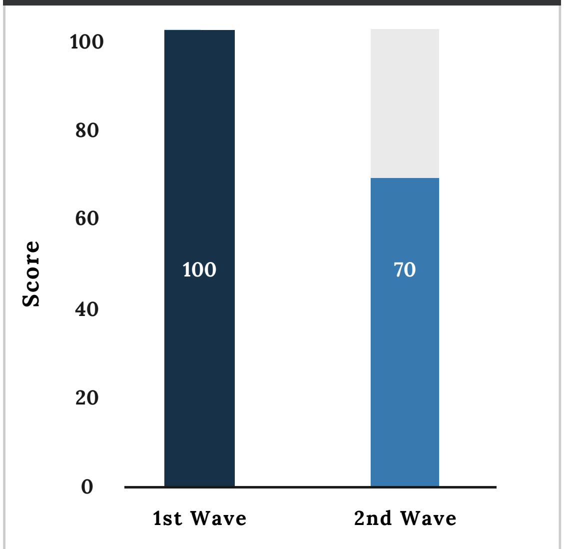
# THE IMPACT OF THE SECOND WAVE ON THE INDIAN ECONOMY

| 2021-21 Growth Forecasts for India (percent) | | | | | |
|---|---|---|---|---|---|
| | Post-second COVID Wave | Pre-second COVID Wave | | Post-second COVID Wave | Pre-second COVID Wave |
| **RBI** | 10.5 | 10.5 | **Goldman Sachs** | 11.1 | 11.7 |
| **IMF** | 12.5 | - | **Nomura** | 12.6 | 13.5 |
| **World Bank** | 10.1 | - | **JP Morgan** | 11.0 | 13.0 |
| **ADB** | 11.0 | 12.5 | **UBS** | 10.0 | 11.5 |
| | | | **Barclays** | 10.0 | 11.0 |
| ***Average growth projection before the second wave*** | | | | ***12.0 percent*** | |
| ***Average growth projection after the second wave*** | | | | ***11.0 percent*** | |

## *The Covid Waves in India – Different Outlooks or Different Frames?*

The second wave of the Covid-19 pandemic in India has wreaked havoc, with the country reporting over three hundred thousand new cases daily beginning April 21, 2021 and growing exponentially. Many states have imposed lockdowns to limit the number of new cases and ease the burden on their healthcare infrastructure. These containment measures have brought many economic activities to a halt. However, the restrictions during the second wave are relatively less severe than the first. The University of Oxford's Covid-19 Stringency Index, which measures the strictness of restrictions imposed on economic activities and movement of people, stood at 70 (out of 100) against 100 last year. In comparison to the first Covid wave, the test positivity rate is *5-10 percent* higher during the second one. However, ***after factoring in the lockdown's stringency and the number of tests, the*** *positivity rates during the two waves are comparable to each other.*

Covid-19 Stringency Index for India




## *Fiscal Measures – Too Few or Shallow Pockets?*

The Government of India has taken some measures to abate the impact of the second wave. This includes a custom duty waiver for essential items like oxygen, oxygen equipment and vaccines. It has also permitted state governments to borrow up to 75 percent of their annual limit for FY22 in the first nine months, i.e., between April-December. To boost private investment for covid-related healthcare, the Government has allowed spends on makeshift

COVID-19 hospitals and temporary care facilities to be treated as an eligible CSR activity. The RBI also announced a few measures to minimise the impact of the second wave. These include (i) term liquidity facility of INR 500 billion to provide fresh credit support for improving COVID-related health infrastructure and services; (ii) purchase of government securities worth INR 350 billion to allow for an orderly evolution of the yield curve; and (iii) a fresh moratorium on loan repayments to individuals and MSMEs. Finally, the Government of India is accepting foreign aid, to combat healthcare challenges posed by the second wave. The decision to accept foreign humanitarian aid marks a directional policy shift, as it is the first such instance in the last 16 years.

The Government of India announced a slew of measures to mitigate the downside economic impact of the first wave of the pandemic. The economic stimulus package - Aatmanirbhar Bharat - of INR 20 trillion (10 percent of the GDP) focused on relief, rehabilitation and rebuilding the economy. These included free food distribution to the people, credit guarantees to MSMEs and structural reforms covering agriculture, industry, mining, infrastructure, and so on. However, the true fiscal stimulus amounted to only INR 2.5 trillion, which is approximately 1.3 percent of the GDP. Notably, India's Covid-19 pandemic fiscal cost was the lowest among major nations such as the US, Singapore, Germany, Canada, the UK and Japan.

