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Prices and Food Management

Drought in seventeen States this year after 14 years of normal or near normal rainfall (last drought was in 1987), raised apprehension of high inflation in 2002-03. The economy, however, displayed its resilience and intrinsic strength. Despite a likely shortfall in kharif output from adverse weather conditions, and high international crude oil prices resulting from tension in the Gulf region, inflation remained contained to low levels during the year.

5.2 A sharp fall in crop production in the past generated serious inflationary expectations since primary articles have a weight of 22 percent in the Wholesale Price Index (WPI). This however did not happen in the current year despite the drought because of the

availability of an abundant surplus stock of foodgrains. Adequate release of surplus stocks of foodgrains helped in both keeping the inflation low and dampening the undercurrents of inflationary expectations. (see Box 5.1) Reduced purchasing power of the farming community as a consequence of the decline in kharif production also dampened the demand for manufactured products, thus reducing to some extent the inflationary expectations in the manufactured sector. International crude oil prices reigned high because of tension in the Gulf region, but this did not exert any undue pressure on inflation despite the dismantling of the Administered Price Mechanism (APM) in April 2002.

Box 5.1 : Drought and inflation

Poor Monsoon results in lower agri/foodgrains output, shortages of primary products and uptrend in overall inflation rate triggered by rise in primary product prices.

In the 1970s, double-digit inflation characterized all the three drought/poor rainfall years, with 1974-75 registering a record inflation rate of 25.2 percent (with primary commodities also rising by 25.4 percent), reflecting the effect of not only reduced supplies but also an amplified psychology of shortages.

1974-75 was also the year when the economy was exposed to the most severe oil price shock with the formation of the OPEC cartel. The combined effect of drought and the external oil shock pushed up the inflation rate to record levels. (see table below)

Years of drought/poor Rainfall in India

Drought/poor rainfall years	All India rainfall (percentage departure from normal)	Average inflation (percent)			Growth rate Agri prod.	percent change Foodgrain prod.
		All Comm	Primary	Fuel		
1972-73	(-)24	10.0	13.9	5.0	(-)5.6	(-)7.7
1974-75	(-)12	25.2	25.4	51.1	(-)2.8	(-)4.6
1979-80	(-)19	17.1	14.4	15.5	(-)13.4	(-)16.8
1982-83	(-)14	4.9	3.8	7.5	(-)0.5	(-)2.8
1986-87	(-)13	5.8	5.4	6.7	(-)0.6	(-)4.7
1987-88	(-)19	8.2	9.7	3.7	(-)1.4	(-)2.1
2002-03	(-)19	2.6*	2.8*	4.6*	-	-

* week ended January 18, 2003

There were three poor rainfall years in the 1980s. Agriculture (and foodgrains) growth was negative during these years and inflation rate ranged between 5 to 8 percent. In recent years, the agricultural economy has by and large moved from a shortage to a surplus situation and is thus more insulated against the vagaries of nature. Therefore, despite the failure of monsoon, average inflation rate remained low thanks to surplus stocks of foodgrains during the last three years. Reduced dependence of foodgrain production on rainfall has helped reduce the severity of the drought. The impact of the present drought could have been more severe had it not been for the fact that today 55 percent of foodgrains are being produced in irrigated areas and only the remaining 45 percent produced in rainfed areas as against only 33 percent of foodgrains produced in irrigated areas in 1987-88 and about 25 percent in the early 1970s.