POST COVID19 CHALLENGES ON INDIAN ECONOMY

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Abstract- Covid19 created an economic emergency in the world. The economic impact of covid19 can be analyzed on two grounds. First, in terms of the ripple effect of Covid19 in the advanced countries to the rest of the world. Second, in the context of an overall slowdown in the Indian economy. Mitigation measures of covid19 through lockdown and social distancing entails severe economic costs. India's growth is service-led and consumption driven. Suspension of transportation and border closure hit the service driven growth of the country. India faces a considerable fall in consumption demand in the absence of work.Government of India (GoI) announced a stimulus package of 1.7 trillion rupees (0.8 per cent of GDP) which covers income security, health, and food security and The Reserve Bank of India (RBI) injected liquidity through policy rate cuts to attenuate the crisis. Predominance of informal sector, active inter-state trade within the economy, and weakness in the financial sector aggravates the consequences of Covid19 on Indian economy.Apart from policy interventions, behavioral factors will play an important role in the recovery process.

Keywords- Covid19, pandemic, globalization, economic effects, India

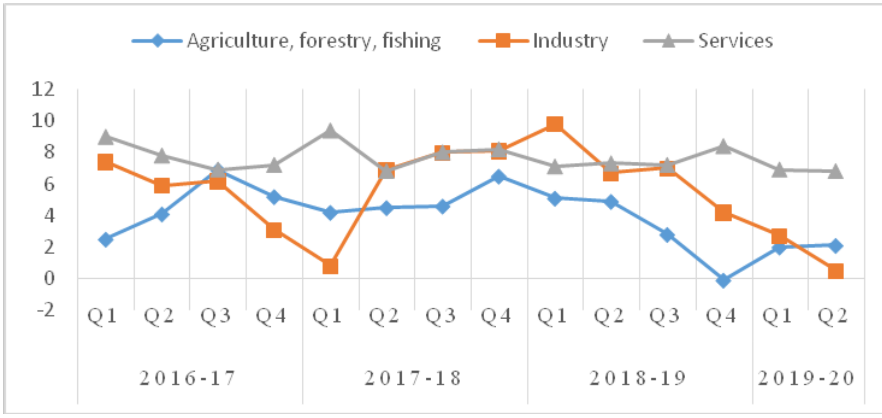
I.INTRODUCTION

Covid19 created a health induced financial emergency in the world. Hunan sea food market in Wuhan city in China is considered as the epicenter of Covid19. An epidemic which was confined to China spread to almost all countries and territories of the world turning into a global pandemic. Covid19 assumes immense significance on several grounds. First, the uncertainty in its duration and spread along with the probability of multiple waves of infection. Second, absence of vaccine which makes it difficult to cure and control the transmission of the disease. Third, the economic impact of Covid19 which stems from the first two aspects. That is, high transmission rate of Covid19 and absence of vaccine have forced nations to adopt the "Early China Model" of controlling the spread through social distancing and lockdown. Countries across the world resort to testing, identification and, quarantining, shutting down schools, offices, industries, and commercial establishments, suspension of transportation and border closure. Economic activities are confined to essential services. In other words, mitigation measures come at the cost of economic growth. Trade-off between mitigation measures (social distancing and lockdown) and economic growth have led to 'life vs livelihood' debate because protection of life bears a cost on livelihood and vice versa. The economic impact of Covid19 becomes more profound in a globalized world which increases the spillover effect of economic shock to other countries. This is detrimental for Indian economy which is on a slowdown since the last few quarters. In this context, the paper examines the potential impact of Covid19 on Indian economy.

The rest of the paper is organized as follows: An overview of economic situation in India on the eve of Covid19 is explained in Section II. The impact of Covid19 on Indian economy is explained in Section III. Policy measures initiated by the Government of India (GoI) and the Reserve Bank of India (RBI) are discussed in Section IV. Section V gives important Discussions. Conclusion is given in Section VI.

II. AN OVERVIEW OF INDIAN ECONOMY

India is the fifth largest economy in terms of nominal GDP and third largest in terms of Purchasing Power Parity. GDP at current prices is estimated to be US$ 2.9 trillion. India transcended from an agrarian economy at the time of independence to a service-led economy. According to Economic Survey 2019-2020, service sector accounts for 54.3 per cent of India's Gross Value Added (GVA), industrial sector accounts for 29.6 per cent and agriculture sector contributes 16.1 per cent.



