



Contract Farming-Prospects and Challenges in India

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ABSTARCT

India is a country where agriculture is an age old practice and back bone of the country. Nearly agriculture contributes 17-18 percent to the country's GDP. In India most of the farmer's are small and marginal farmer's and get lots of troubles at the time of capital requirement. Contract farming has been existing in India since many years. It is the agreement between the farmer's and the company for the production of quality agriculture produces. It also helps the farmer's in increasing their income levels, produce high quality products, gain high price than normal price. Increase in agriculture standards also indirectly helpful for the country's GDP. Contract farming is being done in agriculture sector and its allied sectors like dairy, aquaculture etc. Thus contract farming is the viable option for the development of agriculture in India and raises the standards of farmer's also. Different models and problems of the contract farming from both sides that is farmer as well as company will be discussed in this paper.

Keywords:- Contract farming, Pre-Arrangements, Objectives, Models, Advantages and Problems.

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INTRODUCTION

Agriculture has been backbone of Indian Economy. Due to globalization and liberalization cropping patterns are changing and agriculture is now seen with a commercial outlook. Export oriented products and processed food items occupy vital position in market. In India most farmers fall under small and marginal categories, and are having poor resources [1].

Backward and forward linkages include provision of information on what to grow, rural credit, farming inputs, agricultural extension advice. Contract farming is attaining an important place in Indian agriculture sector in this scenario. Contract farming can be understood as a firm lending "inputs" — such as seed, fertilizer, credit or extension — to a farmer in exchange for exclusive purchasing rights over the specified crop. It is a form of vertical integration within agricultural commodity chains so that the firm has greater control over the production process and final product [2].

Contract farming facilitates farmers in getting inputs and technical advice on time and firms involved in contracts earn profit from agricultural production either by lifting the production and supplying to agro processing companies or by exporting the product after processing by its own. In first case firms act as a facilitator alone but in later they enjoy the export profits. Contract farming is generally defined as a farming under an agreement between farmers and a sponsor (processing and/or marketing firm) for the production and supply of agricultural products under forward agreements, frequently at predetermined prices [3].

WHAT IS CONTRACT FARMING?

- "Agricultural production carried out according to an agreement between a buyer and farmers, which establishes conditions for the production and marketing of farm products."

Pre - Arrangements in Contract Farming:

- **Quantity:** - Quantity availability means how much quantity buys.
- **Quality:** - Quality assurance means quality of goods like size, colure, shape, test, etc.
- **Time:** - Time consideration means decide time period of complete goods.

- **Price:** - Price profitability means what was the price of the goods and price decide on the basis of present market price of the goods.

Evolution of Contract Farming

- **Farming :-**In earlier days every family does farming for their livelihood, produces produce for their family consumption only.
- **Bartering :-**Later Bartering system was introduced in which exchange of produce with other produce occurs.
- **Money :-**As the time proceeds buying of produce with money had came in to existence.
- **Contract :-**To produce large and good quality agri produce contract farming had been started.

Objectives of Contract Farming

- To achieve consistent quality:- as per requirement they produce the agro raw produce (size, shape, colour, etc.)
- To achieve regular supply:- requirement of raw material at a time complete goods.
- To improve quality of produce:- sponsor provide the input (seed, fertilizer, capital), and also provide the knowledge about the market.
- Price Stability:- at a time of contract price decide so after harvesting no change in price because both the party sign in legal document.

NEED OF CONTRACT FARMING IN INDIA[3-5]

To overcome the following problems of farmers:

- Traditional technology and management practices
- Inadequate infrastructure and market information
- lack of post-harvest management expertise
- Inadequate capital to grow a quality crop
- Unfavorable conditions for procurement
- To reduce the load on the central & state level procurement system.
- To increase private sector investment in agriculture.
- To bring market focus in terms of crop selection by Indian farmers.
- To generate income at the individual farmer level.
- To promote processing & value addition.
- To generate gainful employment in rural communities, particularly for landless agricultural labor.
- To generate complete yearly employment, reducing seasonal employment.
- To reduce migration from rural to urban areas.

Who can be as a Partner in CF with Farmer?

