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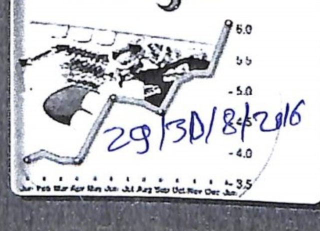

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Efeects of Inflation on Dairy Industries

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- **Introduction :**

Inflation in the price of milk in recent years has been sharp and surprising. It has been persistent now for some time. The questions to ask are Why? What can be done? and Why is it important?Before we answer these, here is some background. India is the world's largest milk producer, accounting for 16 percent of global production. It is also the world's largest consumer of dairy products, consuming almost all of its production. Dairy products are a major source of protein for a population that practices wide spread vegetarianism. Culturally, the Indian diet has a special place for dairy products.

India is estimated to produce 137 million tonnes of milk in 2013-14. Milk production has grown at an annual rate of about 4.2 percent over the last 20 years. This increase of 4.2 percent comes largely from the increase in the number of animals and only to a limited extent from productivity increases. However given the robust increase in production, the per capita availability of milk has bucked the international trend and increased at a 2 percent CAGR from 178 gms/day to 290 gms/day over this 20 year period. This aggregate number masks a wide range in per capita milk availability in states that ranges from a low of well under 100 gms/day in North Eastern states to 930 gms/day in Punjab.

Globally, the dairy sector is one of the most distorted agriculture sectors. Producer subsidies are in place in many developed countries encouraging surplus production. Export subsidies are paid to place this surplus on world markets and tariff and non-tariff barriers are erected to protect domestic producers from 'unfair' competition. The European Union (EU) alone spends about Euro 20 billion each year on dairy subsidies. Despite this, the dairy sector is a very localised business because it is a bulky and perishable product. Only 7 percent of the global annual milk production of 800 million tonnes is traded.

The dairy industry in India has grown strongly for a long period of time despite the benign neglect of the dairy industry after the Operation Flood years (some may say this it is because of the Government's lack of interference that it has grown). However, this growth has come in an ad-hoc manner and without the institution building that will benefit farmers, processors and consumers.

However, the time has come for some institution building and for measures to be taken to mitigate milk price inflation.Inflation can be tackled by creating a cushion in the short or medium term and by improving productivity over the longer term. In order to balance the volatility of prices that comes about because of annual and seasonal variation in milk production, a method has to be devised to create a strategic reserve (SR) for milk powder. This strategic reserve could be organised on a zonal basis under

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the regulatory authority of the National Dairy Development Board (NDDB). The SR should be built up when there is excess production and also as a percentage of exported milk powder. at market milk prices that are averaged over more than one cycle. The SR can over time be augmented with a liquid futures market in dairy and dairy products. Such futures have been launched in the United States and have gradually taken over the role of the buffer stock programme.

- **Objective of Paper :**
  1. To know the effect of inflation on Milk industries
  2. To know the factors affecting Milk price
  3. To know the rising price effect in Milk market

- **Research Methodology :**

  For this paper the secondary data sources have been studied published in books, Journals, Online databases and Govt web portal.

- **Inflation :**

  Inflation Wholesale Price Index (WPI) based weekly inflation rate went into negative territory at the beginning of June 2009. The inflation rate was recorded at -1.61 per cent for the week ended June 6. This raised fears of deflation, but the negative figure has to be seen in context of the high inflation recorded during middle of 2008. Inflation as measured by year-on-year variations in the wholesale price index (WPI), had increased sharply from 7.7 per cent at end-March 2008 to an intra-year peak of 12.9 per cent on August 2, 2008, reflecting the impact of some pass-through of higher international crude oil prices to domestic prices as well as continued increase in the prices of metals, chemicals, machinery and machinery tools, oilseeds/edible oils/oil cakes and raw cotton. The double-digit inflation caused the government to initiate measures to keep prices in check. Subsequently, when effects of global economic downturn were felt across the world, international commodity prices crashed. This caused WPI inflation to decline sharply to 0.3 per cent as on March 28, 2009. During March-June 2009, inflation has been around zero. This has raised fears of recession / deflation. However, most experts are of the view that fundamentals of Indian economy continue to remain strong and there is no noticeable contraction in demand. Usually, in most of the developed countries, inflation is published based on Consumer Price Index (CPI). A CPI-based inflation tracks the year-on-year rise in prices paid by consumers to retailers. In India, the general inflation is published based on the WPI. The WPI tracks the yearon-year rise in prices at the wholesaler level. It tracks a much wider basket of commodities including industrial commodities.