Data Source: Economic Survey 2017-18 to 2019-20

Figure1. Quarter wise growth of sectors (%)

The growth rate of agriculture and allied sector increased to 2 per cent in the first two quarters of 2019-20. The growth rate of industrial sector continues to fall to 0.5 per cent, while the service sector grew at the rate of 6.8 per cent in Q2 of 2019-20. The deceleration in industrial sector is primarily the result of the slowdown in manufacturing sector. Indian economy has been decelerating since 2016-17. The annual growth rate fell from 8.17 per cent in 2016 to 6.8 per cent in 2018[1]. A part of the reason can be attributed to the overall slowdown in the world economy. However, India's domestic sector is not free from problems. According to Economic Survey 2019-20, the economy faces both demand and supply side problems. Decline in real fixed investment is a major lag on the demand side. The fall in fixed investment rate is the result of drop in fixed investment in household sector and public sector as well as the slack in private corporate investment. The problems are more profound on the supply side with a deceleration in the growth rateacross sectors except agriculture and allied sector, and public administration, defense and other services. India's external sector showed signs of improvement. India's foreign exchange reserve amounts to US$461.2 billion on 10th January 2020. Robust Foreign Direct Investment (FDI) and Foreign Portfolio Investment (FPI), better trade balance and lower Current Account Deficits (CAD) give positive outlook to the external sector. (Economic Survey 2019-20).

III. IMPACT OF COVID19 ON INDIAN ECONOMY

As inferred from WHO Situation Report 86, African region and South-East Asian region of the world are comparatively less infected by Covid19. India accounts for the highest number of total confirmed cases as well as total new cases in the South East Asian region. The potential impact of Covid19 on Indian economy can be analyzed on two grounds. First, through the ripple effect of Covid19 on advanced economies, most importantly China, to the rest of the world. Second, in the context of the slowdown in India's economic growth. Furthermore, predominance of informal sector, active inter-state trade within the economy, and financial sector weakness exemplifies the consequences.

Globalisation has led to increased inter-dependence among nations. According to Bhagvati (2006) economic globalization comprises of trade, direct foreign investments, short-term capital flows, international flows of

[1]World Bank data

humanity and technology transfer. They act as channels for transmission of benefits as well as shocks to world economies. The economic shocks of Covid19 spillover to the rest of the world through two channels viz., goods, services, knowhow, people, financial capital, FDI, foreign exchange and international banking (Baldwin and Mauro, 2020)and/or supply, demand, and confidence (Boone, 2020).The magnitude of spillover of economic shock is well understood in the context of the dominance of China, Korea, Italy, Japan, the USA, and Germany in the global supply and demand (about 55%), global manufacturing (about 60%) and global manufacturing exports (50%) (Baldwin and Tomuira, 2020).India shares a strong trade relationship with China, USA, European Union, Hong Kong, Saudi Arabia among others. As on 2018,14.6 per cent of India's merchandise trade originated from China. Indian industries such as consumer electronics is heavily dependent on Chinese import for component parts. Lockdown of Chinese economy has led to severe drop in working hours and production. The first two months of 2020 registered considerable decline in China's industrial profits (38.3%), total retail sale of consumer goods (20.5%), and total value added of industries above designated size (13.5%).[2]The fact that China holds a significant position in the global value chain ramifies the consequence of slowdown in the Chinese economy to the rest of the world. Disruption in global supply chain lead to an increase in the price of inputs and final products especially when India is ill-equipped for an import substitution in the short run. The revival of Chinese economy is not unto itself but also on how quickly the rest of the world recovers.