- In contract farming farmer join with many body. Farmer partner with companies, government bodies, individual entrepreneur, unequal parties (wholesaler, retailer, trader, etc.) or NGO/facilitator (in kheda sadguru foundation).

Managing The Contract Farming

- **Identifying suitable production areas:-**The areas suitable for the produce we want to do contract should be identified.
- **Selecting farmers:-**The satellite farmers in that area are to be selected so that technology can be adopted by them soonly.
- **Forming working groups:-**By forming working groups the knowledge can be shared between the farmers and the inputs can be distributed easily.
- **Providing material inputs:-**Inputs are to be provided to farmers in time either directly or through working groups.
- **Providing logistical support:-**The transport facilities should be provided by company itself for input distribution and transport of harvested produce.
- **Purchasing the product:-**Finally have to purchase the produce.

Table no:-1 Contract farming area in different states

States/UTs	Total Cropped Area (2003-04) (In ' 000 Hectare)	Area under Contract Farming (2007) (In Hectare)	Area under Contract Farming (As on April, 2010) (In Percentage)*
Andhra Pradesh	12366	-	66** (of total horticultural area)
Assam	3962	160	-
Bihar	7882	20	-
Chhattisgarh	5707	-	-
Goa	169	1924	-
Gujarat	11311	2000	-
Haryana	6388	1416	0.24 (of total area under Barley)
Mizoram	98	2447	-
Orissa	8637	5900	28.30*** (of total area under Cotton)
Punjab	7931	121457	1.05
Tamil Nadu	5316	236610	Negligible (Oil Palm only)
West Bengal	9707	-	Negligible
India	190641	425834	-

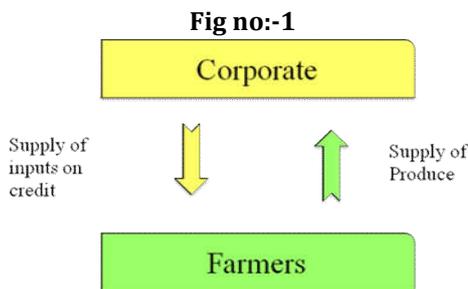
Note: *: As reported by different states,** : Under horticulture crops,***: Area under cotton.

Source:<http://www.indiaagristat.com/table/agriculture/2/agriculturalarealanduse>

The above table gives the information about the area of contract farming in the different states and total area in India i.e Highest area is in Tamilnadu region in the year 2007 and total area of India is 425834 hec.

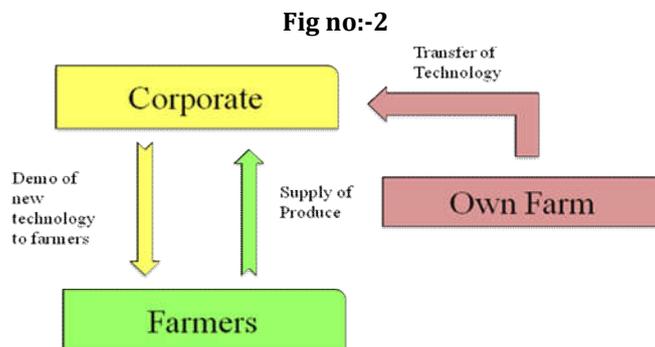
MODELS OF CONTRACT FARMING

Centralized Model



This is a vertically coordinated model where the sponsor purchases the crop from farmers and processes or packages and markets the product. Except in a limited number of cases, farmer quotas are normally distributed at the beginning of each growing season and quality is tightly controlled. A sponsor may purchase from tens of thousands of small-scale farmers within a single project. The centralized scheme is generally associated with tobacco, cotton, sugar cane and bananas and with tree crops such as coffee, tea, cocoa and rubber, but can also be used for poultry, pork and dairy production. Where fresh vegetables and fruits are grown under contract, the term "processing" may include grading, sorting and packaging as well as the provision of cool storage facilities.

