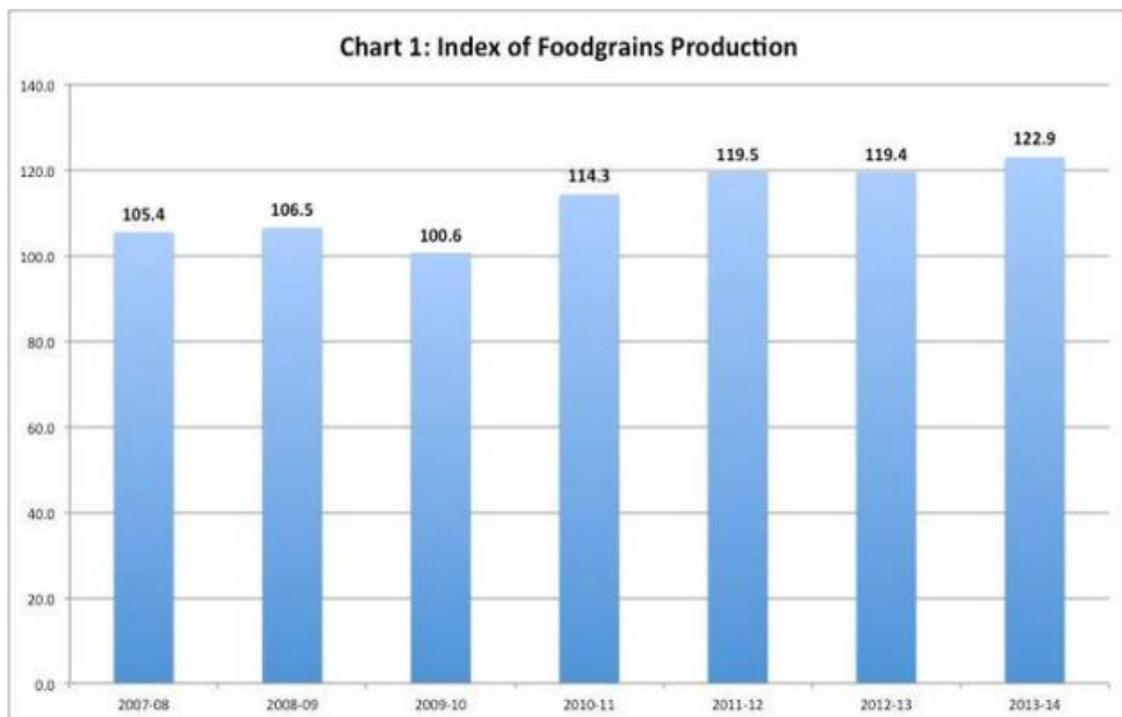


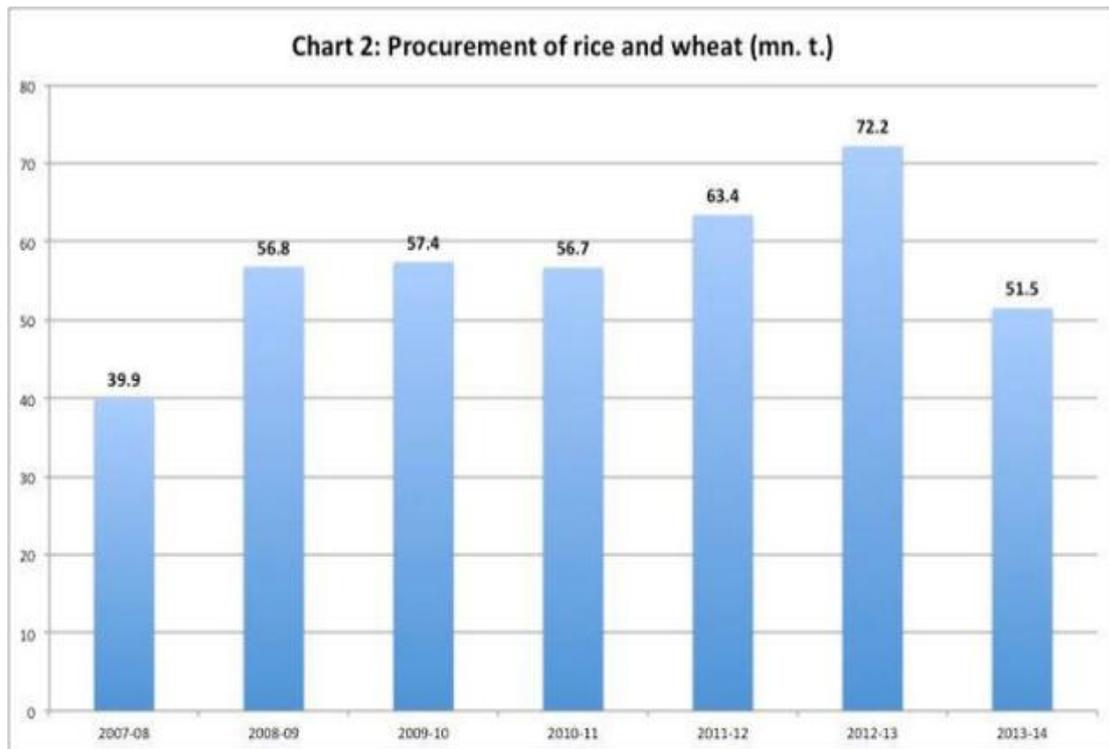
The Last Straw

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As election season nears its end and a new government is set to take office, the spectre of [El Niño](#) haunts India. With unusually high surface temperatures being observed and predicted off the Pacific Coast of South America, meteorologists are now expecting with a higher degree of confidence an El Niño event that, because of changed climate and rainfall patterns, would bring droughts or floods to various regions of the world. In India, the effect, if felt, implies lower than normal rainfall. Already, in its first official forecast, the India Meteorological Department (IMD) has [predicted a below normal southwest monsoon](#) this year. Predictions can go wrong, but the question remains: if after a period of consecutive normal or better-than-average monsoons, parts of India experience a drought and other parts floods, what would be the consequences?



Since wayward rainfall patterns would affect agriculture first, it is to the consequences of a shortfall in agricultural production, especially food production, that we should turn. On the surface India seems well positioned to deal with a shock of this kind. Over the last four years, the munificence or benevolence of the rain gods have ensured that India's agriculture has performed well. If we take food grains production for example (Chart 1), the official index shows that after having stagnated for three years starting 2007-08, production rose sharply in 2010-11 and 2011-12, stayed at that high level in 2012-13 and rose even further in 2013-14. As per the second advance estimates released by the Ministry of Agriculture in mid-February, production of food grains during 2013-14 is estimated at 263.20 million tonnes compared to 257.13 million tonnes in 2012-13.



One result of the production spike was that between 2010-11 and 2012-13 procurement of rice and wheat rose from 56.7 million tonnes to 72.2 million tonnes (Chart 2). As a result, as compared with the official buffer stock requirement of 14.2 million tonnes of rice and 7 million tonnes of wheat on April 1 of any year, the actual stocks rose from 26.7 and 16.1 million tonnes respectively in 2010, to 35.5 and 24.2 million tonnes in 2013. This trend, induced by the good or reasonable harvests, should have strengthened the government's ability to deal with a monsoon shock.

However, something seems to have occurred over the last financial year. Firstly, though the government had estimated that food grains production had scaled a new peak, procurement in marketing year 2013-14 (till 17 April 2014) was only 51.5 million tonnes as compared with 72.2 million tonnes in the previous year.

