Indian Economy’s Greatest Crisis: Impact of Coronavirus and the Road Ahead

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Preliminary

• Based on articles written since March, EPW Article Sept. 26, 2020
• And, Forthcoming book.

• Crisis facing Indian economy and society is greatest; collapse of economy unprecedented - its social and political impact will be long lasting.
Some Facts About Indian Economy

- GDP data erroneous – unorganized sector an issue
- For Q1 2020-21, data only partial – r.o.g -50% and not -23.9%
- Data on agriculture partial – target and not production
Some Facts (Contd.)

• Govt. claims Recovery after April but major sectors still weak
• CPI August at 6.69%. WPI in August at 0.16% before that -ve
• GDP in 2019-20 Rs.204 lakh crore = $2.87 trillion at Rs.71
• GDP in 2020-21 if 18% down,
  Rs.167 lakh crore = $2.26 trillion at Rs.74
If 29% down then Rs.145 lakh crore
• Q1 capacity utilization 48.2%; Investment fell 90% in April
• Exports and imports of goods fell about 50% in April
Unemployment

• Unorganized sector employs 94% and produces 45%.
• India unique case? – Massive migration from cities to villages
• Work stopped in non-agriculture except in agriculture
• Around 200 million lost work in April – different from CMIE – 122 million
• Distinction between employment and work
• Approx 450 million workforce – 45% in agriculture = 202 million. 248 million in non-agri. 27 million in organized sect.
• Those working, One fourth of 248 million = 62 million
Worst Performing Major Economy

Quarterly Growth Rates of Select Major Economies 2020
Health Aspect

• Testing inadequate so numbers of infection not fully known
• India eased restrictions when cases still rising – not in control
Lockdown and Its Imperatives

• Lockdown not a solution to disease
• Lockdown necessary to slow spread of disease – buy time
• Not properly implemented – sudden - Imperatives not implemented
  • Decongesting people in crowded areas
  • Supply them essentials where they were
  • Ramp up health infrastructure
  • Prevent small business from collapsing
• Disease spread to rural areas and small towns
Worse than World War/Global Financial Crisis

• Nothing like this faced globally – voluntary cessation of activity
• Situation worse than during World War or Global Financial Crisis of 2007-09
• During a war there is no unemployment and demand is full.
• In US in 12 weeks 44 million filed for unemployment
• Global Fin. Crisis was usual business cycle- demand shortage
• Now, demand has fallen drastically and supply disrupted
Impact of Lockdown on Poor and Marginalized

• Lockdown means very few are out/mixing with each other.
• Poor earn daily and buy essentials daily – cannot stock up.
• As soon as incomes stop, they start to starve.
• Desperate situation – willing to walk 1000 km - without food.
• Some may return for lack of work in rural areas
• Cottage sector producers exhaust their savings in a short while and will not be able to restart.
• Also, self-employed like, trader, mason, taxi and auto drivers and barber exhaust savings.
Organized sector

• Organized sector employees having fixed incomes may get some part of their salaries – firings taking place here also
• CMIE – 17 million lost work; 5 million professionals
• Can continue their consumption of `essentials’
• But reduced discretionary consumption
• Dissaving of the companies – So, cannot sustain for long
• Self-employed, elderly, retired, etc., eat into their savings
• `Wealth effect’ will impact expenditures of well off.
Business Failures

• Businesses which were already stressed will now face failure
• Highly leveraged firms will be the first to fail.
• Many firms in the financial sector are in this category
• When one firm fails to return a loan the next one also fails
• Moratorium for payment of interest will help
• But, revival is uncertain due to lack of working capital
• Will not be able to get bank loans due to fear of NPA
• Businesses that had large reserves will feel less of pain
Agriculture

• Primary sector consisting of Agriculture, mining, forestry and logging and fishing can continue
• But as incomes fall, demand for their produce declines.
• Then either they reduce production or their prices fall
• Price of the produce falls at source but rises in the consuming centres in urban areas, due to shortages and profiteering. Regulation of trade will be crucial.
• Need extended Procurement and supply in Urban areas
Gradual Recovery – not Steep V-Shaped

• Lock down being relaxed in stages – testing capacity still low.
• Fear of a second round attack
• Neither demand for discretionary items nor investment will revive soon
• Consumer sentiment and capacity utilization will remain low.
• So, production can only recover gradually - no ‘V’ Shaped recovery
• Not like a rubber ball - employment & incomes will revive gradually.
• Businesses that exhaust working capital or fail during lockdown will not be able to restart business. Banks will be wary of lending to them
• Banks’ own financial conditions will deteriorate
Note:

Series 1: V shaped Recovery after 2 months and back to January 2020 in 7 months. 
Series 2: U shaped Recovery after 2 months and back to January 2020 in 10 months. 
Series 3: U shaped Recovery after 2 months and back to January 2020 in 16 months. 
Series 4: U shaped Recovery after 2 months and back to January 2020 in 22 months. 
During Recovery it is assumed that there is a steady rise
Likely Rate of Growth for 2020-21

• In April economy at 25% of January level - just before pandemic - and gradual recovery in a year (optimistic)
  
  Fall in GDP this year will be around 30% (Say, Scenario 2)

• Economy would lose more than Rs.60 lakh crore ($811 billion) of production and GDP would come down to Rs.145 lakh crore ($1.96 trillion)