- **Dairy Price Index:**

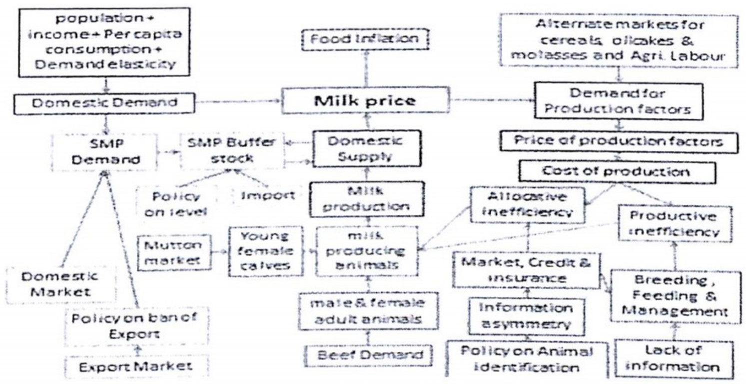
  Consists of butter, SMP, WMP, and cheese price quotations; the average is weighted by world average export trade shares for 2002-2004.

  - Key Areas of Concern in the Dairy Industry
  - Competitiveness cost of production, productivity of animals etc.

The demand for quality dairy products is rising and production is also increasing in many developing countries. The countries which are expected to benefit most from any increase in world demand for dairy products are those which have low cost of production.

- Production, processing and marketing infrastructure: If India has to emerge as an exporting country, it is imperative that we should develop proper production, processing and marketing infrastructure, which is capable of meeting international quality requirements.

Figure 1 Conceptual diagram on factors of Milk Price in India



Source : https://www.iimb.ernet.in/research/sites/default/files/WP%20No.%20472_1.pdf

- Import of value-added products and export of lower value products : With the trade liberalisation, despite the attempts of Indian companies to develop their product range, it could well be that in the future, more value-added products will be imported and lower value products will be exported. The industry has to prepare them to meet the challenges.

Specifically, we examine how the international prices are transmitted to domestic markets through levels of domestic buffer stock of SMP and why a mere rise in the price of milk is found to be insufficient to incentivise Indian dairy farmers to enhance investments in dairy animal rearing and technology to increase milk supply. The latest USDA Global Agricultural Information Network (GAIN) Report of Oct 2014 also reaffirms its earlier doubts about the ability of the existing initiatives of the government including the National Dairy Plan and the organised milk trade which accounts for only 30% of total milk production to be able to service the growing domestic demand for milk (Mani and Intodia 2014).

- **Conclusion :**

The reasons for the persistent rise in the price of milk in India were analysed by understanding the causal factors that contribute to its demand and supply. Between 2006 and 2013, the international price was fully transmitted to the domestic price, resulting in a near similar percentage rise. While this increase came with a high level of price volatility in the international market, the rise in the domestic price was steady and continuous. Since 2006, global price is seen to be transmitted to the domestic price due to a IIMB-WP N0. 472 31 probable reduction in the level of domestic buffer stock on account of free export of SMP. It was this domestic buffer stock of SMP that had moderated the milk price rise, in previous years. The ban on export was lifted not due to glut in domestic stock of SMP but to enable the SMP manufacturers benefit from the then prevailing high international price. After 2006, growth in demand for milk in India is rising at twice the growth rate of milk production; 6% to 8% vs 3% to 4%, making that year a turning point for the Indian dairy sector. This is confirmed by the growth in per capita milk consumption, post-2006. The growth in milk consumption in developing countries is expected to continue, offering livelihood opportunity for milk producers in India, especially the small and marginal farmers who own 71% of the productive adult populationli (Delgado 2003). With increased demand for milk and the supply not responding to it, there is a continuous and increasing mismatch between the two, leading to persistence in milk price inflation. The alternative to domestic production is importing of SMP. However, this is not a viable alternative for milk due to its high and perpetual requirement, limited availability and high price volatility in the international market and high current account deficit (Kolhar 2013). Further, demand for milk in many Asian countries which are net-importers of milk such as China has also picked up. With few exporting countries and limited quantity available for international trade, a small increase in the domestic demand could affect the international price disproportionately

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