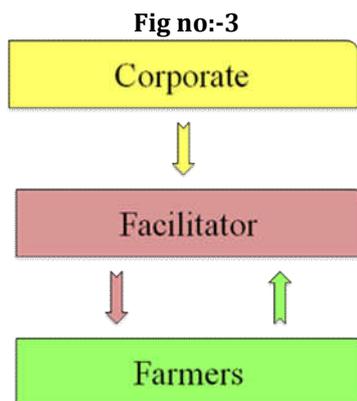
Nucleus Estate Model



Nucleus estates are a variation of the centralized model. In this case the sponsor of the project also owns and manages an estate plantation, which is usually close to the processing plant. The estate is often fairly

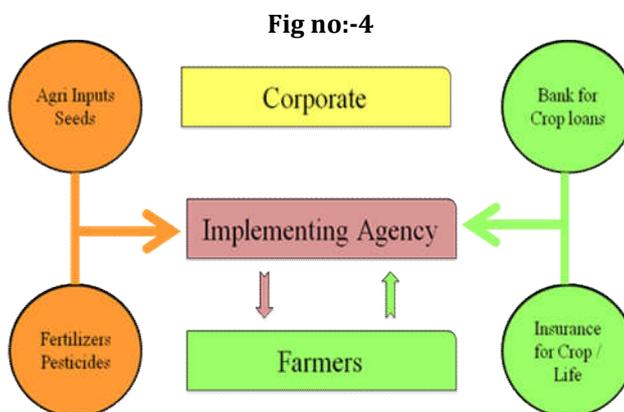
large in order to provide some guarantee of throughput for the plant, but on occasion it can be relatively small, primarily serving as a trial and demonstration farm. The British-based Commonwealth Development Corporation (CDC) was a pioneer of the nucleus estate model although it no longer develops such estates. A common approach is for the sponsors to commence with a pilot estate then, after a trial period, introduce to farmers (sometimes called "satellite" growers) the technology and management techniques of the particular crop. Nucleus estates have often been used in connection with resettlement or transmigration schemes, such as in Indonesia and Papua New Guinea, for oil palm and other crops. While mainly used for tree crops, there are examples of the nucleus estate concept with other products. Indonesia, for example, has seen the operation of dairy nucleus estates, with the central estate being primarily used for the rearing of "parent stock".

Multipartite Model



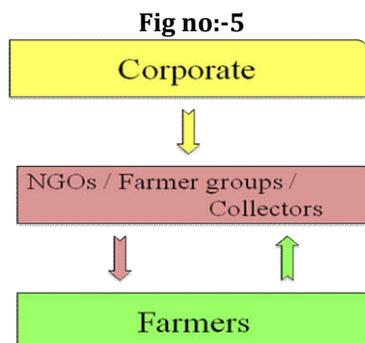
The multipartite model usually involves statutory bodies and private companies jointly participating with farmers. Multipartite contract farming may have separate organizations responsible for credit provision, production, and management, processing and marketing. In Mexico, Kenya, and West Africa, among other countries, governments have actively invested in contract farming through joint ventures with the private sector. Multipartite structures are common in China where government departments as well as township committees and, at times, foreign companies have jointly entered into contracts with village committees and, since the early 1980s, individual farmers.

Informal Model



This model applies to individual entrepreneurs or small companies who normally make simple, informal production contracts with farmers on a seasonal basis, particularly for crops such as fresh vegetables, watermelons and tropical fruits. Crops usually require only a minimal amount of processing. Material inputs are often restricted to the provision of seeds and basic fertilizers, with technical advice limited to grading and quality control matters. A common example of the informal model is where the sponsor, after purchasing the crop, simply grades and packages it for resale to the retail trade. Supermarkets frequently purchase fresh produce through individual developers and, in some cases, directly from farmers. Financial investment by such developers is usually minimal. This is the most transient and speculative of all contract farming models, with a risk of default by both the promoter and the farmer. Nevertheless, in many developing countries such developers are long established and in numerous cases they have proved an alternative to the corporate or state agency approach.

