Impact of Covid19 induced economic restrictions on some selected sectors of the Indian Economy

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Introduction

The deserted roads, empty public places and locked factories in all the major cities of the world depicts a hard to believe spectre that would have been unimaginable a few months ago. As mankind contemplates about the future within the confines of home, there seems to be a trade-off between saving lives and continuing with life.

The spark of COVID 19 in the most populous country on the face of earth and its subsequent conflagration throughout the continents has only a few precedents in terms of scale and severity. Almost all the major and minor economies are engulfed by its impact. In a scenario where everyone depends upon everyone else, India, just like any other country, is also staring at an uncertain future. To gauge the full impact of Covid19 on the economy, it is better to analyse one sector at a time.

1. Agriculture

Though the rural area has largely escaped the severity of the pandemic in terms of the number of affected cases, and the harvesting of Rabi crops can be undertaken with the locally available infrastructure, but, the challenge lies in logistics and transporting the produce to mandis. Some state governments, Punjab for instance, have increased the number of centres where the produce could be purchased and that too in an intermittent manner so as to ensure that adequate spatial gap can be maintained so as to enable farmers realise the fair price. The agricultural labour is highly mobile in India. They migrate to cities when the requirement of labour is less in the countryside, but they do return once the harvesting season begins. With the movement of people being highly restricted, in some states, these migrant labours may have not been able to return to their native place, thereby exacerbating the complications for the sector. On the other hand, some states could be having surplus labour. The recent communication (April 15, 2020) by the ministry of Rural Development in initiating some activities in augmenting rural infrastructure under existing rural job guarantee programs can absorb the surplus labours in those labour surplus states. If the country is blessed with adequate rainfall in 2020, then the negative impact of Covid 19 on agricultural sector could be managed with initiatives such as direct fund transfers, postponement of loan repayments or interest subvention. With a contribution of around 15.26% in the Gross
Value Added for FY 2016 – 17 and 43% absorption of the total workforce in the country the sector can withstand the impact of Covid 19. Of course, it comes with a caveat that the contagion will not relapse in a major scale in the months to come.

2. **Industries**

Even before the arrival of the 2019 stain of coronavirus, the manufacturing sector of India never really realised half of its potential – as it contributes less than 20 percent of the total gross value added – despite having a strong workforce, natural endowments in terms of minerals and ores, vast coastlines and political stability since independence. The political leadership for a long time after independence actually pulverised the sector through archaic laws, restricting foreign collaboration and resorting to political favouritism. A gradual shift in policy making in the last three decades did inject competitiveness into the sector and manufacturing looked for a take-off. Already burdened with lack of credit worthiness in recent years, the Covid 19 has only aggravated the woes.

2.1 **Automobile**

The automobile sector, with a very large fixed cost component and coupled with an already falling demand due to a host of issues, is more likely to be heading towards an economic ventilator due to the emergence of the Wuhan virus. The units of vehicles sold in India across all categories for FY 2020 as published by the Society of Indian Automobile Manufacturers (SIAM), the apex body of all automobile manufacturers revealed a dismal picture in comparison to the previous year. All the categories, be it commercial vehicles or two wheelers, witnessed negative growth rate. Due to the discretionary nature of demand for automobiles and its associated products in addition to their high-income elasticity, a post Covid 19 scenario does not inspire confidence. Hence, it is the manufacturing sector that needs most of the support from the government so as to enable them to carry on by at least realising their variable costs. Serious fiscal support in the form of drastic reduction of tax, both direct as well as indirect, is the need of the hour to protect the entire industrial sector of the economy. Moratorium on term loans as announced by the monetary authority should provide some relief as far as addressing a part of the fixed cost in terms of loan repayment commitment of automobile producers. Perhaps, this is a God sent opportunity to initiate long-standing pending reforms in the form of labour reforms. The twin problems of high fixed cost component and rigidity in altering workforce can be dealt with a single reform. One silver lining in the entire morbid forecast is that the world-renowned companies who relied only on China for manufacturing their products might be searching for alternative destinations. Even if it happens, the benefits will be cornered by countries that provide better infrastructure in terms of logistics and supply chain, trained workforce, geographical advantages, stability in policies, benign tax regime and of course ease in compliances.
2.2 Construction

Another sub sector, which needs immediate attention is the construction sector. With a contribution of around 8% in the GVA and a projected absorption of 67 million of employable workforce by 2022 in the country (if real estate is clubbed together with construction), this industry can go a long way to preserve the aggregate demand for basic consumer goods. After all, this sector trail only to agriculture as far as employment generation is concerned. If activity fails to resume in the sector, then the contagion will force the workers to head towards their respective home states. Unlike farmers, workers of the construction sector are difficult to be identified due to the seasonal nature of the activity and faulty registration process. The Building and Other Construction Workers Act, 1996 tried to address the safety, hygiene, accommodation, etc. of construction workers, but identification and registration of such workers on the ground remained a great challenge. Thus, any targeted transfer of monetary benefits towards the sector may not reach the actual workers.

