



Atul Loke/The New York Times

JUNE UPDATE
Quarterly Review of the Economy, 2020-21:Q1
in Coronavirus times

Sudipto Mundle, Bornali Bhandari, N R Bhanumurthy
with Shankar Acharya and Pronab Sen
in conversation with
Shekhar Shah

Webinar, Thursday, June 25, 2020, 6:30 pm IST

QRE Team

Team Members

Sudipto Mundle, Bornali Bhandari, NR Bhanumurthy (NIPFP), Anil K Sharma, Pallavi Choudhuri, Rudrani Bhattacharya (NIPFP), Saurabh Bandyopadhyay, Prerna Prabhakar, Sanjib Pohit, Poonam Munjal, Devender Pratap and Ajaya K Sahu

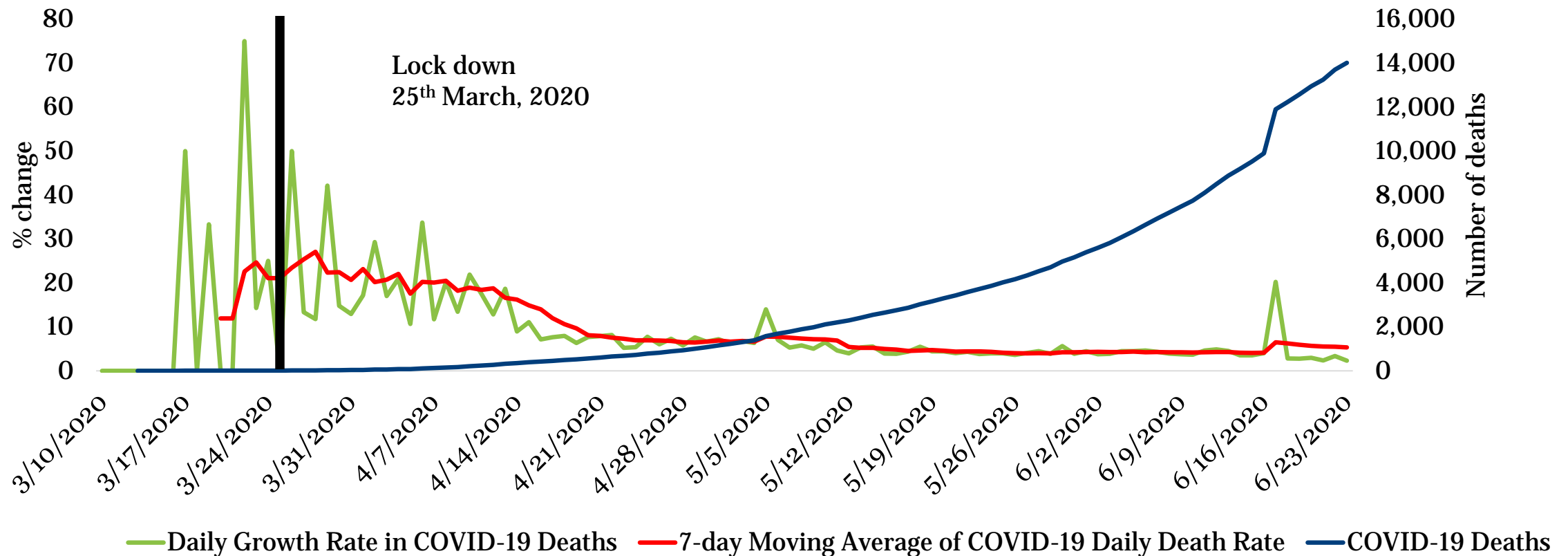
Organisational Support

Sudesh Bala, Praveen Sachdeva, Anupma Mehta, Shilpi Tripathi, Khushvinder Kaur and Sangita Chaudhary

Coronavirus Pandemic

Growth of Daily COVID-19 deaths

Number of COVID-19 Deaths, Growth of Daily COVID-19 Deaths and 7-Day Moving Average of the Daily Growth Rate, 10 March 2020 to 23 June 2020



Outline

I. Stimulus Policy Simulations

II. Performance of the Real Economy and Trade

A. Real Sector Trends

B. Business Sentiments

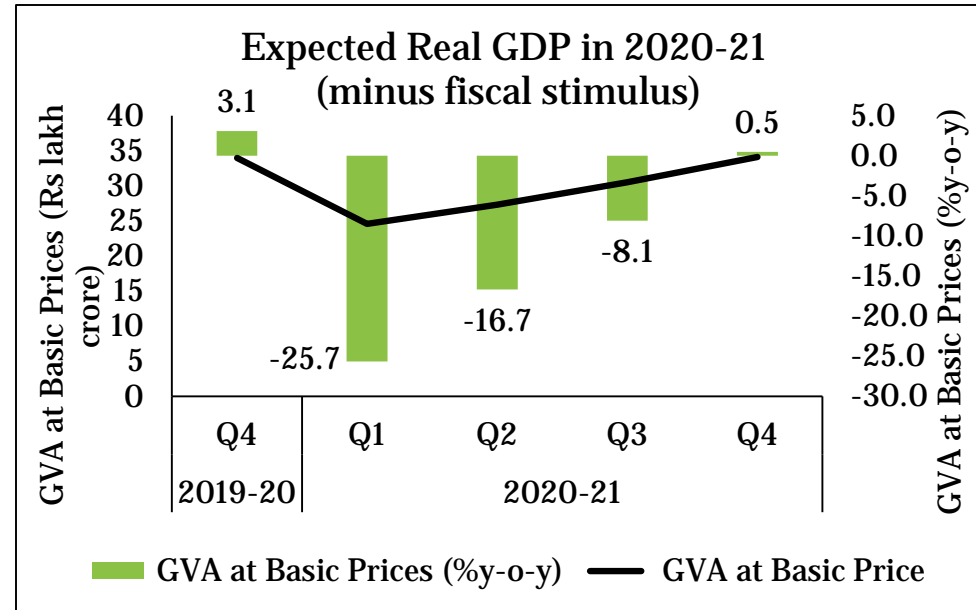
C. Price Trends

III. Macroeconomic Policies

A. Fiscal Outlook

B. Monetary Policy Challenges

Policy Simulations - I



Assumptions about Disruptions in GVA and Key Sectors (%y-o-y)							
Sector	2019-20:Q4*	2020-21:Q1	2020-21:Q2	2020-21:Q3	2020-21:Q4	2019-20*	2020-21
Agriculture	5.9	3.0	3.0	3.0	3.0	4.0	3.0
Industry	(-)0.6	(-)54.2	(-)36.0	(-)18.0	0	0.9	(-)27.1
Services	4.4	(-)16.3	(-)10.9	(-)5.4	0	5.6	(-)8.2
GVA	3.1	(-)25.7	(-)16.7	(-)8.1	0.5	3.9	(-)12.4

Policy Simulations -II

- Initial assumption is that negative growth is assumed to continue till Q3, then recover modestly to 0.5% in Q4
- For the whole year 2020-21 GDP growth is assumed to be (-)12.4%
- This assumes no policy stimulus (either monetary or fiscal)
- What would be the impact of monetary and fiscal policies (including Atmanirbhar Bharat Package) that have been initiated?
- A policy simulation model has been used to assess the impact.
- Simulations used to assess the overall impact with no supply constraints (base case), followed by scenarios with varying degrees of supply constraint.