Intermediary Model

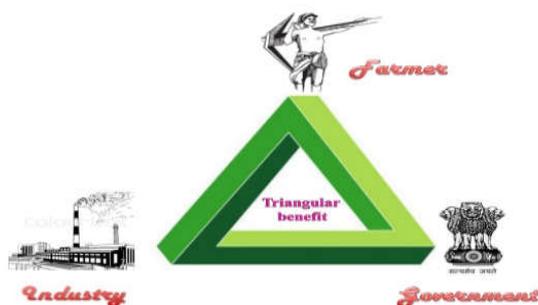


Throughout Southeast Asia the formal subcontracting of crops to intermediaries is a common practice. In Thailand, for example, large food processing companies and fresh vegetable entrepreneurs purchase crops from individual "collectors" or from farmer committees, who have their own informal arrangements with farmers. In Indonesia, this practice is widespread and is termed *plasma*. The use of intermediaries must always be approached with caution because of the danger of sponsors losing control over production and over prices paid to farmers by middlemen. In addition, the technical policies and management inputs of the sponsors can become diluted and production data distorted.

Source:- Khandare V. B. & Kole N. V. [7], Contract Farming In India, ABD Publishers, Rajasthan (India).

Contract Farming – Triangular Benefit

Fig no:-6



We all are know through the contract farming win-win situation for the farmer, industry and government like in India farmer facing some problem like lack of capital, lack of resources (new technology, fertilizer, seed, etc.) and the measure problem is farmer are not connected with the market so they have not knowledge about the market so they not produce as per market demand and they get lower price of produce.

Through the contract farming also benefit for the Industry like at a time of requirement of raw material easily get, risk sharing with the farmer, price benefit like raw material price increase so effect of the cost of production increase and measure benefit is quality of the goods as per requirement.

Also benefit for government like employments generate so reduces government burden, foreign currency, etc.

ADVANTAGES AND DISADVANTAGES OF CONTRACT FARMING [6-16]

Advantages for Farmers

Following are the advantages for the farmers

➤ Provision of inputs and production services

For ensuring a proper crop husbandry practices in order to achieve projected yields in required qualities many contractual arrangements involve considerable production support in addition to the supply of basic inputs such as seed and fertilizer. Sponsors may also provide land preparation, field cultivation and harvesting as well as free training and extension.

➤ Access to credit

With the collapse or restructuring of many agricultural development banks, the majority of small holder producers experience difficulties in obtaining credit for production inputs. Contract farming usually allows farmers access to some form of credit to finance production inputs. Arrangements can also be made with commercial banks or government agencies through crop liens that are guaranteed by the sponsor, i.e. where the contract serves as collateral.

➤ **Introduction of appropriate technology**

New production techniques are often necessary to increase productivity as well as to ensure that the commodity meets market demands. However, small scale farmers are frequently reluctant to adopt new technologies because of the possible risks and costs involved. Private agribusiness will usually offer technology more diligently than government agricultural extension services because it has a direct economic interest in improving farmers' production.

➤ **Skill transfer**

The skills the farmer learns through contract farming may include record keeping, the efficient use of farm resources, improved methods of applying chemicals and fertilizers, knowledge of the importance of quality and the characteristics and demands of export markets. Farmers can gain experience in carrying out field activities following a strict timetable imposed by the extension service. In addition, spill over effects from contract farming activities could lead to investment in market infrastructure and human capital, thus improving the productivity of other farm activities.

➤ **Guaranteed and fixed pricing structures**

The returns farmers receive for their crops on the open market depend on the prevailing market prices as well as on their ability to negotiate with buyers. This can create considerable uncertainty which, to a certain extent, contract farming can overcome. Frequently, sponsors indicate in advance the price(s) to be paid and these are specified in the agreement. Thus Contract Farming ensures guaranteed and fixed pricing structures.

➤ **Access to reliable markets**

Farmers will not cultivate unless they know they can sell their crop, and traders or processors will not invest in ventures unless they are assured that the required commodities can be consistently produced. Contract farming offers a potential solution to this situation by providing market guarantees to the farmers and assuring supply to the purchasers. Even where there are existing outlets for the same crops, contract farming can offer significant advantages to farmers. They do not have to search for and negotiate with local and international buyers, and project sponsors usually organize transport for their crops, normally from the farm gate.

ADVANTAGES FOR SPONSORS

Following are the advantages for the sponsors

➤ **Political acceptability**

Contract farming, particularly when the farmer is not a tenant of the sponsor, is less likely to be subject to political criticism. It can be more politically expedient for a sponsor to involve smallholder farmers in production rather than to operate plantations. In recent years, many African governments have promoted contract farming as an alternative to private, corporate and state owned plantations.

