in the agriculture sector specially to realise the value that small and marginal landholders can produce. As a result, a farmer producer company concept came into being with substantial improvements over cooperative form (Please refer Table 1).“A provision for setting up FPCs was made in the Companies Act, 1956 in 2003 by an amendment to the Act. Despite efforts by the government over the past 15 years or so, including major financial help, the country has just about 3,000 FPCs so far.”(Bhosale 2018)

There have been many positive developments recently that believe in the promise of the concept of FPCs. In July, Union Budget made clear the intention of Central government to promote 10,000 FPOs in the country over next five years, perhaps in hopes of addressing the agrarian distress under the promise of doubling farmers’ incomes. Nonetheless, it has certainly caught the attention of the stakeholders, and there is focused interest to explore and utilise the market potential of FPOs in general and farmer producer companies in particular.

Status and Experience of FPCs from 4 States

Maharashtra

Mr Aman Khanna, Consultant for Asian Development Bank (ADB), conducted an assessment study in Maharashtra. ADB created and supported 18 FPCs in the state by deploying funds from Japan Fund for Poverty Reduction (JFPR) grant from 2012 to 2018. The study aimed to compile experiences of FPCs supported for commercialisation under the grant; derive lessons learnt; and make recommendations for future support exercises by development partners/ aid agencies aimed at commercialisation of FPCs.

The experience form Maharashtra demonstrated that a number of factors impact performance of FPCs. Factors such as presence of experienced individuals on Board of Directors, external professional support deployed, extent of value addition or servicing of organised markets, were important. The diversification of income sources; incremental approach to planned growth; value of commodity produced; and amount of financial aid (by JFPR) absorbed; were other factors that were found to be correlated with performance of FPCs.

The following learnings from Maharashtra were shared by Mr Aman Khanna.

- It was found that cases where membership of FPCs increased steadily based on their performance after starting off with small number were more successful. In other words, the experience of business and catering to physical and logistical challenges, leads to sustainable capacity to absorb more members.
- Capacity building and financial support are required by an FPC simultaneously to sustainably enhance operations.
- Professional management and governance of FPCs is crucial. This required for two reasons. One, to plug the crucial capacity gap to carry out large transaction as a business. And two, to avoid the conflict of interest when ownership and management co-exist, which has often led to catastrophic results for the organisation.

- Since, FPCs operate in diversity of circumstances, location and market milieus; it is observed that blanket support schemes may not be the best bet to support FPCs. It is required that FPCs receive support catering to their unique requirement at ay give point in time.
- Absence of clear and consistent criteria for selection of Board of Directors often leads to inability to overcome disagreements and eventually closing of operation of the organisation.

Gujarat

Mr Kuldeep Solanki, Interim CEO, GUJPRO Agribusiness Consortium Producer Company Limited shared FPC experience from the state of Gujarat. GUJPRO is a consortium of 27 FPOs across 11 districts of Gujarat, and based in Ahmedabad. GUJPRO deals with farmers of mainly 5 commodities and offer different services for the same, like, procurement and processing of groundnut; procurement of oilseeds and pulses under MSP scheme; trading in cumin; and marketing support to mango growers. GUJPRO does high volume procurement for agencies like NAFED, SFAC, etc. They have also entered in an agreement with a private company for procurement, processing to supplying of final groundnut products. Farmers associated with GUJPRO earn a minimum of 3-4% premium over market price.

Key challenges faced by FPCs of GUJPRO are as listed below.

- Poor capacity of FPCs and low understanding of the business side of the FPC by members as well as Board members. Here, promoting institutions have also been seen lacking in having or transmitting requisite knowledge. Most FPCs have done well in agro-input production and doing business with farmers. However, there is lack of understanding or rooting in market business.
- Low level of initial equity becomes a bottleneck for expanding business in initial years. It is further exasperated by lack of access to formal capital. If capital is not available within initial 2-3 years of operation, most FPCs slip into inactivity.
- Professional human resource for management of affairs is unviable for small or medium level FPCs.
- Risk appetite of the members remains low, especially among new FPCs. It limits scope of activities under operation, usually FPCs remain stuck to input production.
- Limited cycles per year due to area being rain fed impacts turnover of the organisation directly. Commodities like milk or vegetables have higher flexibility of absorbing shocks.
- Development of good leadership is rare, and often impacts governance.