Some Simulation Results - I

Five scenarios are:

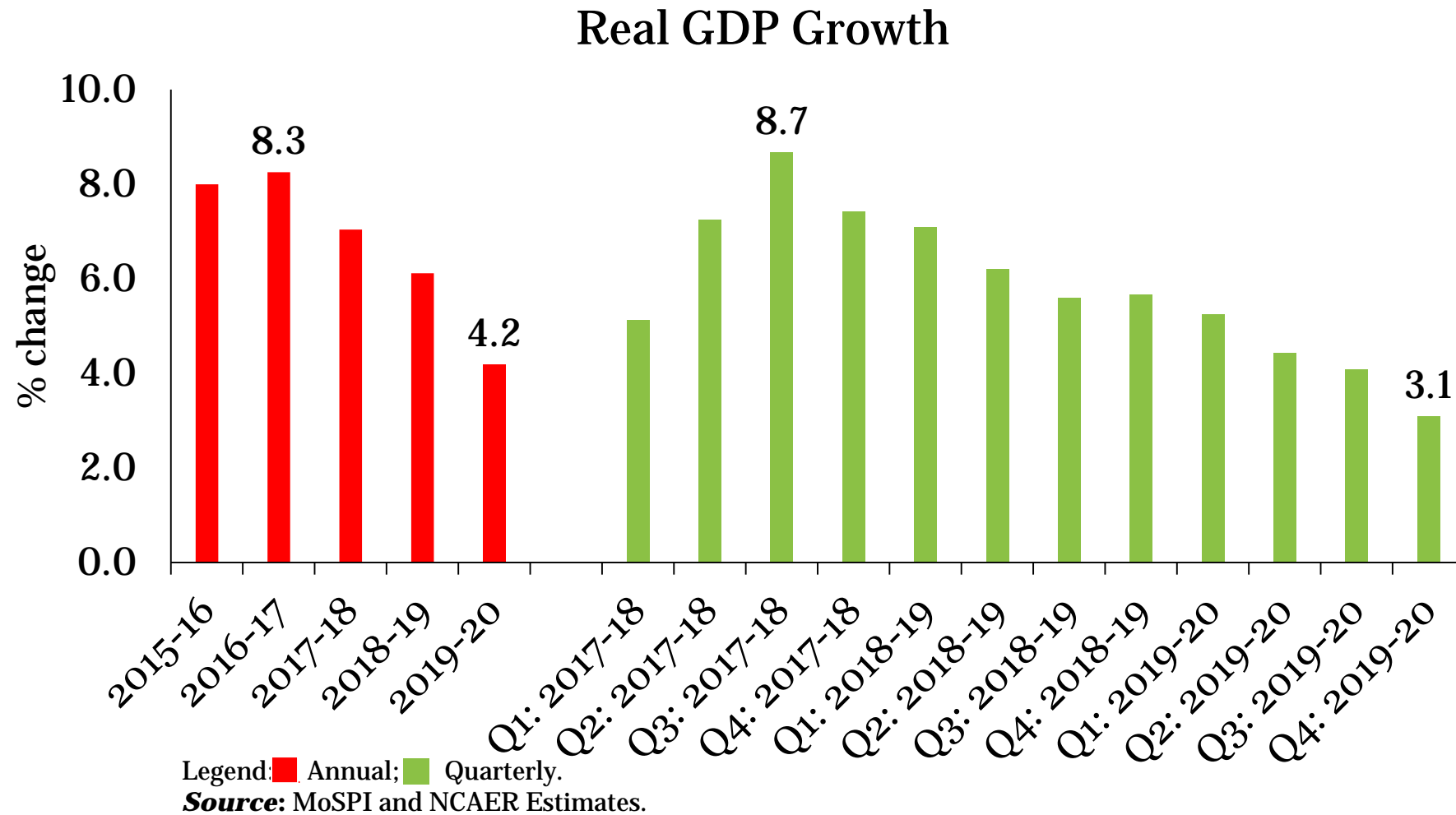
- **Base Case:** Incorporates monetary and fiscal stimulus measures (includes post-Budget additional government borrowing of Rs 4.2 trillion as well as additional States' borrowing of up to 2% of GSDP)
- **Scenarios 1 to 4:** Introduce supply constraint by fixing the GVA growth exogenously at 0 per cent, (-) 2 per cent, (-) 5 per cent and (-) 10 per cent.

Scenarios	GDP growth (%)	Inflation (%)	Fiscal Deficit (as % of GDP)	CAD (as % of GDP)
Base case	1.33	5.46	7.6	2.8
Scenario-1	0	6.03	7.8	2.6
Scenario-2	(-)2.0	6.44	7.8	2.3
Scenario-3	(-)5.0	6.71	7.6	1.8
Scenario-4	(-)10.0	7.78	7.4	1.1

Some Simulation Results - II

- If fiscal & monetary policies are fully implemented without supply constraints, GDP growth could amount to 1.3% in 2020-21
- Economy at present is subject to severe supply constraints due to increased mortality of businesses (MSMEs), reverse migration and large scale disruption of supply chains.
- The five scenarios taken together suggest inflation would vary between 6 and 8%, combined fiscal deficit would be contained at under 8% and current account deficit would vary between 1% and 3% of GDP.
- Stronger the supply constraint higher would be the inflation rate. It is likely to go above the RBI's tolerance band. This is the most plausible outcome given the prevailing supply constraints.

