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SEPTEMBER UPDATE

NCAER's Quarterly Review of the Economy Q2:2020-21 in Coronavirus times

PRESS RELEASE

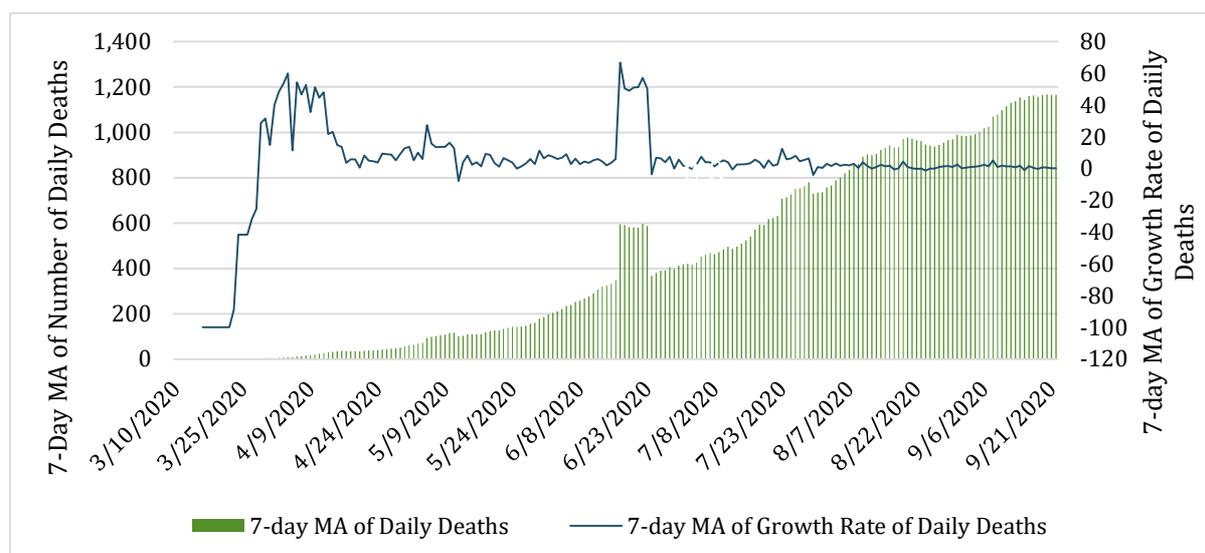
New Delhi (Friday, September 25, 2020): The National Council of Applied Economic Research (NCAER) released its ***Quarterly Review of the Economy (QRE)*** for the second quarter of FY2020-21 at a webinar today. NCAER's latest macroeconomic review was presented by NCAER Distinguished Fellow **Sudipto Mundle**, NCAER Senior Fellow **Bornali Bhandari**, and NIPFP Assistant Professor **Rudrani Bhattacharya**. The webinar also featured **Ashima Goyal**, Professor, IGIDR, and a part-time member of the Prime Minister's Economic Advisory Council and **Pranjul Bhandari**, Chief India Economist at HSBC India, as guest panelists. The webinar was moderated by NCAER Director General **Shekhar Shah**.

The coronavirus pandemic continues to rage in India. The country is now ranked second in the world in the cumulative number of infections¹. India ranks third after the US and Brazil in Covid-19 related deaths, which exceeded 90,000 as of September 22. Although the Covid-19 death rate is still low compared to other countries at 66 per million, this is a matter of little comfort when more than a thousand lives continue to be lost daily (Figure 1). Covid-19 deaths have continued to increase at about 1 percent per day and cumulative deaths at 1.5 per cent through September.

Meanwhile, the economy is in an unprecedented crisis. The NCAER May 2020 QRE and June 2020 QRE Update had assessed that the economy would contract by 26 per cent in Q1. Official estimates have now confirmed that GDP did decline by 24 per cent in Q1 (Table 1.1). At the same time retail inflation has remained elevated at over 6 per cent, i.e., above the Reserve Bank of India (RBI) target inflation band of 2-6 per cent. Elevated inflation along with the steep contraction of the economy requires macroeconomic policy to navigate its way between two competing goals of reviving the economy and containing inflation, a very challenging task especially with the pandemic still raging.