Beyond the implications on external sector, Covid19 is detrimental to the domestic sector of India which is on a slowdown since Q4 of 2018-19. Covid19 poses a serious challenge to the agriculture sector. The agriculture sector in India shows a gradual revival in its growth since the last two quarters. The sector is characterized by predominance of food crops, shrinking agriculture landholding, and heavy dependence on monsoon. The importance of agriculture sector in Indian economy lies not only in ensuring food security but also in providing livelihood to the rural economy. Agriculture and allied sector accounts for 48 per cent of the total workforce in India. Growth rate of agriculture sector revived in the recent quarters after muted growth in Q4 of 2018-19. Lockdown of the economy due to pandemic which coincided with the harvesting season of rabi crops is problematic. Although harvesting and marketing of crops are exempted from lockdown, the sector suffers from labour shortages as most of them, especially migrants, returned to their home town due to pandemic. Shortages of skilled labourers and machineries have affected the harvesting of rice and disrupted crop cycle in plantation sector in different parts of the country. Logistic issue affects procurement and marketing of crops both within and outside the states. India has a strong regional or inter-state trade in agriculture products. States are not self-reliant and depend on neighboring states for agriculture products. India is a major export market for rice, bovine meat, cotton etc. The near economic inactivity not only affects rural livelihood but significantly lowers the export potential of the sector in the immediate term.

Manufacturing hit a downturn affecting supply, jobs, and exports. Traditional industries in India like handloom, handicrafts, coir, cashew, bricks etc. and micro small and medium industries (MSMEs) which are already facing shortage of skilled labourers, adequate marketing facilities, low production capacity, and financial and technological bottlenecks are vulnerable to losses and may become non-viable in the worst case.Industries with exposure to China such as consumer electronics, automobile industry, apparel industry etc. face severe downturn. Closure of industrial units and workplaces lowers electricity consumption thereby reduce revenue generation in power and energy sector.

A distinctive feature of India's economic growth is service led growth. Tourism, hospitality, transportation and IT contributes significantly to the economy. Suspension of trains and flights and border closure affects India's tourism sector which at present contributes 9.2 per cent of GDP. Foreign exchange from tourism will decline considerably in the peak months of April-May. These sectors employ large number of daily wage earners and contractual employees who face temporary unemployment. Tourism sector creates externality in the form of additional employment in the informal sector which is unaccounted for. This will add up the job losses multiple times than what will beactually accounted for. The impending fear of a second wave of infection can induce an aversion to trips and travel, further derailing the recovery process of the sector.

An atypical characteristic of India is predominance of informal sector. According to Murthy (n.d), informal sector accounts for nearly 83 per cent of workforce and contributes 50 per cent or more to the GVA. Workers in the informal/unorganized sector lack job security and fixed income. Informal sector is prevalent in agriculture,

[2]Press releases in National Bureau of Statistics of China website

trade, real estate, construction, professional services etc. and other services, with agriculture accounting for the highest share(Murthy, n.d.). Migrant labourers and casual workers constitute a significant share of informal sector workers. A large majority of migrant labourers in different parts of the country returned to their villages during the lockdown. Economists point out a behavioural change among migrant workers which would limit their re-entry into exiting workplace as they would prefer to work in their home-town instead of finding work in faraway places. A shift in inter-state migration could jeopardize the growth process of states like Kerala which has widespread presence of migrant workers in construction sector, plantation, paddy fields etc.

According to world Migration Report, India has 17.5 million international migrants.The Report statesIndia is the largest source of international migrants in the world and total inward remittances to the country exceed US$ 67 billion.High income countries like the USA, United Arab Emirates (UAE), Saudi Arabia, Switzerland and Germany are the major source of remittances to the world(World Migration Report, 2020). Migrant remittances have been a major catalyst in India's consumption-led growth. The general slowdown in high income countries along with pandemic induced deceleration affect the earnings and hence the inflow of remittances to India. Decline in remittances from rest of the world can drag the recovery process in a consumption-driven economy.Growing period of uncertainty make Indian stock market bearish causing massive sell off by domestic and portfolio investors.