Sustained decline in GDP Growth since Q3: 2017-18 before coronavirus crisis



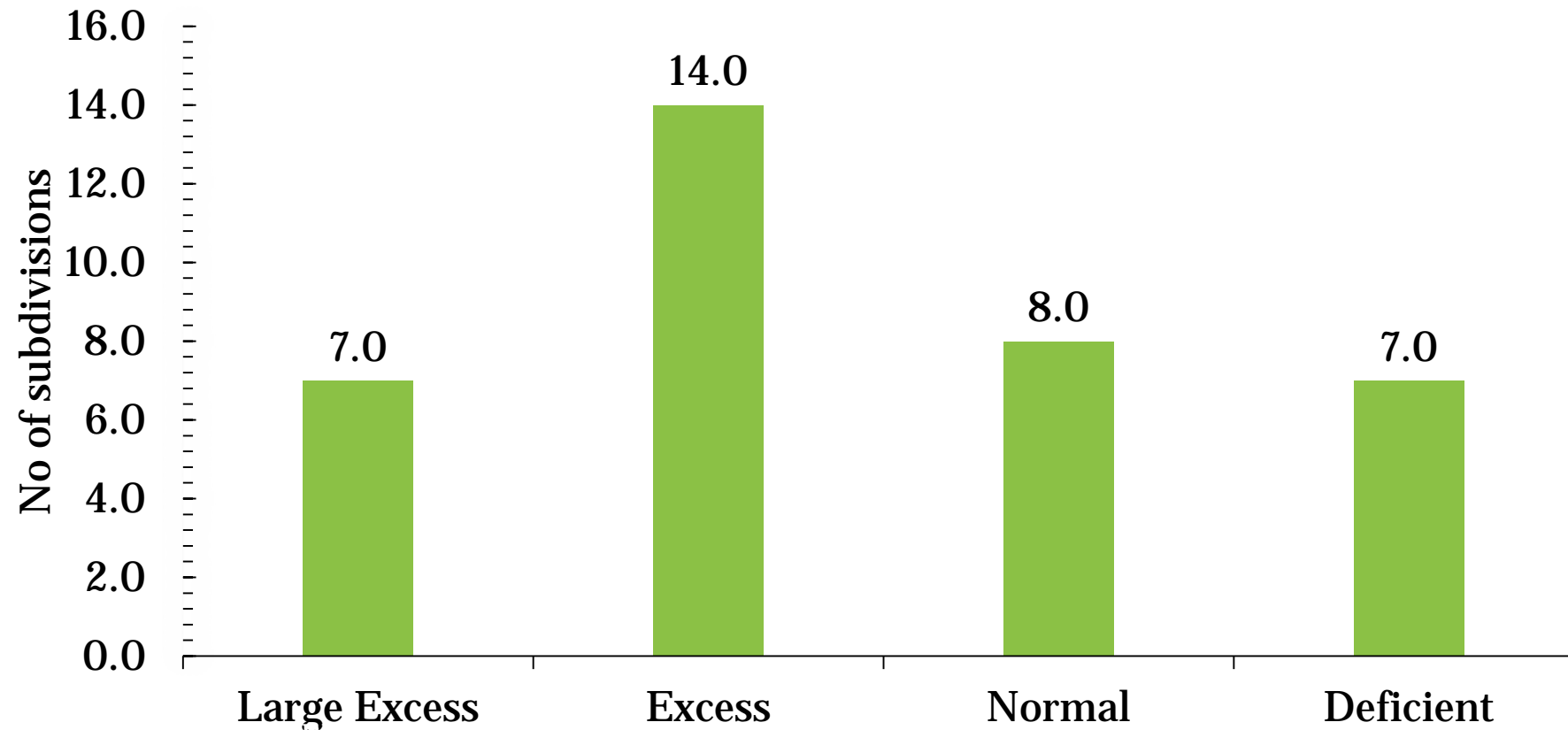
Coronavirus Shock assessment

Table 1: Assumptions of Sector Disruptions in Q1 2020-21 GVA

<i>Sector</i>	<i>Sector</i>	<i>Assumptions of Disruptions in 2020-21:Q1 on a y-o-y basis (%)</i>	<i>GVA in 2019-20:Q1 (Rs crore)</i>	<i>GVA in 2020-21:Q1 (Rs crore)</i>
Agriculture	Agriculture, forestry and fishing	3	4,39,843	4,53,038.3
Industry	Total	(-)54.3	10,16,199	4,64,807.8
	Mining and quarrying	0	92,807	92,807
	Manufacturing	(-)62.4	5,78,936	2,17,892.8
	Electricity, gas, water supply & other utility services	-40	81,628	48,976.8
	Construction	-60	2,62,828	1,05,131.2
Services	Total	(-)16.3	18,51,665	1,554,136
	Trade, hotels, transport, communication and services related to broadcasting	(-)62.4	6,30,860	2,37,518.8
	Financial, real estate & professional services	6.7	8,03,322	8,57,385.6
	Public administration, defence and other services	10	4,17,483	4,59,231.3
Total GVA	TOTAL GVA at basic prices	(-)25.7	3,307,707	24,71,982

Forecast of normal South-west monsoon augurs well for Indian agriculture

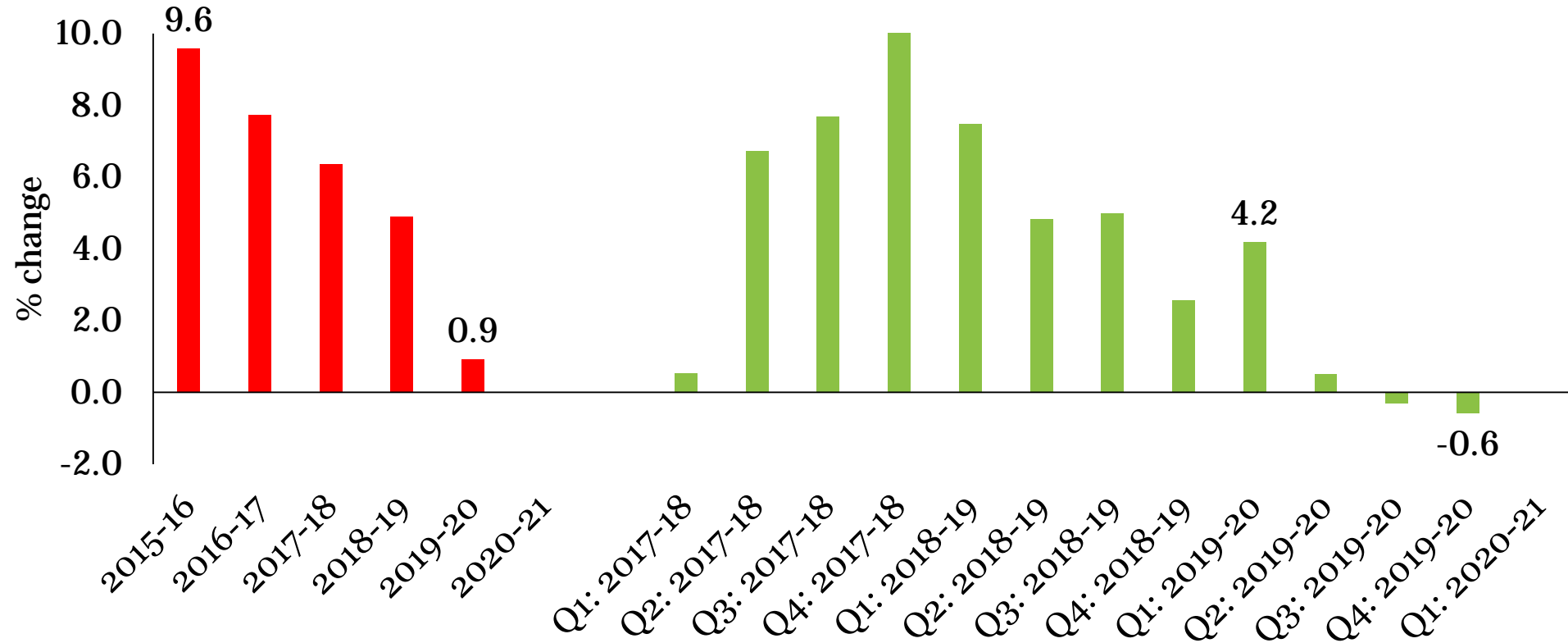
Sub-division wise Rainfall Distribution
(June 1, 2020 to 22 June, 2020)