***A shallow response to the second wave can be attributed to limited fiscal space.*** The Government has exhausted most of its resources for providing relief during the first wave. Besides, deteriorating sovereign ratings and undersubscribed bond issues impede fund raising from foreign and domestic markets. The Government has also struggled to raise funds through disinvestment in select public enterprises like Air India, BPCL, and Shipping Corporation of India. This public sector disinvestment drive is unlikely to yield dividends in the medium term. Consequently, this will further limit the India's ability to respond to the pandemic.

## *Public Administration Needs to Focus on Compliance and Effective Communication*

Table 1: IAS Officials' Response to the Pandemic Management

| Attributes | Affirmation, Percent |
|---|---|
| States should have the autonomy to formulate their own responses for the Covid crisis based on their needs and capacities | 83.0 |
| India had enough laws and rules to deal with Covid crisis | 83.0 |
| There is need for better compliance by all during Covid crisis | 83.0 |
| Granting travel permits to influential people during Covid crisis is unacceptable | 83.0 |
| Denial of selective travel permits during Covid crisis may have adverse consequences | 83.0 |
| Effective communication campaign to secure people's understanding and cooperation, over strict enforcement of penal measures, as the preferred strategy for ensuring successful pandemic management | 83.0 |

The governance structure in India places Indian Administrative Services (IAS) officials at the forefront of the Covid response. They officiated several empowered action groups, special teams and manned field administration to respond to the pandemic. Their role is pivotal because more than 4,000 executive orders were issued to blunt the impact of this humanitarian and economic crisis.

The Centre for Policy Research conducted a survey of 560 serving and retired IAS Officers in the country regarding the Covid-19 response. Table 1 highlights the salient results from the survey. ***Ensuring better citizenry compliance to rules and orders, and administration's effective communication with them may considerably mitigate the ill-effects of the Covid crisis.***

## *Sectoral Impacts are Negative, but Many Fare Better Than in the First Wave*

MSMEs, which run on small operating margins, face a sizable decline in incomes and spending. Consumer-facing sectors (like tourism, consumer retail, entertainment, to name a few) may suffer the most, with States shutting down malls, market complexes, movie theatres and restaurants to break the chain of transmission. The demand for energy has started to show early signs of weakening, registering a month-on-month fall of 4.34 percent during the second wave. This decline is significantly lower than last year, when the month-on-month energy consumption declined by over 18 percent in the first week of April 2020. Railway freight movement of major inputs, such as coal, iron, and steel, has remained relatively steady. This indicates that, in aggregate terms, the impact of the second COVID-19 wave on industrial activities has been minimal. Consequently, industrial employment, which is largely informal, is likely to stay relatively resilient this year. However, diverting liquid oxygen for medical purposes may have some impact on select industries like steel, automotive, and petrochemicals, among others.

Table 2: Sectoral Impact of the Second wave

| Sector | Absolute Impact | Impact relative to the first wave |
|---|---|---|
| MSME | Negative | Lower |
| Energy | Negative | Lower |
| Consumer-facing sectors (tourism, consumer retail, entertainment, etc.) | Negative | Similar |
| Construction | Negative | Lower |
| Travel and transport | Negative | Lower |
| Manufacturing | Negative | Lower |
| MSME | Negative | Lower |

Internet companies, like e-commerce firms, remained largely insulated from the shock of COVID-19 last year as online purchases increased due to safety concerns. However, since the second wave has especially targeted people between the ages of 20-40, these companies also struggle to sustain their operations as many employees are infected by the virus. Additionally, many states have put restrictions on the sale of non-essential items through e-commerce platforms. Therefore, the impact of the second COVID-19 wave on some tech companies may be severe. IT service firms face a similar challenge as reports suggest that nearly 20-30 percent of their human resources are being affected. If the second wave persists or a subsequent wave emerges, many subsidiaries of foreign companies, which dominate IT services, may onshore some operations.

## *The 'Political Economy' of Vaccination*

The two main vaccine manufacturers in India, Serum Institute of India (which makes Covishield) and Bharat Biotech (which makes Covaxin) have catalogued their prices (Table 3). They will mandatorily sell half their stocks to the Central Government, and the remaining half to state governments and private entities. While the price differentials have stirred considerable debate in the country, several states including Delhi, Karnataka, Haryana, Odisha, Jharkhand, West Bengal, have decided to provide free vaccines to people aged 18 years and above.

