

## The changing dynamics of India's consumer economy

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***The propensity to spend is almost identical for bottom 10% households in rural & urban areas, but there are considerable differences in spending power in case of top 10%.***

For a consumer demand-driven economy such as India, understanding consumption patterns is key to predicting economic growth. In recent years, the linkages between slow economic growth, high inflation and consumer demand have been more than evident. While demand for products can be measured in both volume and value terms, it is difficult to quantify demand for public goods and services such as education, health, etc. So as to understand consumer demand across the entire spectrum of consumption categories, the value of spending emerges as a more reliable measure. Indian households have a large and diverse consumption basket, and high income inequality and regional diversity makes the exercise of analysing consumption behaviour even more complex. In an ever-changing socio-economic environment, there is a need to understand the current dynamics of the Indian consumer market to be able to reliably predict future consumption patterns.

The Indian consumer economy grew at an annual rate of 5.7% between FY05 and FY15 in real terms. The pace of growth during the last decade was slightly faster than that observed between FY94 and FY05. Overall, rural consumption grew at a slower pace than urban during last decade. The annual growth of the Indian consumption market is estimated to be 6.7% during FY15-FY20 and 7.1% during FY21-FY25. In monetary terms, this amounts to an estimated consumer market of R34 lakh crore for FY15, expected to grow to R50 lakh crore in FY21, and expand to R71 lakh crore in FY26. This equals to 43.6% of Private Final Consumption Expenditure as reported by National Account Statistics. Even though urban consumers have relatively higher spending power, rural India with a huge population base (70% of total) constitutes more than half of total household sector spending at present (53% in FY15).

Now, let us look at how the consumption basket of Indian households has evolved over the last two decades. Indian spending can broadly be divided into two distinct categories: Necessities and Discretionary Spending. While necessities include food and clothing, discretionary spending includes all other expenses. Trends in share of consumption on these two broad categories have followed opposite directions, with discretionary spending gradually getting more prominence in the consumption basket. Over the years, the gap between the two started narrowing down and eventually the shares became almost equal in FY12, and thereafter discretionary spending started getting a slightly greater importance. It is estimated that, in FY15, Indian households spent a slightly higher share of their total household budget (52%) on expenses other than food and clothing (48%). As per our forecasts, discretionary spending is expected to contribute 55% and 58%, respectively, to total consumption in FY21 and FY26.

Consumption patterns reflect the changes taking place in the economic status of households. For lower income households, the emphasis is on essentials such as food items. But as their disposable income grows, spending on durables, health, education and investment-related products comes into play. For the bottom 10% households, necessities form an overwhelming share of their consumption basket as these households spend a considerably large proportion of their total expenditure on food and clothing. Even though the gap between the two shares is narrowing, they are still way off from a meeting point. Currently, the bottom 10% households spend 63% of total consumption expenditure on necessities. In

contrast, for the top 10% households, discretionary spending outpaced necessities by the end of 1990s. The data reveals that once discretionary spending takes over, there is a much slower change in the share over time. Between FY05 and FY12, expenditure on necessities came down by 1 percentage point only, from 34% to 33%. In FY15, the same proportion is expected to come down to 32%, reaching a saturation point thereafter.

When we look closely at growth of different segments of the consumer market over the last decade, it is observed that some markets have stagnated, some slowed down and others are growing much faster than before. Between FY05 and FY15, out-of-pocket expenditure on durable goods grew at a relatively faster pace than most other categories, at 10% per annum. Education and conveyance are the next two fast growing segments, registering 9% growth each. The bottom two segments in terms of pace of growth are observed to be food (4.2%) and non-food FMCG (4%). Among various food components, beverages and processed food, as a combined category, has had the highest growth. Real growth in spending on food, non-food FMCG, consumer services and education actually slowed down a little during FY05 to FY15, as compared to that during FY94 to FY05. Among food components, the pace of growth declined, especially on essentials such as cereals, edible oil, fruits and vegetables. On the other hand, the segments that have experienced some of the highest increases in growth in the last decade as compared to a decade earlier are apparel, footwear and healthcare.

## Annual growth in household spending

(%, at 2004-05 prices)

Consumption categories	FY94 to FY05	FY05 to FY15	FY15 to FY21
Food	3.0	4.2	5.3
Apparel & Footwear	3.3	6.1	6.2
Health Care	7.1	8.2	8.3
Education	11.5	8.9	8.9
Conveyance	8.7	9.1	9.1
Non-food FMCG	4.9	4.1	5.0
Durable goods	9.8	10.1	10.3
Consumer services	10.6	6.8	6.9
Others	8.4	5.8	6.8
<b>Total consumer market</b>	<b>5.0</b>	<b>5.7</b>	<b>6.7</b>

Source: Indian Consumer Market 2020: Structure, Size, Growth and Intensity, Rajesh Shukla & Mridusmita Bordoloi, 2015, PRICE

whole does not completely reveal the huge differences in spending intensity across rural households. The average spending of a household from the top decile in rural India is three times higher than that of a household from the bottom decile. However, the inequality is much greater among the bottom and top deciles in urban India. An average household from the top decile in urban spent around six times more than that spent by a household from the bottom decile. The propensity to spend is almost identical for bottom 10% households in rural and urban areas. But considerable differences in spending power are observed for top 10% rural and urban households. The latter spends more than twice the amount spent by the top 10% rural households.

Rural and urban consumers behave differently in terms of their spending behaviour and socio-economic characteristics. Policy-makers as well as business enterprises would be well advised to keep these differences in mind while formalising their plans, as a one-policy-fits-all strategy is bound to fail.

The analysis also reveals that there is a high level of inequality in household spending in India. Apart from the rural-urban differences in spending power, there is inequality within rural areas and similarly within urban pockets as well. Therefore, spending pattern in rural India as a

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