

## Onion Rs65/kg, petrol Rs65/lt, beer Rs65!

*For the first time in history, basic needs, lifestyle needs and luxury needs are at the same price, prompting us to explore why basic needs like onions are so expensive*

### □ Event:

Maslow's 'Need Hierarchy pyramid' has transformed into a rectangle. For the first time in history, basic needs, lifestyle needs and luxury needs are all at the same price. Onion prices have more than doubled in the past year, touching a peak of Rs75-80/ kg. This prompted us to explore the drivers of this phenomenon and get a better sense of the ground realities.

We visited Pimpalgaon and Lasalgaon – Asia's biggest onion wholesale markets (240km from Mumbai) – and interacted with more than 25 farmers, a wholesaler, an assistant to the APMC chairman (Agriculture Produce Marketing Committee), and visited three farms. Our takeaways:

### Our Pimpalgaon and Lasalgaon visit... snapshots



Sources: IDFC Securities Research

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## □ Key takeaways

### Supply-driven concerns:

The key reason for price increase has been a severe supply shortage arising from unseasonal rains. While the typical yield for the Nashik red onion, harvested in November is 70-80 quintals per acre, the current yield is only 5-10 quintals per acre due to unseasonal rains in October which damaged the crop just before harvest season.

### Unviable farm economics

The cost of growing onions is ~Rs25000 per acre, while current realizations are Rs2500-3000 per quintal. With yields falling to as low as 5-10 quintals per acre, a farmer's net realization leaves him struggling to even break even.

### Deciphering the onion price chain

In a normal year, a farmer earns Rs 8-10/ kg with yields of 70-80 quintals per acre. A wholesaler incurs ~Rs5/ kg as costs for packing and transportation and adds a 10% margin. We estimate the retailer makes ~20-25% margin (we did not meet any retailer).

Based on the data obtained, our guess is that wholesalers and retailers are making similar margins as last year, but at a higher profit per kg.

### Onion price chain

	Farmer	Wholesale	Retailer
Current sale price	Rs25-30/kg	Rs35-40/kg	Rs45-50/kg
Normal year sale price	Rs8-10/kg	Rs15-18/kg	Rs20-25/kg
Drivers of price	Sowing Seeds Fertilizers Pesticides (~25000/acre)	Rs5/kg transportation and packing 10% margin	Margin

Source: IDFC Securities Research

### Did middlemen gain when onions touched Rs70-80/ kg ?

In December, the price of onions at Lasalgaon touched Rs60/ kg as (albeit very briefly, as the average price of red onions was Rs20/ kg in December). When prices hit Rs60/ kg at the farmer's level, the retailer was forced to sell at Rs70-80/ kg to retain his profit levels. *We believe hoarding, if at all, would have occurred at this time. When prices of onions stabilized at ~Rs20/ kg, middlemen/ retailers could have gained by holding on to the same prices in the pretext of high input prices. However, in the absence of concrete data, this remains a hypothesis.*

### Pressure on onion prices to sustain

Onions are harvested thrice a year – December, March and May. The next onion harvest is expected only in March thereby immediate pressure is visible for the next two months. However, we see pressure on onion prices even beyond that as unseasonal rains have also damaged seeds, due to which seed plantation is believed to be lower than last year. This variety of onions, known as 'Fursangi' and harvested in March and May, has a significantly high shelf life and can be stored for 4-5 months. If supply is lower during the March and May harvests, pressure on onion prices will sustain until next November (assuming no further impact from weather changes).

### Government interventions reduce prices, impacting the farmer

The government has intervened to quell the onion price rise by banning exports, and has been instead importing onions from Pakistan. While this additional supply is expected to provide short-term relief, an indirect burden is getting passed on to farmers, who are forced to sell at lower prices and suffer higher losses.

**Unseasonal rains – tomatoes and grapes suffer as well**

While onion prices received media attention, what has gone relatively unnoticed are tomatoes and grapes which also grown in this region and were damaged by the unseasonal rains. Prices of the items have doubled in the last year to 60Rs/ kg and 40Rs/ kg respectively. With harvests twice a year for tomatoes and once a year for grapes, we foresee sustained pressure in these commodities too.

**❑ Our view**

We believe pressure on the price of onion, tomatoes and grapes is going to sustain for at least 6-9 months due to supply shortage (albeit not to the same levels seen last month when onion prices touched Rs 70-80/ kg). A bigger concern, though, is the possibility of high sustained inflation continuing, especially if supply shortages occur frequently across food commodities (as seen in the past year). Even if supply gets back to normal levels, prices will not reduce to the levels last year for two reasons: 1) farmers, having seen increasing crop disruptions, will demand higher prices in normal years to create a higher safety net for a bad year; 2) having seen that the consumer is willing to pay Rs60/ kg, the entire supply chain will attempt to extract slightly higher prices than earlier (scarcity-driven prices that touch super-normal levels always settle at a higher normal due to the sticky nature of inflation). In this case, with onion prices currently at ~Rs45/ kg (up from Rs 20/ kg last year), even if supply does get back to normal in 6-9 months, it is unlikely to get back to Rs20/ kg seen earlier and is more likely to settle at ~Rs25-30/ kg (still at least a 20% increase). While government interventions in terms of export bans are likely to provide temporary relief to consumers, the threat of sustained long-term inflation is likely to stay.

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