Way forward identified by GUJPRO experience:

- Capacity building of promoting institutions and FPCs, most importantly to generate capital for operations. Enhance patronage, maybe even by sharing produce with the company of not profits.
- Handholding support is required at ground level by experts post classroom type training.
- Design of FPC in terms of size, scope and scale must be catered to specific factors such as commodity, location, infrastructure and market distance, etc.
- Access to capital needs to be enhanced. In event of lack of it by scheduled banks

- Primary processing must be done locally to increase benefit to farmers. Higher level of value addition must be done at aggregated level by FPCs or federations.
- Village level scientific storage models are required that are strongly backed with technology. It would ensure better price discovery and sale, avoiding market uncertainties.
- FPCs must engage with members more vigorously and ensure higher patronage and higher holding in the FPC, which will enable solutions to a few challenges.

Madhya Pradesh

Mr Yogesh Dwivedi, CEO, Madhya Bharat Consortium of Farmer Producer Company Limited (MBCFPCL) shared experience from the state of Madhya Pradesh. MBCFPCL is a consortium of 108 FPC operational in Madhya Pradesh, having reach to over 174,000 small farmers in 43 districts. MBCFPCL is engaged primarily in commodity trading including aggregation, storage and primary processing; seed production and marketing with member FPCs; and backward integration for inputs to members. Additionally, the organisation is engaged in supporting members for credit linkages and infrastructure development; supporting in IT enabled management solutions and meeting statutory compliances; and support in capacity building of member FPCs.

MBCFPCL works with government agencies like NAFED, SFAC, State Agricultural Universities, etc. and also corporates like ITC, Britannia, Parle, etc. In last four years, the turnover has increased from around INR 71 Cr to 150 Cr, paid up capital has increased from INR 16 lakhs to 50 lakhs. However, such a glamorous increase has not been observed in total profits which increased from around 1 lakh to 6.5 lakhs only. It is also learned that farmers associated with 41 FPCs of the consortium earned additional income of INR 4,000 to 15,000 per season.

The state has 148 FPCs, of which around 60% are actively in operation having a total of INR 252 Cr annual turnover. Growth of FPCs business can be divided into three phases based on their average growth rate: 2006-2010 with >25% (total 15 FPCs); 2011-2016

Mr Yogesh Dwivedi, CEO, MBCFPCL shares journey of FPCs in Madhya Pradesh with ~15%; and post 2016 with <10% (±5% based on weather related uncertainties). A significant majority of first phase FPCs (13/15) are doing well without any external support since 2010. A considerable transformation has taken place among member farmers of FPCs, often earning 2-3 times more than they were earning in mid 2000s.

There were many peculiarities that led to high growth of FPCs in the first phase. Participatory varietal selection program (PVSP) done by ASA in association with MP District Poverty Initiative Program (DPIP) created awareness among farmers regarding agri-business model for seed production and prepared them for market oriented initiatives. A sustained financial support by SFAC proved crucial. A number of agencies facilitated timely capital availability. The state government's support in the form of allotment of land, construction of infrastructure using various schemes proved helpful. In addition, FPCs were authorised to supply seeds under government schemes which reduced the risk of new FPCs and allowed them to establish themselves. There was also a group of professionals at the helm of these FPCs who were well versed with local issues and linked with the community.

As per Mr Dwivedi, following challenges are faced by FPCs in Madhya Pradesh:

- High quality of appropriate (willing to work for FPCs in rural areas) and experienced human resource is not available to FPCs. Institutional ecosystem for creating such human resource is missing.
- High risk factor, especially in rain fed areas, restricts the horizon of operations and hinders investments in value additions.
- Support to invest in large scale processing and value addition plant and machinery is not available.
- Credit availability at competitive rates is a big challenge and FPCs have to rely on NBFCs for their capital needs.

Uttar Pradesh

Mr Rajnikant Prasad, AVP, Basix Uttar Pradesh, shared experience form state of Uttar Pradesh. Mr Prasad, along with his team, has promoted around 120 FPCs from 2011 onwards across 29 districts of the state with around 80% of associated farmers being small and marginal landholders. There 11 major commodity specific clusters

As outlined by Mr Prasad, following challenges were faced by FPCs promoted by Basix in Uttar Pradesh:

- The awareness towards and acceptance of the new institutional form took a long time, not only among farmers but also other stakeholders such banks, input marketing companies, etc.
- The working capital remained a challenge for almost all of the FPCs which hindered forward and backward linkages, meeting initial fixed costs, investments in infrastructure for value addition, etc.
- Skilled professionals for management of affairs of FPCs are not available.
- Lack of leadership in FPCs and within Board of Directors, coupled with low level of financial literacy and business orientation.