➤ **Overcoming land constraints**

The majority of the world's plantations were established in the colonial era when land was relatively abundant and the colonial powers had little conscience about either simply annexing it or paying landowners least compensation. However, in present days most large tracts of suitable land are either traditionally owned, costly to purchase or unavailable for commercial development. Contract farming, therefore, offers access to crop production farm land that would not otherwise be available to a company, with the additional advantage that it does not have to purchase it.

➤ **Production reliability and shared risk**

Working with contracted farmers facilitates sponsors to share the risk of production failure due to poor weather, disease, etc. The farmer takes the risk of loss of production while the company absorbs losses associated with reduced or nonexistent throughput for the processing facility. Where production problems are widespread and no fault of the farmers, sponsors will often defer repayment of production advances to the following season. Both estate and contract farming methods of obtaining raw materials are considerably more reliable than making purchases on the open market.

➤ **Quality consistency**

A steady markets for fresh and processed agricultural produce require reliable quality standards. Moreover, these markets are moving increasingly to a situation where the supplier must also conform to regulatory controls regarding production techniques, particularly the use of pesticides. Both estate and contracted crop production require close supervision to control and maintain product quality, especially when farmers are new with innovative harvesting and grading methods.

➤ **Promotion of farm inputs**

It is one of the important considerations as farmers do not get required farm inputs in time due to lack of proper distribution channel. So, in this regard promotion of farm input is the need of the hour.

Disadvantages faced by the farmers

Following are the disadvantages faced by the farmers

➤ **Possibility of greater risk**

Farmers who were entering into a new contract farming venture should be prepare themselves to assess the prospect of higher returns against the possibility of greater risk. Such risk is more expected when the agribusiness venture is introducing a new crop to the area. There may be production risks, particularly where prior field tests are inadequate, resulting in lower-than-expected yields for the farmers.

➤ **Outdated technology and crop incongruity**

The introduction of a new crop to be grown under conditions meticulously controlled by the sponsor can cause disruption to the existing farming system. Again, the introduction of sophisticated machines (e.g. for transplanting) may result in a loss of local employment and overcapitalization of the contracted farmer. Furthermore, in field activities such as transplanting and weed control, mechanical methods may produce less effective results than do traditional cultivation methods.

➤ **Manoeuvring in quotas and quality specifications**

Incompetent management can lead towards production exceeding original targets. For example, failures of field staff to determine fields following transplanting can result in gross over planting. Sponsors may also have unrealistic expectations of the market for their product or the market may crumple unexpectedly owing to transport problems, civil unrest, change in government policy or the arrival of competitors. In some situations management may be tempted to manipulate quality standards in order to reduce purchases for honouring the contract. Such practices may cause sponsor-farmer confrontation, especially if farmers have no method to dispute grading irregularities.

➤ **Corruption**

Problems occurs when staff responsible for issuing contracts and buying crops taking undue advantages of their position. Such practices result in a collapse of trust and communication between the contracted parties and soon undermine any contract. In a large contract, the sponsors can themselves be dishonest or corrupt. Governments have sometimes fallen victim to dubious or “fly-by-night” companies who have seen the opportunity for a quick profit. Therefore, in every case farmers who make investments in production and primary processing facilities run the risk of losing everything.

DISADVANTAGES FACED BY THE SPONSORS [12-16]

Following are the disadvantages faced by the sponsors

➤ **Limitation on land availability**

Farmers should have a suitable cultivable land on which they are to cultivate contracted crops. But problems can arise when farmers have minimal or no security of tenure as there is a possibility of drainage in sponsor’s investment as a result of farmer - landlord disputes. Difficulties may also arise when sponsors lease land to farmers. Some contract farming ventures are dominated by customary land usage arrangements negotiated by landless farmers with traditional landowners. While such a situation allows the poorest cultivator to take part in contract farming ventures, discrete management measures need to be applied to ensure that landless farmers are not exploited by their landlords. Before signing a contract, the sponsor must ensure that access to land is secured, at least for the term of the agreement.

