ICRA

INDIAN ECONOMY

Modest fiscal support, extension of lockdown, looming labour supply mismatches suggest deeper GDP contraction of 5.0% in FY2021

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Aditi Nayar
+91 124 4545 385
aditin@icraindia.com

Aarzoo Pahwa
+91 124 4545 873
aarzoo.pahwa@icraindia.com

The immediate fiscal support under the "Aatma Nirbhar Bharat Abhiyan" announced by the Government of India (GoI) is estimated at a modest 10% of the substantial total package of Rs. 21.0 trillion. With the further extension of the lockdown, and the expectation of substantial delays in getting the full supply chain operational, especially given the likelihood of enduring labour mismatches following the return of migrant workers to their home states, we now anticipate the GDP contraction in Q1 FY2021 to be deeper, and the subsequent economic recovery in India to be shallower and more delayed than our earlier assessment. Accordingly, we now expect Indian GDP (at constant 2011-12 prices) in FY2021 to record a sharper year-on-year (YoY) decline of 5.0% relative to our earlier expectation of 1.0-2.0%.

To support the Indian economy in the aftermath of the Covid-19 pandemic, the GoI had announced the "Aatma Nirbhar Bharat Abhiyan" or "Self-Reliant India Movement" on May 12, 2020, with an intended package of Rs. 20.0 trillion. The measures detailed subsequently amount to a higher Rs. 20.97 trillion (refer Exhibit 1), which is equivalent to ~10% of the nominal GDP of India for FY2020 (as per the 2nd Advance Estimate released by the CSO). The package includes the monetary measures already announced by the Reserve Bank of India (RBI; Rs. 8.02 trillion) as well as the initial announcements made by the Centre (Rs. 1.93 trillion), which include the relief package announced under the Pradhan Mantri Garib Kalyan Yojana (PMGKY), revenue foregone due to tax concessions since March 22, 2020, and the emergency response and health system preparedness package.

Exhibit 1: Break-up of the stimulus provided under the Aatma Nirbhar Bharat Abhiyan package

Items	Amount in Rs. Trillion
Tranche I	5.95
Tranche II	3.10
Tranche III	1.50
Tranche IV and V	0.48
Sub-Total	**11.03**
Earlier measures announced i.e. under PMGKY, health sector, revenue loss due to tax concessions	1.93
RBI monetary measures	8.02
Sub-Total	**9.94**
GRAND TOTAL	**20.97**

Source: Ministry of Finance, GoI; ICRA research

Some of the fresh support includes additional allocations for free food, MGNREGS, etc., that would aid migrant workers who are faced with a severe loss of income. In addition, the GoI has announced various measures focussing on several sectors of the economy such as MSMEs, health, NBFCs, MFIs, state governments, Discoms, housing, agriculture and allied activities, defence, real estate, mining, civil aviation, space as well as migrants, street vendors, taxpayers, etc. These measures have come in the form of credit support, liquidity provision, cash outgo and regulatory reform measures.

In our view, many of the GoI's announcements are in the form of enabling provisions to support a recovery in economic growth after the lockdown is eventually lifted, such as the working capital support to MSMEs. Several of these announcements seek to provide credit to stressed sectors, that will help them to restart operations after the lockdown is lifted, but would not absorb their losses related to the lost output for more than two months. Moreover, many reforms have been announced, that while much awaited and welcomed, may manifest in improved economic activity only with a lag of a few years. ***Overall, we estimate the direct fiscal cost of this package to be limited to 1.0% of GDP, or around 10% of the total announcements. While the measures are welcome, many of them will not be able to counter the demand destruction caused by the Covid-19 outbreak, or address the prevailing supply chain infirmities.***

In the meantime, the number of Covid-19 infections in India has escalated rapidly, and the GoI has extended the lockdown period by another two weeks, i.e. till May 31, 2020. Under the new guidelines issued by the Ministry of Home Affairs, all states and UTs have the authority to demarcate their areas into Red, Orange, Green, containment, and buffer zones, based on certain parameters and can impose further restrictions, if required. Only limited activities remain prohibited throughout the country, irrespective of the zones, such as domestic and international air travel (except for medical and security purposes permitted by the MHA), metro rail services, schools, colleges, hospitality services (except those used for housing health/police/Government officials/healthcare workers and quarantine purposes), religious activities, and large public gathering places such as cinema, shopping malls, etc. However, the government have decided to relax the restrictions imposed on certain activities, particularly in areas barring Containment zones, such as opening up of shops and markets with staggered timings, sport activities without spectators, restaurants only for takeaways and home deliveries, etc. In the case of Containment zones, only essential activities will be allowed, as announced earlier. Notably, there are few other activities which are now permitted, but with some restrictions, such as movement of individuals by trains, inter-state movement of stranded persons by buses and trains with mutual consent, etc. However, the intra-state movement of vehicles and buses is to be decided by the states and UTs.

With multiple extensions of the lockdown creating uncertainty regarding the resumption of gainful employment and income generation opportunities, many migrants have chosen to avail of the special trains being run by the Indian Railways to return to their villages in their home states. With a considerable portion of their savings likely to have been used up over the last two months, we are apprehensive that the migrant workers may choose to delay their return to the cities and towns until after the festive season is over, which could affect the pace of normalisation in various economic activities, including manufacturing and construction.