Way forward identified by Basix experience in Uttar Pradesh:

- Allowing two types of shares in FPCs – one with voting rights that are exclusive to

Mr Ashis Mondal, Director, Action for Social Advancement (ASA), making critical inputs at the event

the producer members, and second without voting rights to investors.

- Compliance requirements may be relaxed for FPCs and made different than private limited companies.
- Merging of FPCs or creating federations may additionally enhance economies of scales.
- Creating formal linkages with banks for making capital available at lower rates and decrease reliance on NBFCs.

Based on the experience of these states and the discussion held at the consultation, these functions/ services of the producer companies can be categorised into following core focus areas which need attention from policymakers and other stakeholders.

- Capacity building- Capacity building includes form the aforementioned list of functions - support on organisational services, technology services, education services, and management of resources.
- Capital/financial markets- It includes support on financial services i.e. various mechanisms of creating capital for long term sustainable growth.
- Connections- It includes the production services, and marketing services as mentioned in the above list, and some services in technology and education too.
- Miscellaneous- These areas cannot be appropriately fitted into above mentioned categories. Nonetheless, these are important to achieve the stated goals of an FPC.

These core focus areas are delved into some detail, exploring the major inhibitors and the way forward to address the same. These are based on discussion during the consultation, available literature on the subject and separate consultations with a few experts.

Capacity

The concern which echoes in most discussions around FPCs is their inability to understand business side of things, or lack of entrepreneurial culture, which often leads to unviable transactions in the initial phase with worst of downside risks playing out. It is often linked to the promoting institutions' lack of capacity beyond mobilising farmers to form an FPC, and also to tendency of resource institutions to not being able to transfer those skills creating a dependency. Lack of capacity also exists in understanding the institutional form of FPC by member producers and also the Board of Directors, often failing to meet statutory compliances.

It can be noted that the areas where FPCs require capacity building are independent of peculiarities that exist with regard to commodities that they deal with and building value chain. There exists an opportunity to easily aggregate such functions of capacity building geographically, may be at a regional level or state level. It will separate out functions which cannot be aggregated geographically and require particular support. Hence, specific verticals of capacity building can be addressed separately.

Mr Ashish Mondal, Director of Action for Social Advancement (ASA) shared their attempt to do something similar. ASA has created Centre for Incubation and Support for Smallholder Producers' Organisations (CISSPO) which has separate verticals within to address capacity needs of the FPCs. With over 40 professionals, CISSPO is engaged in FPCS in verticals ROC and governance; seed production value chain; organic cotton and pomegranate value chain; procurement and quality control; logistics and warehousing; credit linking; etc. in an integrated fashion. The Centre is financed from within ASA's grants.

From experience of various experts consulted, federations of FPCs at regional or state level have the potential to address capacity challenges. But the key to such federations at regional or state level is that they must commodity specific. This ensures greater cohesion within member producers and companies, better knowledge sharing, better price discovery, economies of scale throughout the value chain, etc. Some of the benefits of having commodity specific federations address concerns in other focus areas too. Please refer to section on Connections including production and marketing linkages, and also knowledge linkages.

Capital

Capital constraints have been the biggest bottleneck in an expected and take-off of the FPC concept. Since, it is aimed at small and medium landholder farmers, the initial paid up capital in almost all cases remains small. Plus, for FPCs engaged in commodities that have once a year cycle, absorbing even one season of losses becomes impossible as opposed to commodities such as milk, and vegetables, which have continuous production cycles. Low capacity of member producers to pool adequate funds not only limits the risk taking capacity of the FPC, but also the scale of operation due to low working capital, investments in capacity building and value addition. Most of the few examples of "good" FPCs that we come across had an advantage at the onset. For example, Sahyadri Farms started with around 10 farmers who contributed around 15 lakhs each to the company.