As a result, as on April 1, 2014, stocks with the government of rice and wheat were only 30.6 and 17.8 million tonnes respectively, pointing to a combined fall of 11.3 million tonnes or about 19 per cent relative to April 1, 2013. One reason for this could have been the unwillingness of a government exercising fiscal restraint to continue to hold the large stocks it had accumulated and its decision to make the necessary adjustment by resorting to a substantially reduced procurement despite the high level of output.

The other could be that the government's production estimate for 2013-14 is exaggerated. That is what Vishwanath Kulkarni and Harish Damodaran (Business Line April 25, 2014) suggest, based on the much [lower market arrivals of paddy](#) (till April 24) in 2013-14 (52.7 million tonnes) as compared with 2012-13 (49.9 million tonnes). Whatever be the reason, as the nation prepares for a possible fall in agricultural production due to the El Niño effect, the stocks the government has at hand to deal with the potential shock is significantly lower than a year earlier.

This suggests that there are two obvious consequences that a shock of this kind would have on the Indian economy. The first is that India's flagging economic growth will take a further hit. This will happen directly, because reasonably good agricultural growth contributed to the realisation of the 2003-08 boom in GDP growth and also helped buffer the recession that had set in over the last two to three years. It will further have adverse indirect effects, because a reasonably healthy agriculture is also a way of sustaining demand for and growth in nonagricultural production.

The second is that food price inflation is bound to accelerate not just because of the changed supply-demand balance in the aftermath of any agricultural shock, but also because of the speculative demand and price increase that this would give rise to. A disturbing feature of the Indian economy in recent years has been a high level of food price inflation despite reasonable good production. This was obviously due to cost-push factors that necessitated suitable upward adjustment of procurement prices and a rise in the cost-plus floor they set to open market prices. Now, cost-push inflation in food prices would be aggravated by the demand side pull triggered by the supply-demand imbalance.

This possibility of worsening stagflation will thus be an immediate challenge for the new government.

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