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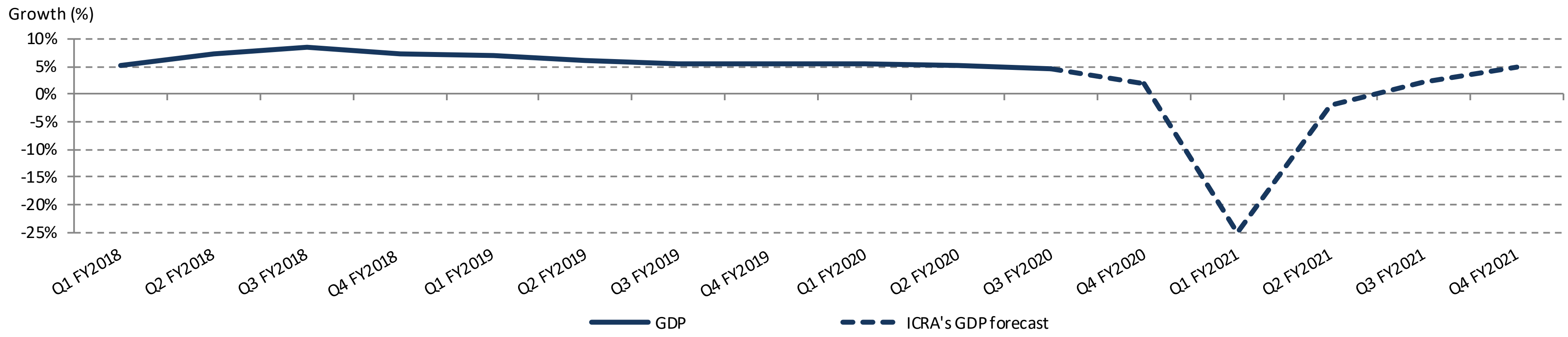
At present, we have assumed that the lockdown will be lifted within Q1 FY2021, based on which the trajectory of GDP indicates a V shaped recovery. However, if there is a second wave of infections that forces subsequent lockdowns either in India or globally, the ensuing demand uncertainty and supply chain hiccups could result in a W shaped economic cycle, the inflection points of which can't be gauged at this stage.

Exhibit 2: YoY Growth in GDP (At constant 2011-12 Prices) and ICRA's forecast for Q4 FY2020 and FY2021



Source: CSO; CEIC; ICRA Research

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ICRA

Business Contacts

Mr. L. Shivakumar
E-mail: shivakumar@icraindia.com
Tel: +91 22 6114 3406 / +91 98210 86490

Mr. Jayanta Chatterjee
E-mail: jayantac@icraindia.com
Tel: +91 80 4332 6401/ +91 98450 22459

Media and Public Relations

Ms. Naznin Prodhani
E-mail: communications@icraindia.com
Tel: +91 124 4545 860

Registered Office:

1105, Kailash Building, 11th Floor,
26, Kasturba Gandhi Marg,
New Delhi - 110 001
Tel: + 91 11 2335 7940-45

Corporate Office:

Building No.8, 2nd Floor,
Tower A, DLF Cyber City Phase II,
Gurgaon- 122 002
Tel: +91 124 4545300

Ahmedabad

1809-1811, Shapath V,
Opposite Karnavati Club
S.G. Highway, Ahmedabad - 380015
Tel: +91 79 4027 1500/01

Bengaluru 1

'The Millenia', Tower- B, Unit No. 1004,
10th Floor,1 & 2 Murphy Road,
Bengaluru - 560 008
Tel: +91 80 4332 6400

Bengaluru 2

2nd Floor, Vayudooth Chamber,
15-16, Trinity Circle, M.G. Road,
Bengaluru - 560 001
Tel: +91 80 4922 5500

Chennai

5th Floor, Karumuttu Centre,
634, Anna Salai, Nandanam
Chennai - 600 035
Tel: +91 44 4596 4300

Hyderabad 1

No. 7-1-58, 301, 3rd Floor, 'CONCOURSE',
Above SBI-HPS Branch, Ameerpet,
Hyderabad - 500 016
Tel: +91 40 4920 0200

Hyderabad 2

4A, 4th Floor, SHOBHAN,
6-3-927, A&B Somajiguda,
Raj Bhavan Road,
Hyderabad – 500082
Tel: +91 40 40676500

Kolkata

A-10 & 11, 3rd Floor,
FMC Fortuna 234/3A,
A.J.C. Bose Road,
Kolkata -700 020
Tel: +91 33 7150 1100/01

Mumbai

3rd Floor, Electric Mansion
Appasaheb Marathe Marg,
Prabhadevi,
Mumbai - 400 025
Tel: +91 22 6169 3300

Pune

5A, 5th Floor, Symphony,
S. No. 210 CTS 3202 Range Hills Road,
Shivajinagar,Pune - 411 020
Tel: +91 20 2556 0194, 020 6606 9999

Email: info@icraindia.com
Helpdesk: 9354738909
Website: www.icra.in/ www.icraresearch.in