Source: IMD

Steep Decline in Industrial Growth since Q4: 2017-18

Growth in Industry GVA



● **Estimated decline of (-)54.2% in Q1: 2020-21**

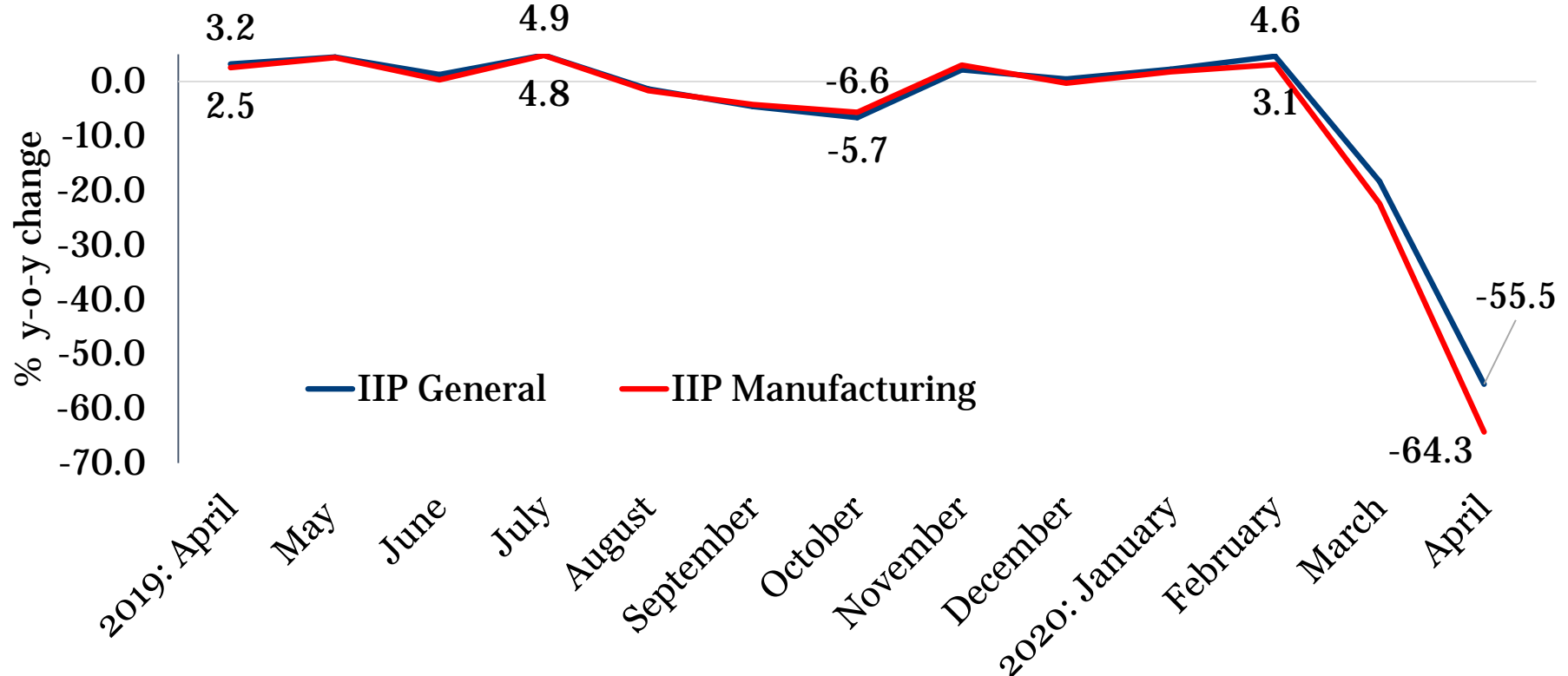
Legend: ■ Annual ■ Quarterly.

Source: MoSPI and NCAER Estimates.



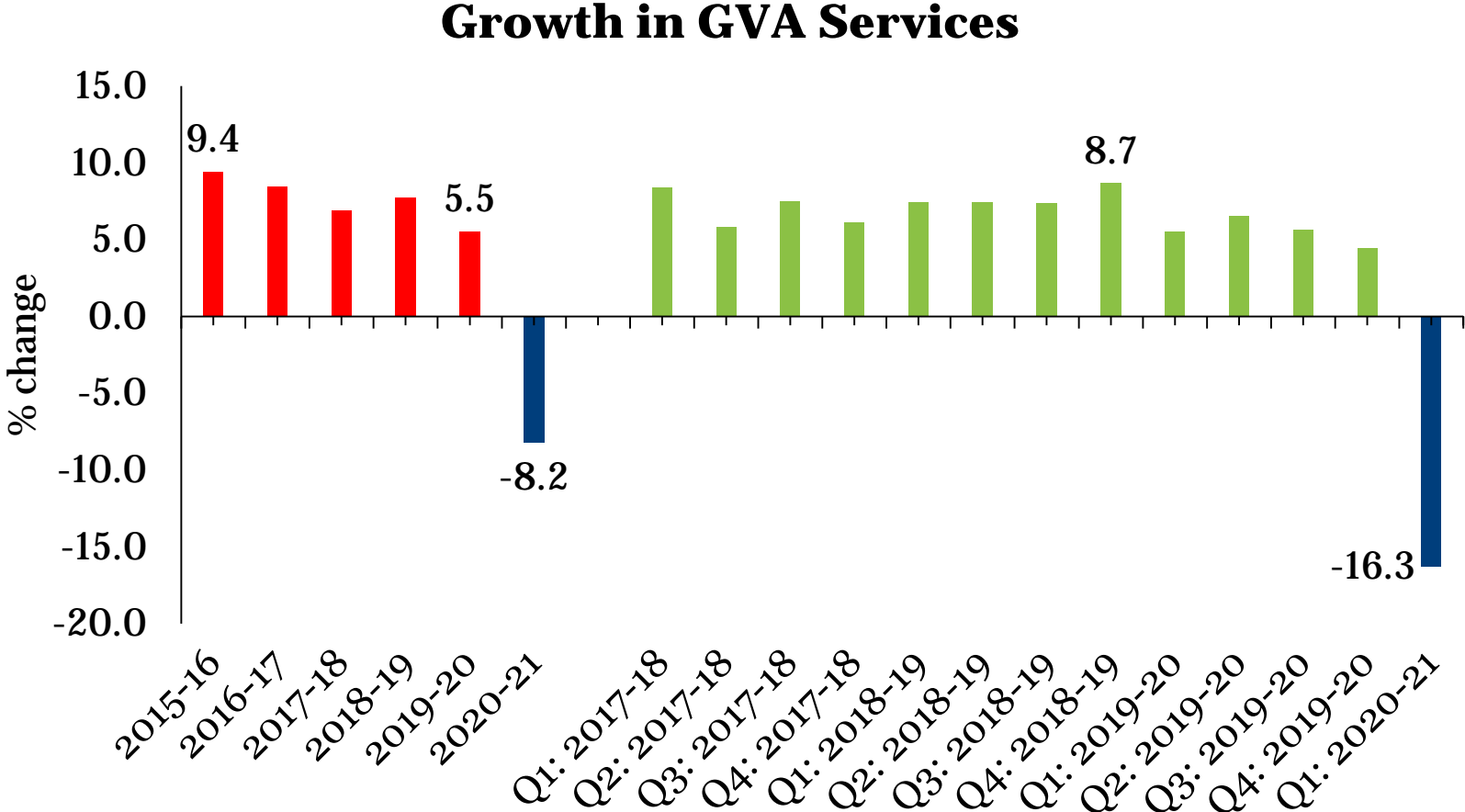
IIP confirms continuing industrial slowdown

IIP General and IIP Manufacturing (%y-o-y)



Source: MoSPI

Sharp decline in services growth projected for 2020-21

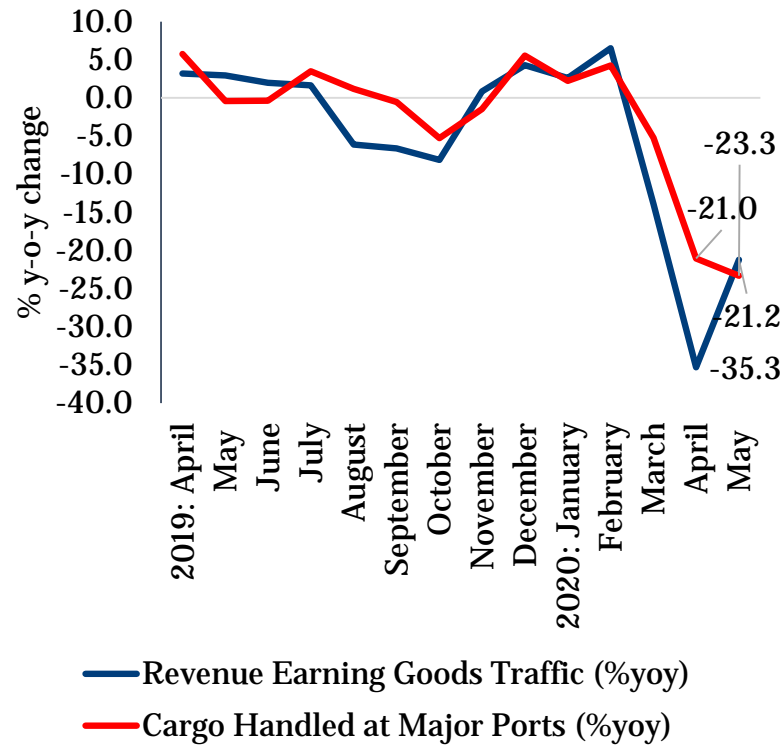


Legend: ■ Annual; ■ Quarterly and ■ Projections.