IV. POLICY MEASURES

The International Monetary Fund (IMF) suggested proper coordination of fiscal, monetary and regulatory framework to overcome the economic emergency created by Covid19. Countries across the world announced combination of fiscal and monetary policy stimulus to help the economy combat the crisis. Government of India (GoI) announced a stimulus package of 1.7 trillion rupees (0.8 per cent of GDP) income security, health, and food security. The Reserve Bank of India (RBI) injected liquidity through policy rate cuts. Major fiscal and monetary policy measures adopted by India include[3]:

4.1 Fiscal policy-

i. 5kg wheat/rice and 1 kg preferred pulses free for next three months for 80crore poor people.
ii. Increase in MGNREGA wage to Rs. 202 a dayfor 13.62 crore families
iii. Rs. 50 lakh medical insurance cover for next three months to all health workers including doctors, nurses, and ASHA workers.
iv. Rs. 500 per month for next three months to be transferred to 20.4 crore women JhanDhan account holders and ex-gratia transfer of Rs. 1,000 to 3 crore senior citizens, disabled people, widows among the poor.
v. Rs. 2000 to 8.7 crore farmers under the Pradhan MantriKisanYojana
vi. Rs. 20 lakh collateral free loans to be given to women Self Help Groups (SHGs)
vii. Free cylinders for the next three months to 8.3 crore BPL families
viii. Construction Workers Welfare Fund to be used by the States for the relief measures of registered construction workers
ix. Wage earners below Rs. 15,000 per month employed in businesses with less than 100 workers to receive 24 per cent of monthly wages into their PF account for three months.

4.2 Monetary policy-

i. Repo rate reduced to 4.4 per cent (75 basis point cut)
ii. Reverse repo rate reduced to 4 per cent (90 basis point cut)
iii. Cash Reserve Ratio (CRR) reduced to 3 per cent (100 basis point cut) of Net Demand and Time Liabilities
iv. Marginal Standing Facility(MSF) and Bank rate reduced to 4.4 per cent from 5.15 per cent
v. Open market purchase of Rs. 10,000 crore on March 20, Rs. 15,000 crore on March 24, and Rs. 15,000 crore on March 27 was made to strengthen liquidity

[3]Based on IMF policy responses to Covid19, RBI Governor's Statement March 26, 2020, https://www.thehindu.com/business/Economy/17-lakh-cr-package-with-doubled-food-rations-cash-

vi. Accommodative stance to be continued, keeping inflation within the target of 4 per cent (CPI inflation) with +/- 2 per cent variation.
vii. Three months moratorium on loan repayment.

V. DISCUSSION

The spread of Covid19 across the world shows how a real shock in the form of a disease outbreak propagates through channels of globalization leading to the disruption of demand and supply operation across the world. For India, with its strong international relation in the form of trade and immigration, pandemic weakens the stability attained by the external sector in recent times. Consumption is the propeller of India's growth process. Absence of work affects earning capacity of individuals which in turn affects their consumption. According to Suresh (2020) in an economy characterized by inequality in cash holding, the lowest 47 percentile of the population will run out of cash by the end of the first phase of lockdown and the population between 47^{th} percentile and 87^{th} percentile will be left with half the cash they had. Workers in the informal economy and the poorest of poor will face job loss and cash crunch which will increase unemployment and poverty in India. The lockdown is damaging to the financial sector. Job loss and business shutdowns (especially in the MSME sector) in the worst case create credit default, increasing the NPAs of bank and affecting theirlending capacity. This can spiral into a credit crisis in the economy. An immediate V shape recovery primarily depends on the revival of service sector. Apart from policy interventions, behavioral factors will play an important role in the recovery process. The general fear and panic created by the infectious spread of the disease, if persist for the fear of a second wave,will dampen the growth of travel, tourism, hospitality and recreation sectors. Individuals have to behave like a caged bird set free, by spending more to drive the consumption-led growth of India. The government has to pump prime the economy, recapitalize banks, adopt remonetisation[4], and set cash in the hands of common man to fuel the consumption and demand in the economy.

VI. CONCLUSION

The economic growth of India is consumption driven. Muted working hours due to the pandemicwill lead to considerable fall in income which causes the consumption demand to fall to its lowest level. In other words India will face a considerable fall in aggregate demand resulting from a fall in consumption demand and an already dampened investment demand. This would endanger India's 'virtuous cycle of growth'. Predominance of informal sector, a small fraction of regular salaried employees in India's workforce, and prospects of job loss across sectors will bring more people below the poverty line. Shortfall in value addition and income generation or supply-demand constraint will accelerate the downward spiral. This lowers the possibility of an immediate V shape recovery of the economy.

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