DEBATE

Will the drought hit rural demand?

The rural economy no longer subsists on agriculture, but the umbilical chord that ties Bharat to agriculture remains intact since 46 per cent of rural income is still drawn from the farm sector

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Over the past four to six weeks, newspapers and television channels have been flooded with news about a deficient monsoon and the impact it would have on the economy. I, too, have not been spared, with many people asking me what impact a deficit monsoon would have on the fast moving consumer goods, or FMCG, business.

If you go back in time to 2009, which was a drought year, there was an impact — on the economy, farming community, and, yes, FMCG. So predicting the worst is not a difficult task.

But I beg to differ here. This time, the deficiency in rainfall may not impact FMCG companies as it did in the past. Here's why:

First, although the rural economy is dependent on agriculture, things have changed in the last decade. Reports today suggest that 55 to 60 per cent of rural India depends on agriculture and agriculture-based income. This is lower than what it was earlier.

Second, the produce of those dependent on the rains may be impacted in terms of output levels, but that does not mean their incomes would be affected too. Why? A shortage in the marketplace could actually push up crop prices. So incomes don't get impacted as a consequence.

Another important point is this: the government (both central and state) understand the importance of deficit monsoons in a year they describe as "critical". Whatever the situation earlier, I think the government will not stop from acting this time around. My hypothesis is based on the fact that we are closer to 2014 – the year the general elections are due to be held – now than we were in 2009. I don't think it is lost on the government that its actions now could impact its vote base and voter turnout later. I anticipate higher spending on rural schemes, a greater thrust on financial inclusion and so on. This is likely to leave some money in the hands of rural consumers. So rural demand will not contract to the extent that many think it will.

Given that there would be questions raised about the government's ability to fund these schemes, measures such as divestment could be triggered to raise money for such initiatives. As I write this piece, I am privy to developments in this regard. The new finance minister has already indicated that steps would be taken to revive the economy and mitigate impact of both inflation as well as the drought. All of this gives me hope that there will be some action at the ground level. I think the government can no longer ignore it.

Last but not least, FMCG companies have been saddled with the longest and possibly highest rate of inflation, which has crippled the Indian middle class as well as the bottom-of-the-pyramid consumer. We have had years of government inaction in terms of policy formulations. We also had a spell of tormenting input costs and are in the middle of a global slowdown. Despite this, most Indian companies in the FMCG space have actually come out with their strongest possible results over the last six to eight quarters. That's because companies have been able to innovate, adapt and, most importantly, execute plans in the most trying of times so as to add value to their brands as well as provide value to consumers.

This innovation cuts across both rural and urban consumers. I am sure companies today are better prepared to face situations such as a drought as never before. My only concern remains this: that companies do not shrink brand investments in the face of adversity. In my view, companies that are conservative are at the greatest risk of losing more than what they normally would have. The innovators survive.

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In a world of highly mechanised commercial farming where agricultural labour force is small, it seems feasible that drought may have only a minor impact on economic conditions of households. But this seems like a distant dream for India at the moment. The share of agriculture in GDP has been steadily declining and non-farm employment in rural areas has been growing, but the umbilical chord that ties rural India to agriculture remains intact. As long as this is the case, what affects agriculture will continue to affect the rest of the nation.

Data from the India Human Development Survey (IHDS) conducted in 2004-5 by the National Council of Applied Economic Research and University of Maryland – the only survey in recent years to provide information on income and expenditure – provides some startling figures. It documents that 51 per cent of rural male workers and 84 per cent of rural female workers are employed solely in agriculture or animal husbandry. A further 21 per cent males and seven per cent females undertook multiple activities including both agricultural work and non-agricultural work such as construction labour; while only 28 per cent males and nine per cent female workers focused solely on non-farm work.

This suggests that more than three-fourths of the rural workforce is still involved in agriculture. Since 2004-05, growth of Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS) has increased employment in non-agricultural casual labour but National Sample Survey data documents only about a four-percentage point decline in agricultural workforce between 2004-05 and 2009-10.

The IHDS also documents that almost 83 per cent of rural households draw some income from cultivation, agricultural labour or animal husbandry. Non-agricultural incomes are higher so even though only a small proportion of households may have non-agricultural incomes, these are often high-income households such as those belonging to local doctors or teachers. Nonetheless, 46 per cent of *total* rural income is drawn from agriculture.

Anything that affects 46 per cent of total rural income and 83 per cent of rural households is not minor. But its ripple effects are even larger. When farm incomes suffer, it reduces expenditure of agricultural households on non-essential items. These non-essential items may include purchase of new clothing, affecting local tailor's income or reduction in private tutoring for children, reducing the income of the local school teacher.

A number of forces may moderate the impact of drought on agricultural households. When supply drops, prices should rise benefitting the producers and harming consumers. However, given the structure of our agricultural markets and procurement policies, producers tend to benefit less than the middlemen. So, while retail food prices rise, the price at which a farmer is able to sell his or her crops does not rise commensurately. Moreover, many Indian farmers are subsistence farmers, consuming their own crops. These households are sheltered to some extent from rising food costs but do not benefit from higher sale prices. Agricultural workers are the worst off. They don't benefit from higher harvest prices since their work comes before sale and drought may reduce work available to them.

A more promising avenue to income stability lies in increased employment in MGNREGS. However, less than 10 per cent of the households that obtained any work in the scheme completed the full 100 days of work.

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These views are personal