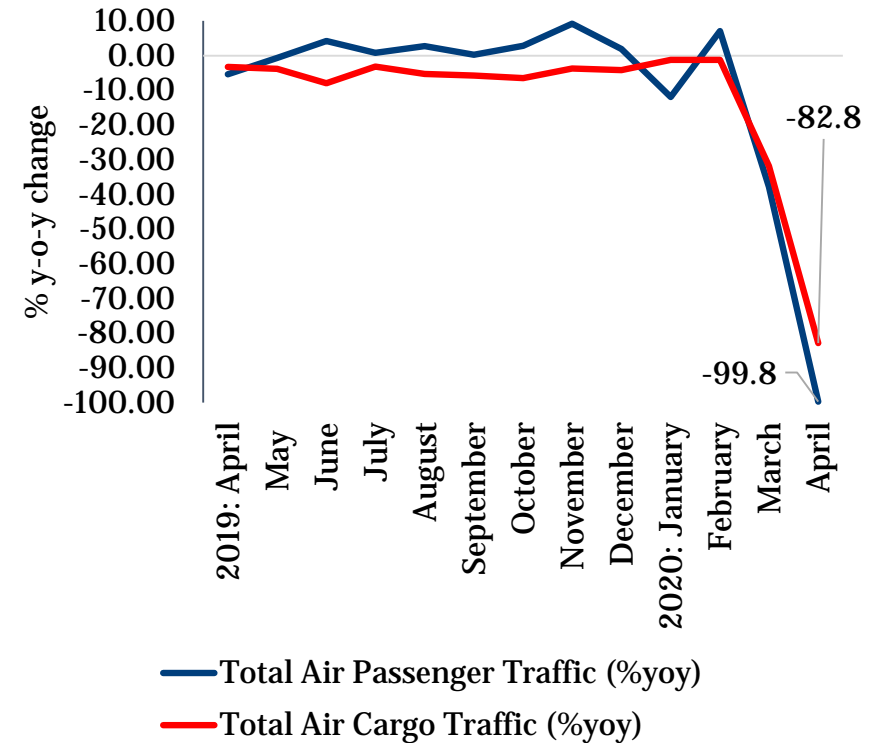
Source: MoSPI and NCAER Estimates

Cargo and passenger traffic have declined sharply

Revenue Earning Goods Traffic and Cargo Handled at Major Ports



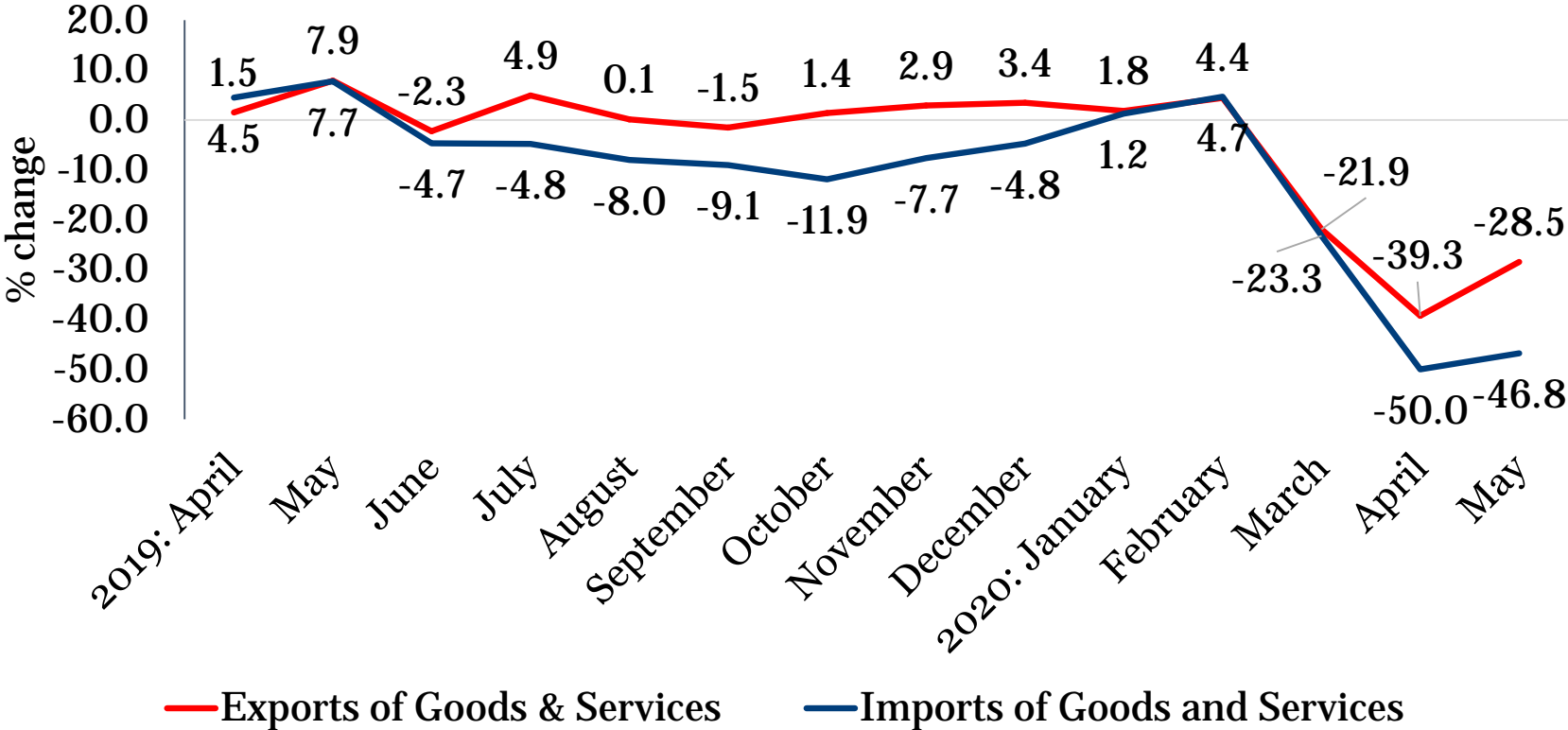
Air Passenger and Cargo Traffic



Source: CMIE and Airports Authority of India.