**Table 3: Price per Vaccine Dose (INR**

| Sector | Covishield | Covaxin |
|---|---|---|
| Central Government | 150 | 150 |
| State Governments | 300 | 400 |
| Private Entity | 600 | 1,200 |

**Table 4: Cost of Vaccine Provision**

| | | | |
|---|---|---|---|
| **18+ Population, million**<br>**GDP, RS. billion** | | **810**<br>**134089** | |
| | **Scenario 1**<br>Complete vaccination by Central Government | **Scenario 2**<br>50% vaccination by Central Government, 50% by State Governments | **Scenario 3**<br>50% vaccination by Central Government, 30% by State Governments, 20% privately |
| Cost to Central Government for 2 doses, INR billion | 243 | 121.5 | 121.5 |
| Cost to State Governments for 2 doses, INR billion | NIL | 254.6 | 152.7 |
| Cost to private entities for 2 doses, INR billion | NIL | NIL | 222.2 |
| **Total vaccine cost, INR billion** | **243.0** | **376.1** | **496.4** |
| **Percent of scenario 1** | **100.0** | **154.8** | **204.3** |
| **Percent of GDP** | **0.2** | **0.3** | **0.4** |

We present three scenarios in Table 4. We assume a 6:1 mix of Covishield and Covaxin for the population, based on the respective production capacity. ***In a scenario where the Central Government provides 50 percent, State Governments provide 30 percent and the remaining 20 percent doses are privately provisioned, the total cost of vaccinating 18+ population will be INR 496.4 billion (Scenario 3).*** This is INR 120.3 billion more relative to the case when the Central and the State Governments equally provision doses for the 18+ population (Scenario 2), and INR 253.4 billion more relative to the case where the Central Government alone provisions vaccines for the 18+ population (Scenario 1). ***Policymakers must factor in this aspect while formulating a vaccination strategy to ensure quick and all-inclusive coverage.*** A delay in vaccination or incomplete coverage may lead to considerable economic rent (or dead-weight), as avoidable expenditures, and forgone opportunities and incomes.

Notably, the two vaccine manufacturers in India, SII and Bharat Biotech, can together produce around *90 million doses a month.* At this rate, ***vaccinating 840 million people who make up the 18+ population in India (two doses each) will take approximately 19 months!*** Imports of other vaccines (e.g., Pfizer, Moderna, Johnson & Johnson, and Sputnik V) may shorten this duration to some extent, but not drastically. Even if India ramps up its domestic vaccine production capacity, they are only *70-80 percent efficacious.* The possibility that some variants will not respond to the available vaccines is also not ruled out. If so, ***Indian policymakers will have to dynamically rethink the country's vaccination strategy, with all instruments available at hand.***

## *Unemployment Rises at a Slower Rate, but Many Labour Market Concerns Remain*

As many states implemented containment measures, labour conditions deteriorated in April 2021. However, the impact is considerably moderate. ***The Unemployment rate is estimated to increase to 8 percent*** in the month of April '21 from 6.5 percent in March '21. This is significantly lower than the unemployment rate in April '20, which stood at a staggering 23.52 percent. However, with states extending lockdowns, employment outlook remains bleak in the country. Experts argue that the labour market situation is starker than he numbers suggest for three reasons: a fall in the number of employed people, a decline in labour force participation and the rise of those who are unemployed yet, are not looking for jobs.

The quality and duration of unemployment pose an even more serious concern for the country. Approximately six million salaried and three million businesses in rural India joined agricultural jobs during the first wave. But, the rise in agricultural output is merely 2-3 percent in each of the four quarters of 2020-21, as against 3-4 percent in the previous year. Taken together, these imply ***a sharp fall in labour productivity.*** During the second wave this dynamic is unlikely to have changed as growth in rural salaried jobs and business is negligible. The urban salaried sector lost nearly 3.6 million jobs during the first wave of the pandemic. It is unlikely that these have regained completely due to muted economic activities till the second wave surfaced. ***The job market will remain subdued till the pandemic looms. Policymakers need to devote time and effort in (1) reallocating labour from agricultural to non-agricultural activities, (2) skilling for the evolved nature of economic activities, and (3) putting in place a redistribution policy to tackle growing income inequality, that arises because more workers will join agriculture – a sector where productivity has fallen.***

