

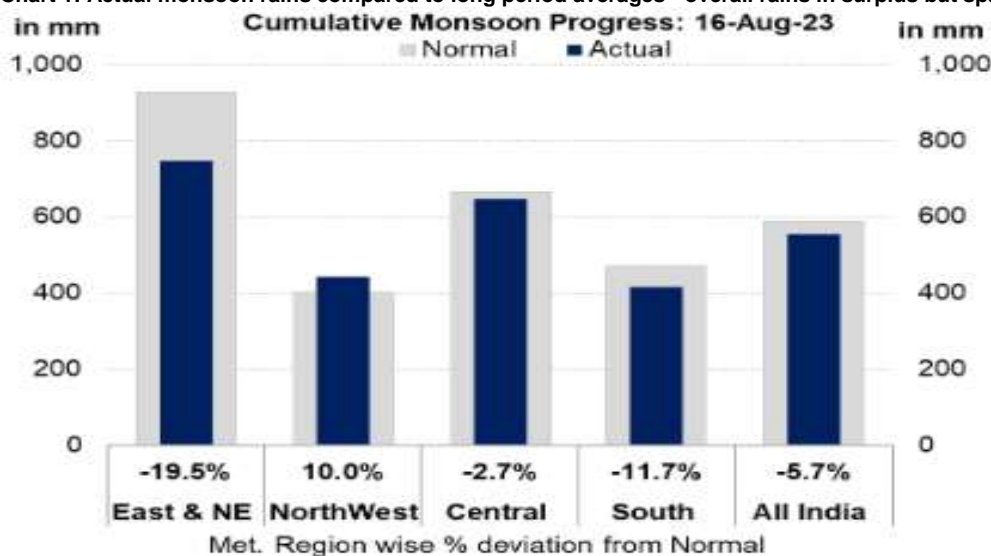
Monsoon back in deficit

A deficit monsoon with very poor spatial and temporal dispersion might adversely affect crop sector output. El Niño is now likely to resurface during Sep-Nov.

Monsoon rains are now in a deficit as rains vanish almost across the country.

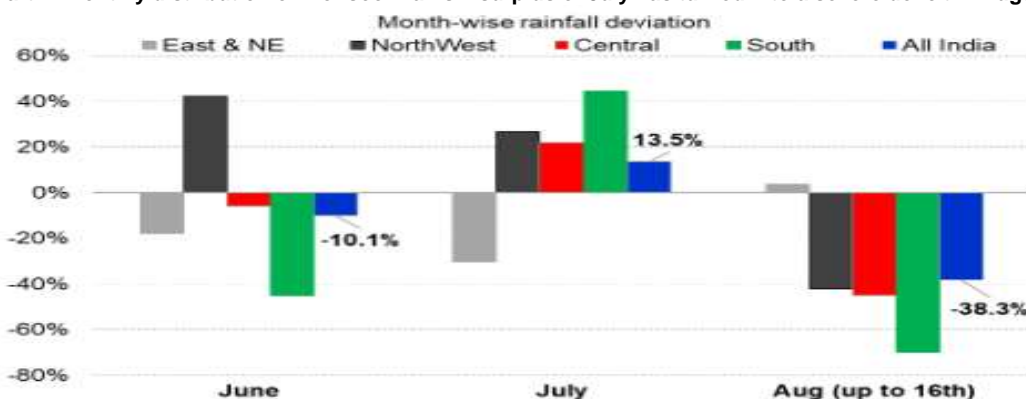
- Monsoon progress remains uneven: initial June deficit of 10.1% was covered by surplus rains in July (monthly surplus of 13.5%) but has been followed by sharply weaker rains in August (monthly deficit up to 16th of 38.3%).
- Overall monsoon deficit of 5.7% as of 16th Aug. stands in stark contrast to peak season surplus of 7.1% on 28th July.
- Apart from the quantitative deficit, quality has also been very low as seen in the lopsided temporal and spatial distribution.
- Monsoon metrics include extremely intense and concentrated rainfall: this has led to retarding cropping activity as much as deficient rainfall especially in the Kharif season where dependence on rains is heavy.
- Spatially, off the four meteorological regions, only North-West is in surplus (10%)
- Around 50% of districts in states of UP, WB, BR, JH, and KL and 37% of all districts have received deficient rains.
- In addition, 21% of districts received heavily surplus rain, which as noted above regards cropping.
- Temporally too, quality of the monsoon has been poor, with dry conditions followed by torrential rains, causing rivers to overflow and flood fields.

Chart 1: Actual monsoon rains compared to long period averages - overall rains in surplus but spatial distribution remains skewed



Source: Axis Bank Business and Economic Research Team

Chart 2: Monthly distribution of monsoon rains – surplus of July has turned into a severe deficit in August.



Source: Axis Bank Business and Economic Research Team

Quality issues are also hidden in sowing indicators

- Kharif coverage, though overall marginally better compared to last year, masks damage caused due to poor quality rainfall.
- Coverage under pulses is lower by 8% compared to previous year: arhar (-5%), urad (-13%) and moong (-7%) and this could aggravate the problem of rising pulses' prices unless supply measures are taken.
- The sharp increase in vegetable prices might therefore prove to be the precursor to events that may crop up later.
- As an example, consider tomato prices, which initially rose on excess rains due to transportation disturbances, though over time, crop damage in hilly regions of North India exacerbated the issue. Prices of tomatoes have since cooled off from peak levels but remain elevated.
- Shortages due to lower foodgrains output could be more damaging for inflation, given the longer time-period required for course correction and in some case may have to wait for the next Kharif crop.

Extrinsic vs intrinsic volatility

- Global implied volatility benchmarks tend to move together, with periods of low and high volatility clustering across asset classes which is a consequence of financialized, algo-driven markets.
- INR volatility measures also tend to track these extrinsic measures, moving close to EMFX implied volatilities. But there are divergences which open and close over time.
- These divergences are due to factors intrinsic to the INR, and also largely align with the three phases of INR management noted above.
- A chunk of movements in intrinsic volatility are explained by sensitivity to volatile global hot money flows.
- This is seen when the CAD and capital flows ex FPI and RBI forwards (both proxies for stable gradual flows) are superimposed with hot money FPI flows.
- When stable capital flows are much larger than the CAD, there is a large margin for FPI volatility to be absorbed, leading to low intrinsic volatility.
- In contrast, when the gap is small or negative (2008, 2011, 2014, 2018 and 2022), volatility increases sharply.

EI-Niño alert continues with development likely during Sep-Nov period

- The Southern Oscillation Index (SOI) reversed rapidly, to deeply negative levels. Even though momentum has stalled recently, levels below -7 are indicative of EI-Niño conditions.
- The Australian Bureau of Meteorology's El Niño alert continues (in the latest release on 15th Aug), with El Niño development likely during Sep-Nov'23.
- Though the Sea Surface Temperatures (SST) in the tropical Pacific are exceeding thresholds, the weaker than average Trade winds are not yet consistent with atmospheric conditions usual during El Niño events.
- At the same time, the Indian Ocean Dipole (IOD) which is currently neutral is likely to turn positive during Sep-Nov'23 - normally supporting rainfall in the Indian sub-continent. This will likely offset the negative effects of El Niño.
- Revival of monsoon rains is imperative at this juncture to support Kharif crops, and to be assured of improved agriculture output in the year.

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