To address the capital constraints, especially at incubation or early stage, a provision for preference shareholding can be made for non-producers as well, may be NBFCs or agribusiness firms. These shares may entail no or limited voting rights."In case a Producer Company makes losses for two (or more) consecutive years, the preference shareholders shall have the right to move a resolution in the AGM/EGM of the company, seeking to elect other members in place of an existing member(s) of the Board of Directors and also another person in place of existing CEO. The voting on this resolution, however, would still be confined to the farmer members." (Mahajan 2014)

There have been a slew of steps taken by the government and governmental agencies to provide FPCs with access to capital. There is a credit guarantee scheme; funds from NABARD under producer organisations development, food processing categories, etc.; and equity grant fund of SFAC; and others. These funds have been described as inadequate by the experts; however, this is not the only challenge with it. The compliance levels and eligibility criteria to obtain these funds are unrealistically stringent for new FPCs. It has led to underutilisation of such funds. The credit guarantee scheme, too, has not succeeded in facilitating fund flow from commercial banks into the FPC system. Even as there have been MoUs and agreements, the challenge remains at the level of the decision makers, which is often a branch manager. In such a scenario, FPCs have been found availing loans from NBFCs at a higher rate of interest. This engagement with NBFCs dents into their margins, however, facilitates the business nonetheless.

As to facilitating cheaper credit from scheduled banks, the credit instruments needs orientation at the decision maker level. The current credit guarantee scheme may have to be notified by the RBI, as part of the priority sector lending. Also, unnecessary compliances for eligibility for credit need to be removed. According to Mr Emmanuel Murray, Senior Advisor at Caspian Investment, the current market size for debt to FPOs is estimated at around 600 Cr. The same report highlights that demand being met is around half of it around 300 Cr and rest is an opportunity that new NBFCs are attempting to fill. Large number of NBFCs entering the credit market in FPO space is a good signal to scheduled banks pointing to the promise of FPCs. The scheduled banks can target FPCs at emerging/ growing stage or matured ones looking to expand operations across the value chain.

A novel model which has emerged to address the most crucial need of capital is a Special Purpose Vehicle (SPV) model. This model recognises the limitations of FPCs operation and forms partnerships to perform an SPV a mutually beneficial manner. It essentially takes the functions of value addition and accessing capital to stakeholders and partners with specialisation to that end, by forming a different institution, usually a private limited company, with FPCs as shareholders along with corporate partners and/or NGOs.

Yuva Mitra, an NGO in Nashik area of Maharashtra, has promoted FPCs, which are also supported by NABARD. They have setup an SPV called Kisan Mitra Agro Services Pvt. Ltd., which is a joint venture of eight FPCs, Yuva Mitra, and Aditya Birla group as the corporate partner. Aditya Birla group is a majority shareholder in the SPV. This new institution takes care of infrastructure creation, capacity building, quality assurance and human resources. It has established three cluster level procurement and value addition centres. These centres are populated with capable human resources form local area doing grading, packaging, and supply to retail stores (which the SPV has entered into agreement with). At present the turnover of this SPV has touched 10 Cr. Since these FPCs are in rain fed area, it is difficult for them to access debt market. To address this challenge, Yuva Mitra has promoted another company in partnership with corporates.

Conclusion

FPCs offer a viable platform to create a space for small and marginal landholding farmers to retain the value of their produce, dignity of their labour, and avoid becoming a victim of captive or hierarchical value chains in face of the capacity and capital of large corporates. It has been more than a decade and there are unaddressed issues that require action from concerned stakeholders. A significant number of FPCs seem to have provided benefit to their member producers in real terms by facilitating better than market prices for commodities, inputs at reduced costs, and reducing transaction costs, etc. However, this is not enough given the greater challenge in food systems that is not favourable to the vast majority of small and marginal landholding farmers.Hence, there is a need for fine-tuning of the idea to make FPCs able to do what they are designed to do.

To that end, an FPC may not be considered successful unless it has end-to-end control over value chain of at least one food product, either directly or through some other mechanism. Today, there are very few which can be assessed as successful with this benchmark. To create a conducive milieu for majority of FPCs to attain the same benchmark, serious efforts to ease capacity, capital and other constraints of an FPC are required from policymakers. It may be best to use a multi-pronged approach, using suggestions described in this report,to design new generation of solutions required to make FPCs work.

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