2.3 Consumer Electronics and Mobile Handset

The consumer electronics industry, especially the mobile phone industry saw some good news before the restrictions on movement of people set in. The Indian mobile handset industry, which recently earned the tag of second largest manufacturer in the world is now estimating a Rs. 15000 Cr. revenue loss if production is halted for the month of April 2020. According to a study conducted by IIM – B, it was estimated that by 96% percent of the entire demand (Figure 2) for mobile in the country would be met by domestic production by 2020. The Government had already cleared an incentive program linked to the scale of production for the mobile handset manufacturers before the lockdown, the benefit of which would be reaped once normal business activity resumes and the pent up demand gets released. India Cellular & Electronics Association, the apex body for mobile and electronics manufacturing units is sanguine over the Rs. 41000 Cr. incentive linked to production of handsets and development of clusters for electronic items. The graph (figure 2), published by
2.4 Healthcare

The only sector that has shown resilience as far as the stock market outperformance in recent times is concerned, possibly because of stability in revenue generation during the Wuhan virus crisis, is the health care sector. The pharmaceutical sector is on a solid foundation due to the rising demand for unbranded medicines and because of its capability to augment production of those drugs that has recently been out of patent protection. According to Pharmaceutical Export Promotion Council of India, Indian pharmaceutical exports in FY 2020 is expected to touch $22 billion. The Nifty Pharma index has delivered a return of + 16.7% against – 22% for multi sector Nifty 50 in the last one year. As many as four Indian drug manufacturers have obtained clearance for their production facilities from the USFDA in April 2020, which in normal times would have been unimaginable. One can safely conclude that the investors are feeling safer under the umbrella of pharma sector rather than the broader multi sectored Nifty 50.

3. Services

With an overwhelming share of 53.2 % share of India’s GVA, the services sector is highly diverse and undoubtedly the largest component of the economy. Within the sector: trade, repair, hotel and restaurant (12.19%), transport, warehouse, media and communication (7%) and financial, real estate and professional services (21%) accounts for a considerable chunk. New norms regarding spatial gap and general risk aversion among consumers will definitely create new challenges with regard to increasing cost and limiting the ability to achieve economies of scale. Take, for instance, a restaurant that will have to reduce the number of tables or airlines that may need to reduce the number of seats to meet the norms for social distancing. A post Covid era may also witness lesser frequency of trains from stations and lesser number of flights allowed from an airport to prevent crowding. Tourism could well be the worst sector as it falls in the category of discretionary spending and well as general risk aversion among the travellers. As per the forecast
of UNWTO (United Nations World Tourism Organization) international tourism can decline by 20 – 30 percent in the current year. The forecast is based upon the experience gathered during the SARS outbreak of 2003 and the financial crisis of 2008 – 09. The fallout of the current crisis could be of a much bigger magnitude and hence the impact much worse than what has been predicted. Coming back to restaurants including cloud kitchen which provide direct employment to 7.3 million people, initiating a contactless delivery would increase costs by at least by 4 percent. According to National Restaurant Association of India, contact delivery includes adopting practices such as use of thermal guns to check temperatures of kitchen staff and delivery personnel, use of protective materials by staff, disinfecting the entire facility more frequently and delivery of the food item at a designated spot. Increased costs in addition to a squeeze in demand may force 2 out of every 5 food and beverage outlet to close down.

![Figure 3: 2020 Forecast – International Tourist Arrival, World (in millions)](image-url)

![Figure 4: 2020 Forecast – International Tourist Arrival, World (% Change)](image-url)
3.1 Financial Services