¹ John Hopkins University, Coronavirus Resource Centre website. <https://coronavirus.jhu.edu/map.html>.

Figure 1: 7-day Moving Averages (MA) of Number and Growth (%change) of Daily Deaths March 10, 2020 to September 22, 2020



Source: Authors' computations from Ministry of Health and Family Welfare.

Out of the three sectors, agriculture was the only exception that registered positive growth in Q1: 2020-21. Industry and services sectors recorded double-digit year-on-year (y-o-y) contraction. On the demand-side, barring government final consumption expenditure, all other components, namely private consumption, investment, exports and imports contracted sharply (Table 1).

Table 1: GDP, GVA and its components, Q1: 2020-21(% change y-o-y)

Item	(%y-o-y)	Item	(%y-o-y)
Agriculture	3.4	Private Final Consumption Expenditure	(-) 26.7
Industry	(-) 38.1	Government Final Consumption Expenditure	16.4
Services	(-) 20.6	Gross Fixed Capital Formation	(-) 47.1
GVA	(-) 22.9	Exports	(-) 19.8
		Imports	(-) 40.4
GDP			(-) 23.9

Source: MoSPI.

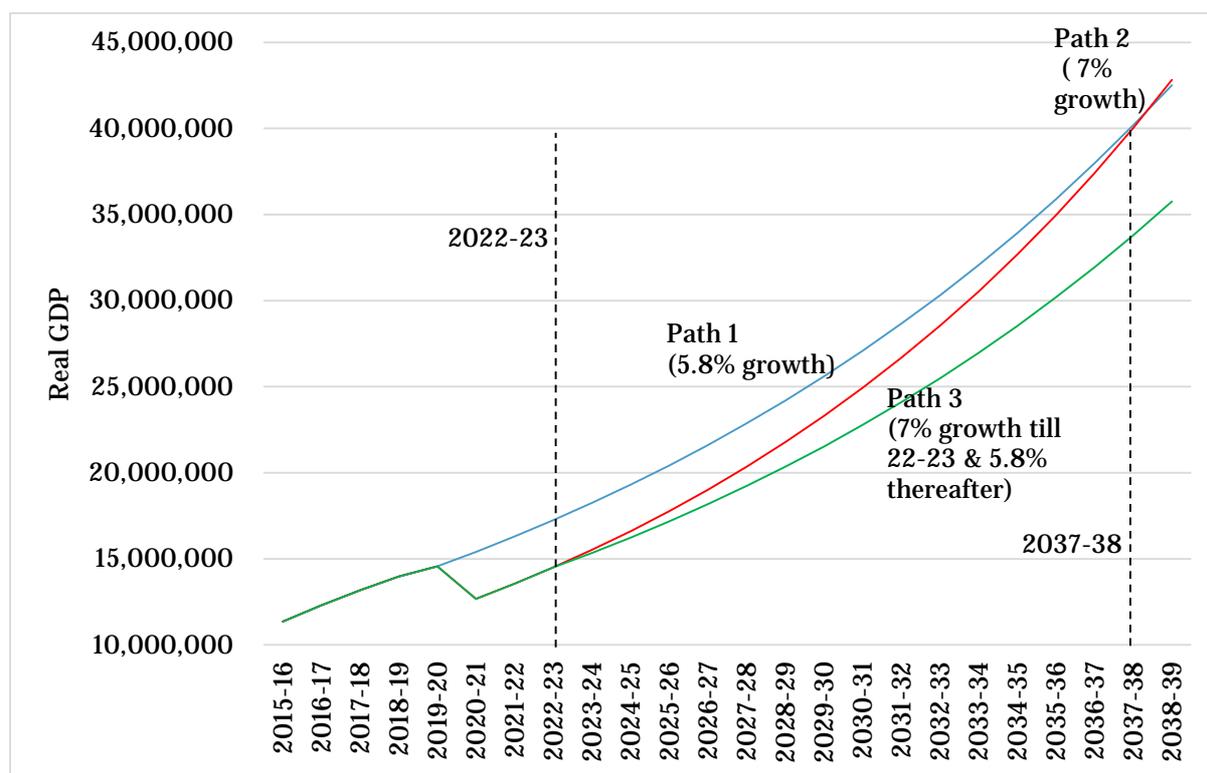
Thus, both supply and demand collapsed during Q1: 2020-21. However, inflation has remained elevated and sticky at 6.7 per cent in July and August 2020, breaching the RBI's inflation target band of 4 per cent \pm 2 per cent despite the contraction in demand. This suggests that supply contraction has dominated macroeconomic dynamics. The nation-wide lock down was gradually eased since June 2020 to enable the revival of economic activities. Some States have subsequently imposed local lockdowns to cope with the pandemic. Therefore, supply constraints have continued, albeit with some easing. The leading indicators for the second quarter suggest that while y-o-y growth is still negative the

