

INDIAN ECONOMY IN 2020: OVERVIEW

Context

The Covid-19 pandemic upended the Indian economy but a deeper-than-anticipated recession may now be making way for a faster bounce-back. Over one crore Indians have been infected by the pandemic, and per capita income will likely slip right back below an already paltry \$2,000 a year amid two straight quarters of contraction in GDP growth so far.

GDP Growth

First, a slowdown and then the pandemic meant India's GDP growth eased to 3.1% in the quarter ended March 2020, before it slipped to -23.9% in the June quarter, showed data released by the Ministry of Statistics and Programme Implementation.

GDP contracted by 7.5% in the three months through September, according to the ministry's latest statement.



The contraction in government expenditure came as a shock, while capital formation saw a smaller than estimated contraction in the September quarter.

Private consumption, too, contracted at a decelerating pace aided by pent-up demand and festive demand. It is estimated to grow by 0.1% in the October-December quarter, according to the Reserve Bank of India.

The Tailwinds

NSO's GDP data release packed a surprise result — the downturn in Q2 turned out to be shallower, and the pace of recovery beat most predictions, aligning broadly with high frequency indicators that pointed to a pick-up in economic momentum.

RBI's economic activity index too projected that real GDP growth was expected “to break out into positive territory in Q3” (0.1%).

Sectoral-split shows that auto and capital goods could be seeing a turnaround in forward earnings. Healthcare, IT, FMCG companies are sighting stronger earnings outlook. Digital technologies are seen as a bright spot.

Despite the challenge from a new wave of infections, the outcome of the US presidential election and positive news on vaccines could have a sustaining impact on the prospects of the global economy. A positive outcome of the Brexit negotiations is a plus.

Equity markets, which were vacillating between rallies and sell-offs up to November, have since surged past previous highs.

Q4 2020 is projected to be the strongest quarter for emerging market economies inflows since Q1 2013.

Most of all, India is bending the Covid curve and a couple of vaccine candidates have hit not only trial status but also suitability for usage in India, with more in the pipeline.



The Red Flags

Demand conditions remain weak, evidenced by the decline in exports and imports, which reflect the state of external and domestic demand, according to NCAER.

The November RBI Consumer Confidence Survey showed that while consumer sentiment was higher that month than in July and September 2020, confidence was lower in November compared to the same period a year ago.

On the GDP-linked demand side, the latest data show a 22% contraction in the government final consumption expenditure in Q2, while on the GVA output side, the public administration, defence and other services sector — a proxy for government spending — was down 12% in the Q2 after a 10% dip in the Q1. The trend points to the reluctance of central and state governments to provide a fiscal spending boost to balance the fall in investment demand.



India's growth had been moderating since the beginning of Q4 2018-19.

Centre's gross tax receipts are projected to fall by over 10%, on top of the 3.4% slide in 2019-20. Non-tax revenues appear to be bleak.

States, saddled with higher expenditure on health and locked in a tussle with the Centre over GST payouts, are unlikely to restart the capex cycle.

If demand conditions cannot be rekindled, the private sector is not

expected to restart investments or hiring, which would further deteriorate demand conditions. In the absence of a counterbalancing push, the problem could turn cyclical.

As the government largely refrained from providing substantial income support to businesses, jobs were lost as MSME earnings took a hit. The third quarter of fiscal 2020-21 will end with employment of 395 million, which would be 2.5 per cent lower than the 405 million employed in the December 2019 quarter, as per CMIE data.

Contact service sectors such as hotels, restaurants, airlines, salons, which were doing exceptionally well before the pandemic, are among the worst hit, and will continue to struggle till the time the fear of the virus lasts.

As the restrictions were lifted, many who did not get jobs went on to leave the labour force. Typically, when more people find jobs, larger numbers should come looking. But the reverse seems to have happened since September.

Also, CMIE surveys up to August show the biggest losses in employment are in quality jobs — salaried employment. Women have been more impacted.

The RBI in its December monthly bulletin highlighted the risks from continued high inflation: “...Efforts need to be redoubled to excoriate the 'worm in the apple' — inflation — before it hurts the impulses of growth that are taking root”.

According to Nomura, retail inflation is unlikely to come down enough for RBI to cut rates in the whole of 2021. Over the medium term, there are chances of inflation heating up again, and RBI may have to switch to hiking rates as well in 2022.

Looking ahead



Investment in research and development in medicine, biotechnology, and pharmaceuticals are the need of the hour.

Industry is watching the resolution efforts at Wistron's iPhone manufacturing facility in Karnataka and when there is continuing labour unrest at Toyota Kirloskar Motors' plant outside Bengaluru.

Investors are also watching the government's reactions on the legal setbacks in the Cairn and Vodafone retrospective taxation cases. India has chosen to challenge the Vodafone verdict, and a challenge is expected in the Cairn case as well.

Since April 2020, with the moratoriums kicking in, the recognition of defaults has been pushed down the road. It's a double whammy for the sector — loans have turned bad, even if they're not being recognised as NPAs, but the lender is not getting the interest in cases where firms have folded up.

According to the IMF, the economy is likely to contract by 10.3 per cent in the current fiscal, and then grow by 8.8 per cent in 2021-22. But while real GDP is expected to rebound, it may take almost two years for it to get back to pre-pandemic levels.