Exports and imports growth declining since Q2: 2018-19, now negative

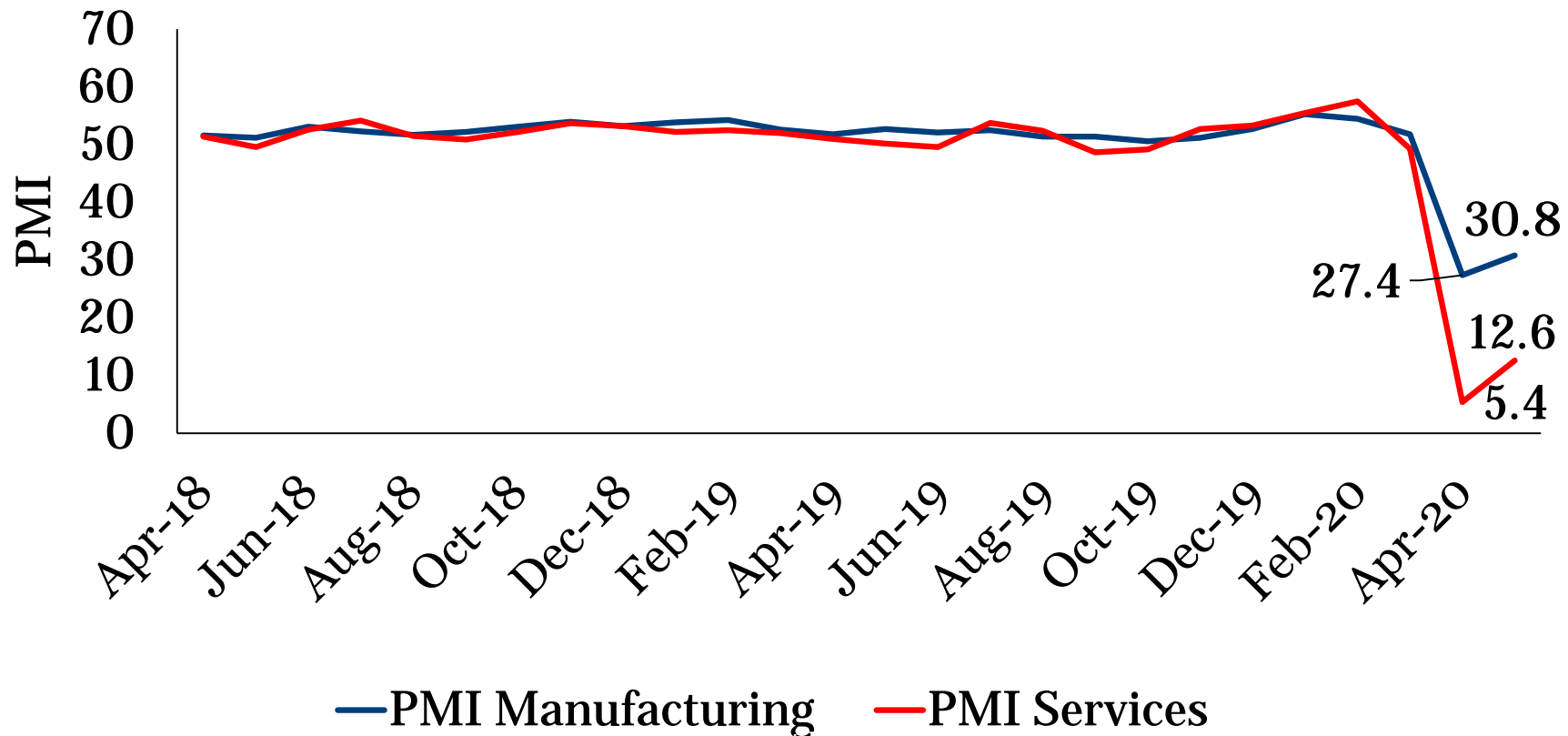
**Growth of Exports and Imports of Goods & Services
(US\$ terms, %y-o-y)**



Source: Ministry of Commerce and RBI.

Nikkei PMI indicate continued contraction in April and May 2020

Indices April 2018 to May 2020

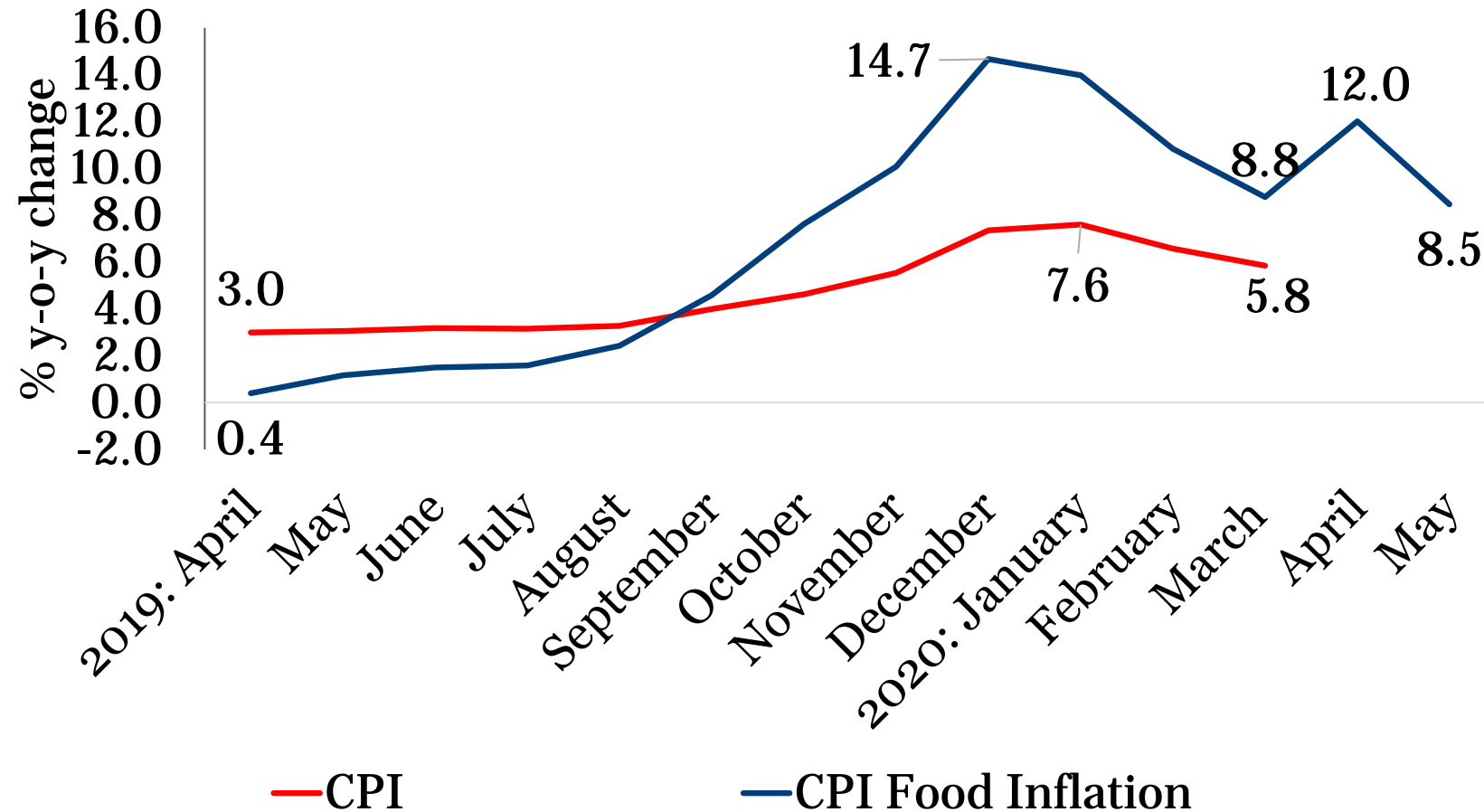


Source: Nikkei PMI



Inflation trends

CPI and CPI Food Inflation (excluding meat & fish)



Decomposition of the Atmanirbhar Bharat (AB) Stimulus Package

Item	Amount (Rs trillion)	GDP (%)	Remarks
Total (Stimulus component only)	18.7	9.3	AB includes reforms, etc. + fiscal & monetary/credit components, only latter included here as stimulus
RBI liquidity injection	8.0	4.0	Undertaken prior to 13 May, 2020. Mainly adding to M3
AB credit guarantee measures	8.1	4.1	Implementation contingent on financial institutional decisions. Will add to M3
Fiscal component	2.6	1.3	Will add to fiscal deficit
Contingent Liability	0.9	0.5	No stimulus impact. Not included in Rs 18.7 trillion.