Financial services, which was already battered due aggressive advances without due diligence (IL&FS, DHFL) and corporate governance issues (YES Bank) woke up to another rude shock when Franklin Templeton a leading mutual fund AMC suddenly announced closure of six debt oriented schemes during the virus outbreak. These schemes were classified under short – term debt oriented category and were considered the safest investments due to their short tenure, exactly the schemes a risk averse investor wished for to park funds. The projected fall in future earnings for companies and a general cloud of uncertainty in equity market forced many investors to seek refuge in debt schemes with short maturity. The mutual fund AMC in question bought illiquid debt securities of companies that enjoyed less than comfortable credit worthiness to offer better return than its counterparts. The news of closure of six debt schemes evoked both trepidation and suspicion among the investor community. The development forced the RBI to open a special window of Rs. 50000 Cr. earmarked for the mutual fund industry. While the move has allayed the fears for the time being, sceptics point towards the efficacy of such measures where the portfolio managers are at fault. It also brings back the focus on disclosures to be made in the fact sheet of mutual fund in a more conspicuous manner rather than mentioning in small sized font. The virus contagion and the temporary closure of the economy led to a lower revenue realisation by the businesses and consequently there was a widespread fear of failure in debt servicing emanating from them. Therefore, the malaise is embedded in the real economy. Hence, the support measures should also be directed more towards the real economy.

3.2 Information Technology

Not all sectors, however, are so intertwined by the current circumstances that they cannot device strategies to bypass the requirement of avoiding physical proximity. TCS, for instance, has promised a major overhaul of its existing business configuration by eliminating the boundaries of workspace. The new model envisages to enable about three quarters of its personnel to work from remote locations, thus, bypassing the bottleneck of lockdown and enhancing the safety of its employees. The current situation will only increase the intensity of corporates to adopt automation and artificial intelligence in their workplace. If the new model adopted by TCS proves successful, then it can prevent a decline in its revenue and grab additional market share due to the first mover advantage. That other IT companies will follow the same path is not a matter of conjecture anymore.

Crude Oil: In Slippery Path

The crude oil price reflects the state of geopolitics and the condition of the global economy. The data for the last five years (before the onset of Wuhan virus) for WTI (West Texas Intermediate) show a benign pricing for the oil consuming countries barring the second half of 2018. A steady price augurs well for both the producers and consumers as it offers predictability. But, this stability was greatly disturbed, so much so that the WTI price started to chart a negative territory on 29th April 2020, effectively meaning that the buyers were obtaining crude oil as well as dollars from sellers, a situation that defies logic. The sellers resorted to this extreme behaviour because the storage space was running out. Although the price of Indian basket of Brent crude did not go down below zero, still it tested a price of around $19 a barrel. Can the abnormally low level of
crude price do any good for Indian economy? On the face of it, yes, because keeping the currency rate constant every fall of a dollar in crude oil price leads to a saving of around Rs. 3000 Cr. for India.

Figure 5: WTI Crude Price (Jan 27th, 2020 – April 29th, 2020) Source: Trading Economics

According to one estimate, published in a leading business newspaper, India’s crude import payment for 2020 – 2021 could fall below the level of $ 64 billion that was seen in 2015 – 2016. That it will lead to tangible benefits in India’s current account, currency rate and inflation are obvious. However, just like many other sectors, the COVID contagion has only magnified the problems in this sector was already going through because of a price war between the two leading producers, Saudi Arabia and Russia. The Saudis tried to outwit both Russia and the US by keeping the price deliberately low for long term benefit by driving the other two out of the market. If the crude oil price remains where it is, i.e. at around $20 a barrel, then, many US oil producing companies will go out of business and the Russians will barely break even triggering bankruptcies and a fresh round of financial crisis. This situation is far more threatening for Indian economy than saving some amount in its import bill.

Figure 6: Cost of Production of Major Crude Oil Producing Countries (Source: Knoema)
Conclusion

With almost all economic activities stalled for a month or two, the Covid 19 contagion will leave a deep scar across industries in India, except a few. Agriculture as the largest employment generating sector may have escaped a big blow largely because the Rabi crops were either already harvested or on the verge of completion of harvesting before the large scale spread of the virus began. Another factor that might have helped the sector is that the virus spread has largely been limited to big cities. The biggest challenge before the government is to safely allow the farmers to offload their produce at a fair price. Both automobile and construction sector are more likely face most of the brunt because of their inherent weakness before the crisis, limitations in labour mobility and practical difficulty in adapting to safety norms. The problem is compounded due to the ongoing crisis in the microfinance industry. Some sectors like electronics and pharmaceuticals may show more resilience and may even show positive growth by the end of FY 2021. The former may get a boost because of the release of pent up demand once the lockdown is over and because of the incentive package declared before the onset of the crisis. And lastly, a stable crude oil price is more beneficial as compared to an unrealistic low price to keep the producers afloat. Any large-scale bankruptcies of crude oil producing companies either within or outside the OPEC can trigger a fresh crisis. In a situation which is continually evolving, and prognosis is difficult India can consider itself lucky if it can endure the crisis with a 1 – 2 percent decline in its GDP in FY 21.

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