Quickonomics

June 4, 2020

The one bright spot in the economy

Agriculture and allied activities could be the Indian economy's only bright spot in a year when the Covid-19 pandemic has slammed the brakes on industry and services.

Overall, CRISIL expects a real agricultural growth of 2.5% in fiscal 2021, with risks tilted to the downside due to a hit to horticulture and any likely impact of locust attacks.

The effects of the pandemic on the sector thus far have, however, been varied. That's because agriculture and allied activities is not a homogeneous group, but an umbrella of activities, each having its own set of dynamics.

For instance, while the share of crops in the agriculture sector's gross value added (GVA) is the largest, it is also the most volatile in terms of performance. It is the only sector that showed negative performance during some years in the past decade.

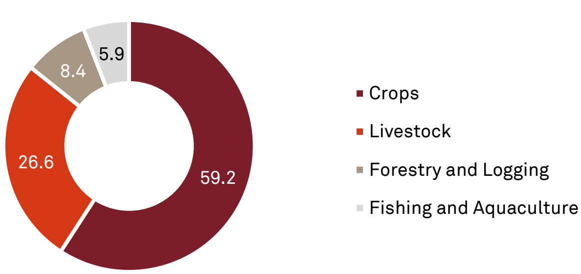
Livestock, though only half the size of crops, plays a crucial role in driving the agricultural GVA growth. Its role attains prominence particularly in years when crops takes a hit.

Further, crops can be classified into food grains and horticulture.

Horticulture production has exceeded that of food grains since crop year 2012-13. In crop year 2019-20, horticulture production is estimated at 313.35 metric tonne (MT), compared with 291.95 MT for food grains. According to estimates of the agriculture ministry, horticulture's share in the GVA of agriculture and allied activities is ~30%, similar to that of food grains.

Crops are the mainstay* of the farm economy

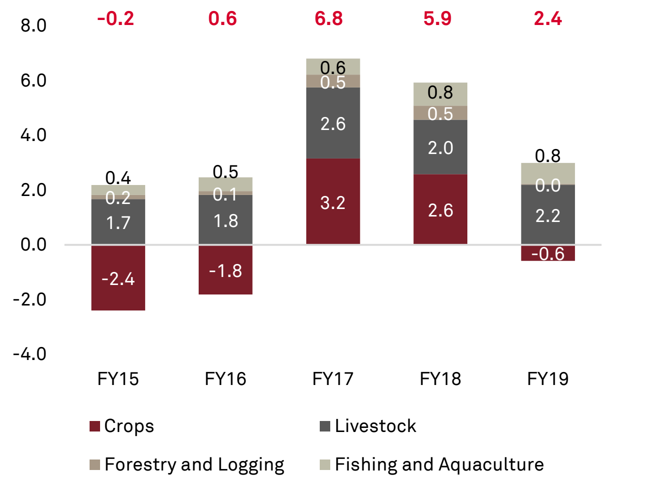
Share in agri and allied activities GVA (%)



**FY15-FY19 average share in agriculture and allied GVA*
Source: National Statistical Office (NSO)

Livestock plays an important role, especially in years when crops suffer

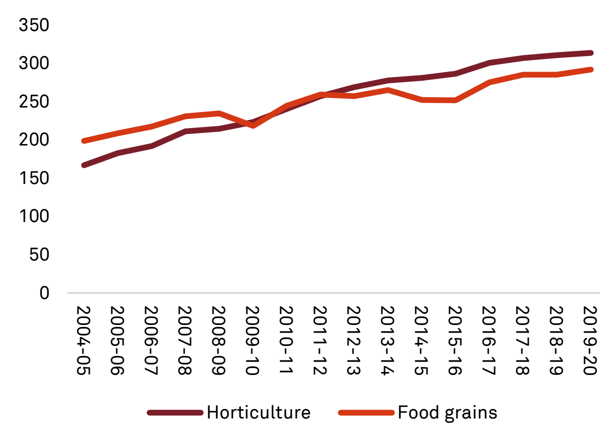
Weighted average growth rate (%)



Note: Figures in red at the top are overall agriculture and allied sector growth
Source: NSO

Foodgrain is just one part of crops, the other equally important part is horticulture

Production (MT)



Source: Ministry of Agriculture and Farmers' Welfare

However, in terms of value of output, the share of horticulture is much lower. For instance, in 2016-17[1], the value of horticulture output was Rs 4.52 lakh crore, whereas the value of all agricultural crops stood at

[1] *Latest year for which disaggregated price information is available*

Rs 16.37 lakh crore, implying that horticulture's share was roughly 28%. This suggests that while horticulture production exceeds that of food grains, price realisation in the case of former is much lower – largely attributed to perishability.

With the pandemic and the ensuing lockdown, demand for horticultural produce is likely to be impacted much more than that of food grains.

Food grains are non-perishable and can be stored. Plus, they have the government's minimum support price (MSP) and procurement support. As things stand, Rabi procurement has proceeded quite well and the government has announced MSP hike for 14 kharif crops, assuring farmers 50-83% returns on their cost of production.

This, however, is not the case for horticulture produce, which is perishable in nature. This was evident in the collapse of wholesale prices of vegetables and fruits in April despite a sharp reduction in their mandi arrivals.