Fiscal Stimulus Budget plus Post-Budget

Item	GDP (%)
Central Government Budget Deficit	3.5
Post-Budget additional borrowing	2.1
AB fiscal component	1.3
States' Budget	2.8
Additional borrowing headroom for states	2.0
Total	11.7

- The 11.7% of GDP total excludes extra budgetary resources such as 0.9% of GDP in the Central budget and any State Government off-budget borrowing. So total Public Sector Borrowing Requirement could be around 13% or more.
- This is a very strong fiscal stimulus, coming together with RBI liquidity injection plus additional credit guarantees (especially for MSMEs) adding up to over 8% of GDP on the monetary side
- Impact of such strong demand stimulation will depend on strength of supply response

Impact of Fiscal & Monetary Stimulus

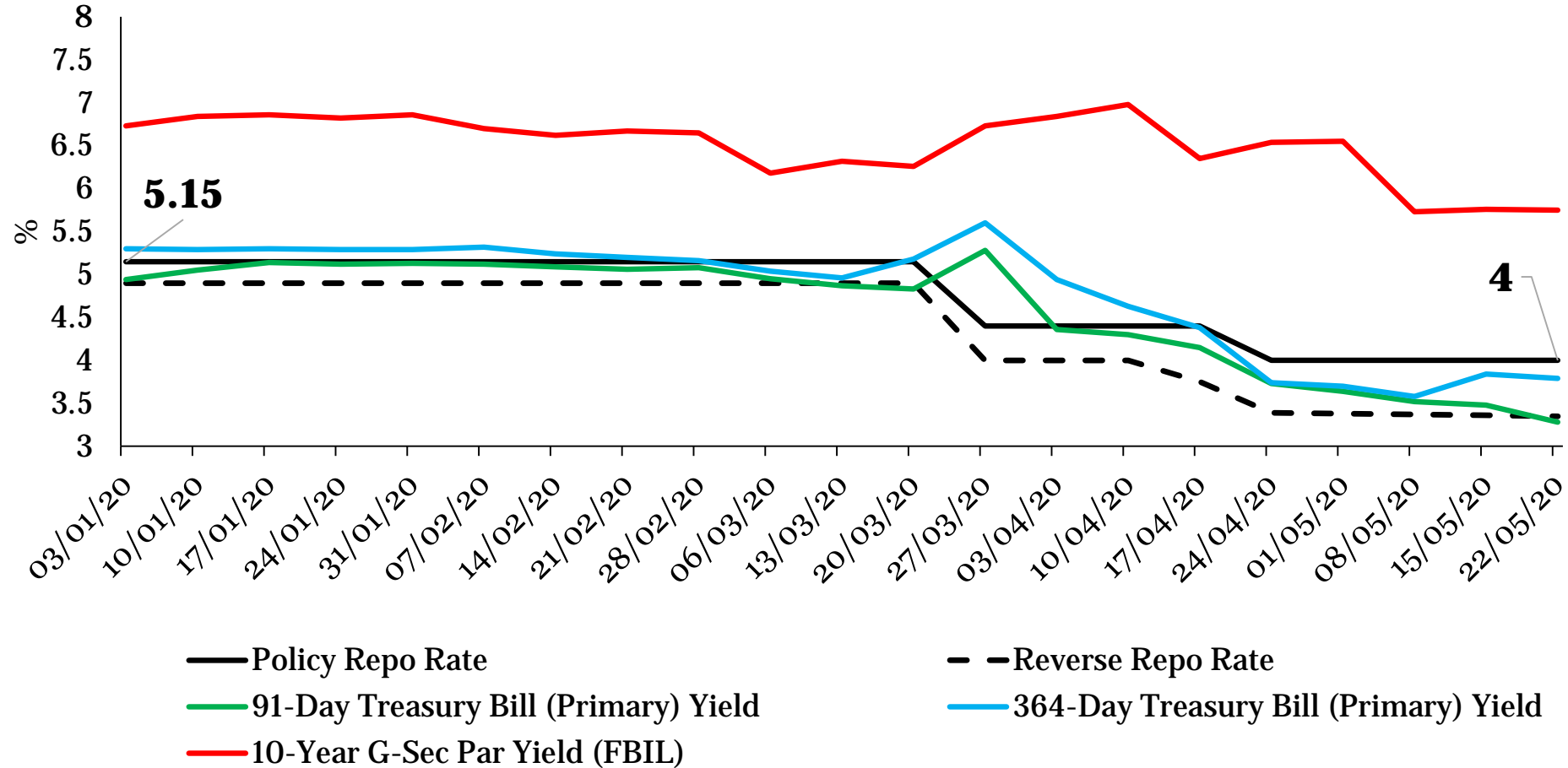
Scenarios	GDP growth (%)	Inflation (%)	Fiscal Deficit (as % of GDP)	CAD (as % of GDP)
Counterfactual Scenario	(-) 12.4	4.5	6.4	1.4
Base case	1.3	5.5	7.6	2.8
Scenario-1	0	6.03	7.8	2.6
Scenario-2	(-)2.0	6.44	7.8	2.3
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Main takeaways from these scenarios:

- The stimulus measures can drive a strong recovery in the absence of supply constraints. However, strong supply constraints are likely to be binding.
- Inflation, fiscal deficit and current account deficit may be somewhat elevated in some scenarios but not alarming
- A sudden acceleration in portfolio capital flight could be de-stabilising. This risk is not factored into the simulations.