• Support would be required both for workers and the small businesses
• Big investment required in health infrastructure and tackling disease
• Require tightening governance
Government Resources and Deficit

• Taxes collected from incomes and production and consumption
• Tax collections will collapse - fall by much more than this amount
• Tax revenues of Centre and States could fall from 16% of GDP to 12% of reduced GDP of 2020-21.
• From Rs.36 lakh crore ($487 billion) it would be down to about Rs.17.4 lakh crore ($235 billion).
• Non-tax revenue will also decline in same proportion
• Government expenditures have a committed part like, interest
• Public investments can be postponed and new projects shelved to reduce expenditures. But economy will be further down
Lack of Resources – Need Survival Package

• Fiscal deficit was already 10% of expected GDP; would be 15.5% of reduced GDP – if Expenditures are not cut.

• Deficit rise due to fall in revenue (14.5% of the reduced GDP)

• Increased expenditures on sustaining half the population at half poverty level ($1.9 per person per day at Rs.75 to the dollar) for the year (amounting to 12.4% of GDP) and

• Increased medical expenditures on dealing with COVID-19, etc..

• Government would have to go for massive expenditure cuts to maintain population – need for a survival package
Pandemic and Labour

• Using the pandemic and lack of opposition – states changing labour laws – hours of work, bonus, industrial disputes, hire and fire, etc.

• Weakening labour further – lead to more alienation

• Not offering enough under MGNREGS so as to force labour to return to urban areas

• Need urban employment scheme

• Inequality will rise in education, employment, gender bias ...

• Employment and wages will fall
Package Announced

• Rs.20 lakh crore = $270billion - of this 10% is from budget
• Rest is loans and credit availability
• Or, policy changes that have been on the agenda since 2014
• Little of immediate relief – mostly medium and long run
• Privatization, pro corporate steps
• MSME changes - benefit to medium scale units
• Atmanirbhar and trying to attract foreign capital
• Agriculture steps to corporatize
• What investment will come now – when house burning...
Resources for Survival Package

• Resource shortage in budget due to deficit + revenue short fall + requirement of survival package = 22.5 + 20 + 18 = Rs.60 lakh crore, 41.4% of 2020-21 GDP; $810 billion
• Tax rates can be raised little except on essentials – difficult
• Tax expenditures can be curtailed and raise 5% of GDP
• Wealth tax also fraught with difficulties but can get 2% of GDP
• So, cut inessential government expenditures
• Salaries may have to be cut – when 80 crore are in distress
• Float COVID Bonds – Financial institutions + Wealthy
• Rest, RBI to monetize the deficit – not inflationary
Ethical Aspect: Need Social Justice

• New normal – capacity redefined due to physical distancing
• Marginalized more marginalized – unable to cope with crisis.
• Hit by demonetization, GST, NBFC crisis and digitization
• Workers seen as providing cheap labour for homes and businesses
• Unemployed are reserve army of labour - keep wages down
• Vast majority do not get a living wage
• Live in uncivilized conditions – cannot cope with health crisis
• Won’t get much work in cities either – will be in a limbo
Road Ahead

• Relook at the development paradigm
• Problem is collective and need to strengthen the collectivity – nationally and globally
• Reduce alienation – pay living wage
• UBI not a solution – current cash transfers required
• Reduce the hours of work for full employment
• Technology to be introduced in a socially responsible manner
• Crisis as a challenge to bring about genuine reform
Conclusion: Way Ahead

• Machines, factories and offices exist, but economy stalled
• Poor and unorganized sector producers who have little saving need support and expanded PDS needed
• Were always marginalized and more so now.
• Step up health infrastructure – Otherwise, Breakdown
• Government’s resource position stretched - can only cater to survival – Budget should be reformulated.
• Problems due to uneven development – A rethink about development paradigm required – inequality, trade, openness, environment, travel, education … .
• Presently opposition decimated – what chance of rethink/new ideas.
Annexe: GDP and Budget calculations

- GDP in 2019-20 Rs.204 lakh crore = $2.87 trillion at Rs.71
- April economy at 25% of January level - gradual recovery in a year (optimistic)
- If 29% down then Rs.145 lakh crore ($1.96 trillion)
- Tax collections will fall by much more than this amount
- Tax revenues of Centre and States could fall from 16% of GDP to 12% of reduced GDP of 2020-21.
- From Rs.36 lakh crore ($487 billion) down to Rs.17.4 lakh crore ($235 billion).
- Non-tax revenue will also decline in same proportion
- Deficit rise due to fall in revenue (14.5% of the reduced GDP)
Fiscal deficit for Public Sector was already 10% of expected GDP in 2020-21; would be 15.5% of reduced GDP – if Expenditures are not cut.

Without expenditure compression Fiscal Deficit would be 30%

Increased expenditures COVID-19 related 12.4% of GDP

Already committed 1.5% so increase would be 11%

Resource shortage in budget due to planned deficit + revenue short fall + requirement of survival package (= 22.5 + 20 + 18) = Rs.60 lakh crore, 41.4% of 2020-21 GDP; $810 billion

Decline in demand due to cons., investment and govt cuts 30%

Stimulus of at most 27% if expenditures increased otherwise only 15.5%