Likewise, demand for flowers has collapsed as religious places are shut down and marriage ceremonies are kept in abeyance or muted.

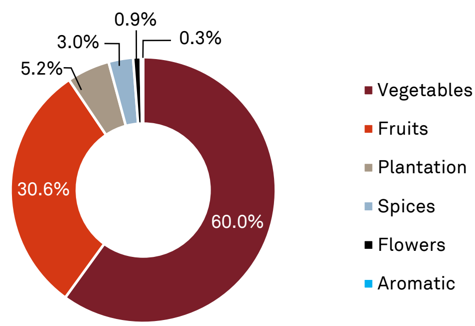
Early indications suggest horticulture exports, too, could take a hit, as fruits such as grapes and mangoes are not being exported amid restrictions in many countries.

The recent locust attack remains a key monitorable. Its impact on agriculture output is not a worry for now, as rabi crops have been harvested and a full-fledged kharif sowing is yet to begin[2]. That said, a number of standing crops – largely horticulture produce, which was not harvested because of problems in selling – have reportedly been attacked. Measures to control the locust attack are needed on a war footing, as the kharif sowing season is approaching fast.

Moving to livestock, milk is the largest contributor to this sector with a two-thirds share, followed by meat and a very small share of eggs. Fortunately, milk consumption from the household segment has remained largely stable despite the lockdown. Demand from the hotels/restaurants/catering segment (which contributes 15-20% to total milk consumption) has certainly collapsed, but is expected to pick up gradually once the lockdown is lifted. Moreover, the current slowdown in consumption demand is being dealt with by converting liquid milk into skimmed milk powder (SMP), which can be stored in the inventory.

Vegetables, followed by fruits, constitute the major chunk of horticulture

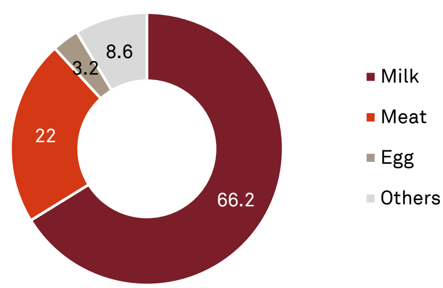
Share in horticulture production (%) - 2019-20



Source: Ministry of Agriculture and Farmers' Welfare

Milk largely holds the key for the livestock sector

Share in livestock output (%)



Source: NSO, CRISIL Research

How is the pandemic likely to affect various agriculture and allied sub-sectors?

Sub-sector	Risk to output/ growth
Crops - food grains (30%)	Low
Crops - horticulture (29.2%)	Medium
Livestock (26.6%)	Low
Forestry & logging (8.4%)	NA
Fishing and aquaculture (5.9%)	High

Note: Figures in parentheses are shares in agri GVA
NA = Not assessed

[2]*Cotton planting seems to have begun in some parts of central and southern India*

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The bottom line

Growth in agriculture and allied activities this fiscal hinges on a bumper food grains production. A normal monsoon will be critical, too. Horticulture might have to bear some burnt because of perishability. Livestock is an important fall-back in times crop output volatility. Milk, which comprises the biggest chunk of livestock, is expected to do well.

On the other hand, categories such as meat, eggs, fishing and aquaculture are likely to face a prolonged impact, as there is a tendency to reduce consumption of non-vegetarian food during the pandemic. A fall in exports in these commodities too is expected to hem in demand. But with the contribution of these items in the agriculture and allied activities sector being relatively lower, the overall agricultural growth may stay resilient.

What does this mean for food inflation

Food inflation was a key concern last fiscal for the Reserve Bank of India's (RBI) inflation-targeting policy. After almost six years, food inflation again entered into double digits in November 2019, pushing the headline CPI inflation outside the RBI's target band of 2-6%. Similar concerns have cropped up again, at least for the time being. After softening a little bit in March 2020, retail food inflation again flared up in April – the first full month of the nationwide lockdown. From 8.8% in March, food inflation rose to 10.5% in April. While the rise was broad-based, vegetables and pulses saw particularly high inflation at 23.6% and 22.8%, respectively.

Another divergent aspect of food inflation is the rise is retail food inflation, even as it softens at the wholesale level. From 5.5% in March, wholesale food inflation was down at 3.6% in April. This suggests that the firming-up of retail food inflation can largely be attributed to supply-related disruptions because of the lockdown. Once the situation normalises, retail food inflation can be expected to soften. A bumper rabi harvest and higher kharif target – because of a forecast for a normal monsoon – are likely to keep a tab on food inflation.

Reforms bode well for the medium term

Reform measures related to agriculture stand out in the Atma Nirbhar Bharat Abhiyan package. The proposed new law, which provides the farmer a choice in selling the produce rather than being captive to the Agriculture Produce and Marketing Commission (APMC) Act, was long overdue.

Over years, instead of supporting farmers to sell their produce in the market, the APMC had left them vulnerable to price manipulation by traders and commission agents. The amendment of the Essential Commodities Act to deregulate food items (food grains, oilseeds, onion and potato), too, is aimed at improving price realisation for farmers and in curtailing the ambiguity.

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