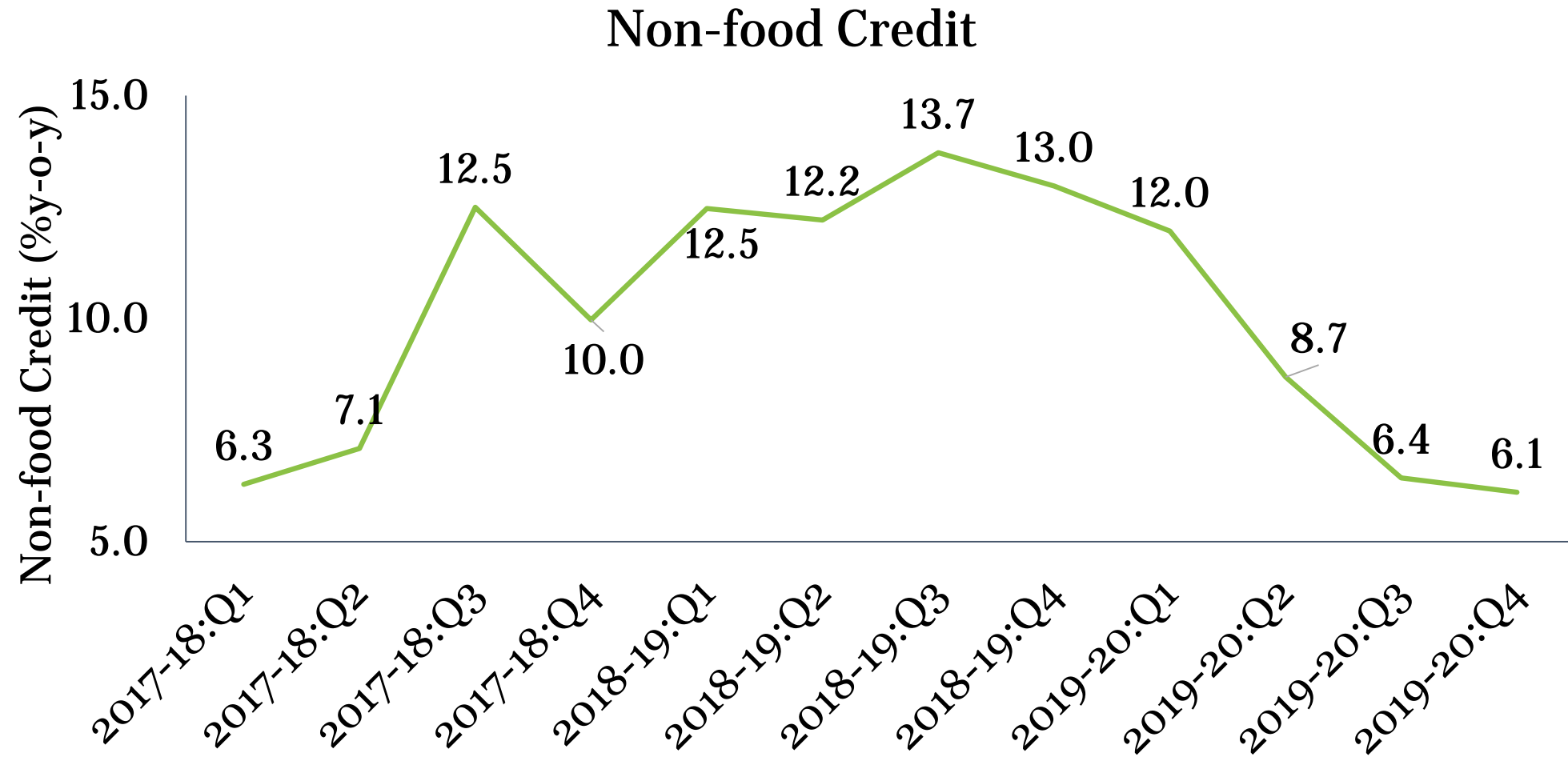
Weak Transmission

Rates and Yields, % (January to May 2020)



Source: RBI

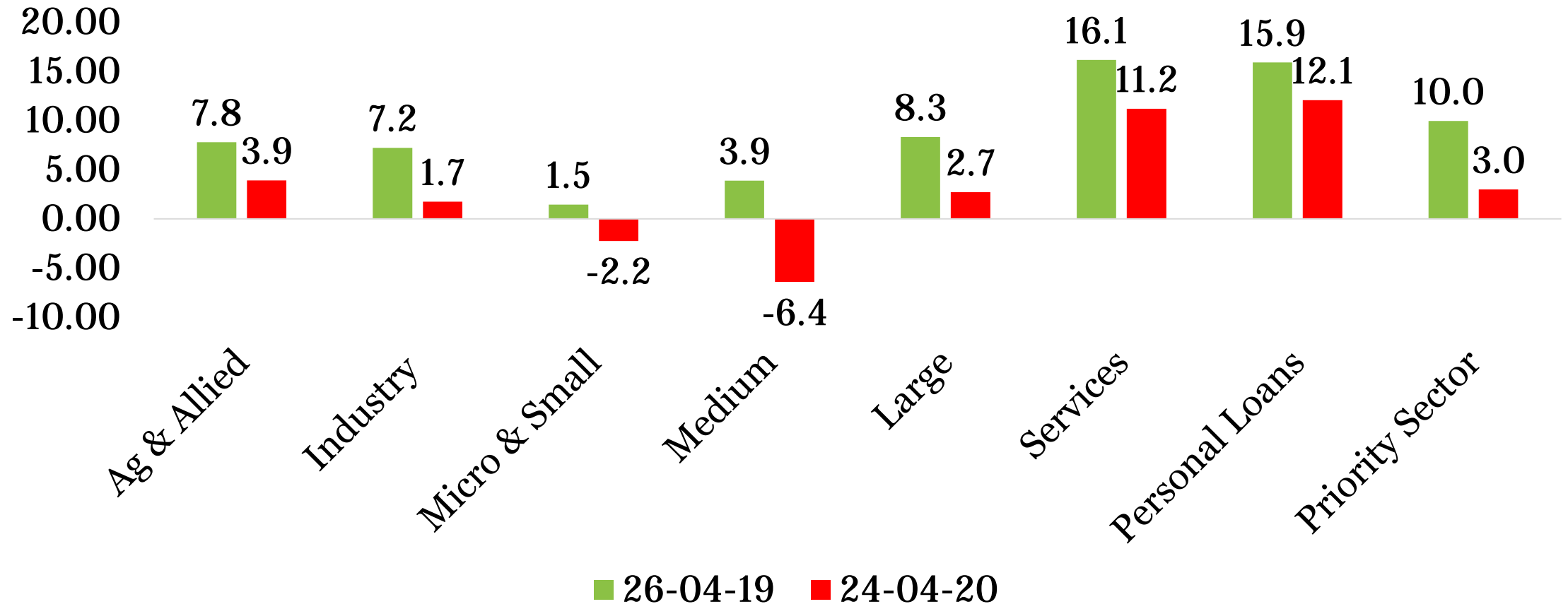
Non-food credit growth has declined sharply since Q3: 2018-19



Source: RBI

Credit growth has declined further in 2020

Growth Rate of Bank Credit by Sectors (% , y-o-y)



Source: RBI

Rising Risk Aversion and Stalled Bank lending

- Rising risk aversion against lending to NBFCs due to scams like IL&FS & coronavirus crisis
 - Targeted Long Term Repo Operations (TLTRO 2) of ₹25,000 crore, intended for directing credit to NBFCs remained only half subscribed.
 - But NBFCs are the main source of credit for MSMEs.
- Similar rising risk aversion in lending to MSMEs.
- Such risk aversion likely to increase under Covid-19 crisis
 - MSME borrowers also averse to borrowing under present conditions
 - Credit flow to MSMEs has virtually dried up
 - Need credit guarantees or partial credit risk guarantees
- Atmanirbhar Bharat package (13 May 2020) include these provisions
 - Government credit guarantee for MSMEs
 - RBI Partial credit guarantee for NBFCs.

Challenge of Massive Government Borrowing

- Total government borrowing programme of well over ₹ 17 trillion (8.8-10.8% of GDP).
 - Announced Central government borrowing programme of 6% of GDP, including ₹1.3 trillion additional borrowing to finance fiscal component of AB package.
 - This also includes State government borrowing of up to 4.8% of GDP, including recently provided additional headroom of 2% of GDP.
- Government borrowing on such a scale unprecedented in India, not clear if financial system can cope
- Multiple channels need to be used to face this massive demand for sovereign loans
 - Market borrowing with part indirect monetisation in secondary market by RBI.
 - Further liberalisation of 'Ways and Means' advances, subsequently converting them to dated securities.
 - Direct monetisation of residual deficit by RBI, lender of last resort, through private placements
- Finally, it may be necessary to spread this borrowing over two years, 2020-21 & 2021-22 in order to maintain financial stability while reviving the economy.

Thank You!