➤ **Social and Cultural constraints**

Promoting Contract Farming is a cultural, customary beliefs and religious issues. In communities where custom and tradition play an important role, difficulties may arise when innovative farming is introduced. Therefore, before introducing new cropping practices, sponsors must consider the social attitudes and the traditional farming procedures of the community and decide how a new crop can be introduced.

➤ **Farmers disgruntlement**

Sometimes, situations may crop up which may leads towards farmer discontent; e.g. biased buying, late payments, incompetent extension services, poor agronomic counsel, undependable transportation for crops, a mid-season change in pricing or management's impoliteness to farmers will all normally aggravate the relationship between sponsors and the farmers. If not readily addressed, such circumstances will cause antagonism towards the sponsors that may result in farmers withdrawing from projects.

➤ **Below quality agro-input**

Sometimes farmers are forced to use inputs supplied under contract for the purposes other than those they were intended for. They may choose to utilise the inputs on their other cash and subsistence crops or even to sell them. As a result contracted crop’s yields were reduced and the quality are affected. Improved monitoring by extension staff, farmer training and the issuing of realistic quantities of inputs can resolve the matter successfully. Majority of farmers conform to the agreement when they have information that the contract has the advantages of technical inputs, cash advances and a guaranteed

market. However, until a project is very poorly managed, input diversion is usually an infirmity rather a serious problem.

➤ **Sale of crops by the farmers beyond contractual agreement**

The sale of produce by farmers to a third party, outside the terms of a contract, can cause major problem to the sponsors. However, extra-contractual sales are always possible when there is an alternative market. The outside buyers offered cash to farmers as opposed to the prolonged and difficult collection of payments negotiated through the cooperative. Sometimes the Sponsors may encourage extra-contractual practices as there are several companies working with the same crop (e.g. cotton in some southern African countries) and they could collaborate by establishing a register of contracted farmers.

CHALLENGES OF CONTRACT FARMING IN INDIA

- ✓ **Highly restrictive and regulated agricultural marketing system:-**The marketing system present in India in markets is highly restrictive and regulated as only few can enter into the market for purchasing of produce from farmers as the government have to permit all with rules and regulations.
- ✓ **Price setting not transparent - both producers and consumers are often cheated:-** Price fixed only by mouth saying and at last the company may cheat farmer by purchasing at low prices as there is no bond between them, In same way if farmer gets higher price from other company then he will sell to other only by cheating the contracted company.
- ✓ **Monopoly of the State Governments to set up of markets:-**The APMCs by state governments are only markets where there should be the selling and purchasing of produce should be done.
- ✓ **Mandi revenues not deployed for infrastructure development:-**The revenues got my Mandi doesn't utilize for the development of infrastructure in it, so it become a challenge for the farmer to store the produce in Mandi.
- ✓ **Lack of proper retail supply chain:-**As there is monopoly of the markets, there is no proper retail chain which is a big challenge for farmers to sell their produce at good price.

SUGGESTIONS FOR IMPROVEMENT ON PERFORMANCE OF CF IN INDIA

- ✓ Emphasis should be on infrastructure development.
- ✓ For the better understanding of terms and condition of contract farming the agreement should be in regional language.
- ✓ The data should be maintained at state level, country level to made available for effective policy making.
- ✓ Success in developing contracting models or other forms of farm-firm linkages such as clusters that are effective for small holders will be a key to small holder participation .
- ✓ The contract farming in India in nascent stage so steps should be taken to boost growth of contract farming in India.
- ✓ Government need to ensure that contract farming is generally commodity specific tends to promote monoculture thus land use planning is necessary.
- ✓ Government should give some incentives to contract farming firms.

CONCLUSION

Contract farming modernizes farmers by providing new technology, credit, inputs and technical advice besides linking them to the international market. It is not a easy to solve all related problems of agricultural production and marketing systems. But contract farming could be evaluated as a way of providing earlier access to credit, input, information, technology and product markets for the small scale farming structure. But there are some problems in contract farming. For successful implementation of contract farming, having co-ordination and collaboration, consciousness and acting in an organized manner are advisable for both sides. On the Other hand, Government attributes and incentives are also important aspects.

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