contraction is moderating. Going forward, much will depend on how the spread of the disease plays out, how Central and State governments respond to it and how workers & entrepreneurs respond to the disruption. All these factors are major unknowns at this time. Hence, the outlook for the rest of 2020-21 and 2021-22 remains highly uncertain.

We are now forecasting that y-o-y growth will remain negative through Q2, Q3 and Q4 at (-) 12.7 per cent, (-) 8.6 per cent and (-) 6.2 per cent respectively. For the year as a whole 2020-21 GDP will decline by (-) 12.6 per cent.

The key question is how the economy will perform thereafter. References to V-shaped recovery obfuscate more than they reveal. The fact is that economic hysteresis, the medium to long-term footprint of a major economic shock, is indeed very long. Post 2020-21 annual growth of 7 per cent would imply a growth swing of 20 per cent not ever seen so far in India. Assuming optimistically that 7 per cent growth is indeed achieved because of the base effect of a steep decline in 2020-21, combined with strong policy measures to revive growth; we would still reach the previous peak output level of 2019-20 only by the end of 2022-23 (Figure 2). If that annual growth path of 7 per cent can be sustained over the long term, again a heroic assumption, the economy will catch up with its pre-pandemic growth path only by 2037-38. A more likely scenario is that after getting back to its previous peak output level by 2022-23 the economy will settle back to its pre-pandemic growth path of 5.8 per cent. To nudge the economy to any higher growth path would require ambitious economic reforms across a wide front like the 1991 reforms. A strong revival of global demand could also move the economy to a higher growth path.

Figure 2: Simulated Paths of Medium to Long-term Growth



Source: NCAER Authors.

The ***Quarterly Review of the Economy*** aims to meet the needs of policymakers, corporates, and others interested in tracking the latest developments in the Indian economy. As with this September QRE for Q2, NCAER issues QRE for each quarter to track the Indian macro economy and assess the impact of policies and shocks like the present Coronavirus pandemic. It provides a data-driven, independent analysis of current policies and tracks sector-by-sector developments in India and globally. It contains special sections on external developments, prices, fiscal policy, monetary policy and capital markets. NCAER's quarterly and annual growth forecasts are widely quoted in the Indian and international media. Each QRE is released by NCAER at a quarterly State of the Economy seminar/webinar that brings together policymakers, industry leaders, and researchers.

About NCAER | The National Council of Applied Economic Research

Established in 1956, NCAER is India's oldest and largest independent, non-profit, economic policy research institute. NCAER's work cuts across many sectors, including growth, macro, trade, infrastructure, logistics, labour, urban, agriculture and rural development, human development, poverty, and consumers. The focus of NCAER's work is on generating and analysing empirical evidence to support and inform policy choices. It is also one of a handful of think tanks globally that combine rigorous analytical and modelling capacity with deep data collection capabilities, especially for household surveys. More on NCAER is available on www.ncaer.org.

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