## *Cautious Discretionary Spending with Bleak Future Outlook*

The second wave of COVID-19 has cautioned households against discretionary spending. According to the RBI's consumer confidence survey for March 2021, ***58.5 percent of them reduced their discretionary expenditure relative to the previous year, with a majority (75.4 percent) expecting it to further deteriorate or remain at that reduced level*** in 2021. Besides, a survey conducted by Centre for Monitoring Indian Economy (CMIE) indicated that 54 percent of urban Indian households considered the current period the worse time to indulge in discretionary spending. Only 12 percent of the

The first wave of Covid-19 in India had severe adverse impact on discretionary or non-essential expenditure. According to a survey by KPMG, 78 percent of the respondents reduced their discretionary spending. However, 51 percent of the respondents also believed that the impact of the COVID-19 pandemic will be short lived. Due to this optimistic attitude and resumption of economic activities, the country witnessed a gradual rise in the discretionary expenditure in the latter half of the previous fiscal.

households increased their spending on non-essentials compared to 28 percent last year. From goods and the supply-side of services, this means a ***considerable hit for industries in the non-essential segment with low sales revenue and capacity utilization***.

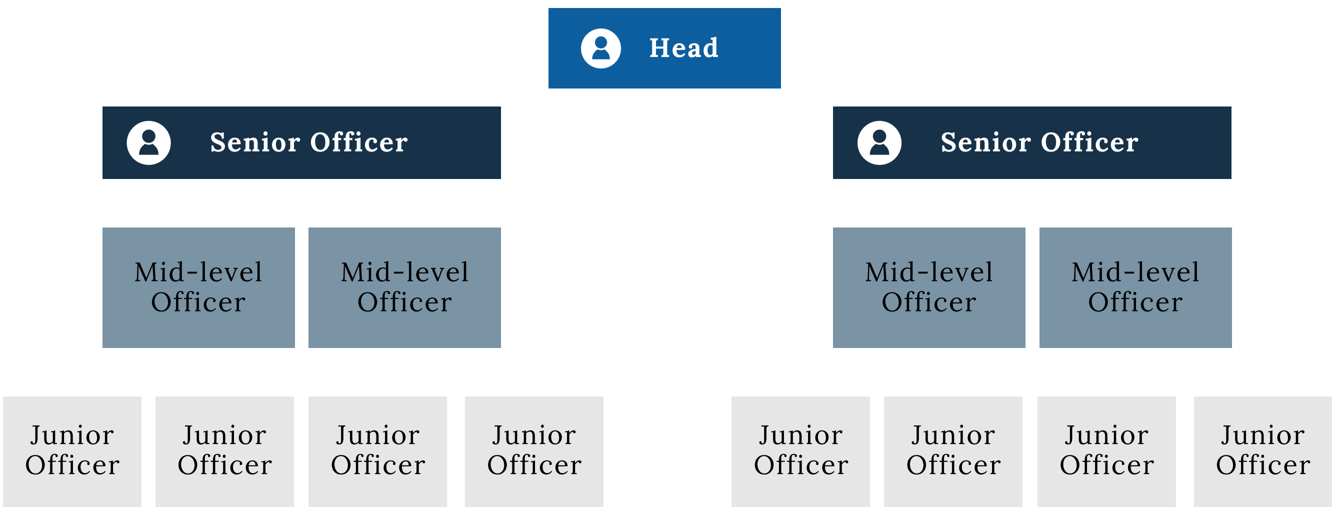
## *India's Globalised Avatar is Jolted*

India's response to the first Covid wave made it a benchmark for other countries to follow. In fact, several multilateral for a, such as the World Health Organisation (WHO) and the United Nations (UN), lauded the efforts of the Indian Government to control the pandemic. However, the second wave has jolted India's image abroad. International media and the large global community have termed the surge in cases as a serious policy failure and asked difficult questions of the Narendra Modi Government.

Several countries have restricted the entry of travellers and cargo from India. This is likely to have a considerable downside effect on trade in goods and services, which already registered a negative growth of 16.66 percent during April-September 2020. The spillovers percolate to several domestic activities as well. For example, India hosts several professional sporting leagues such as the Indian Premier League (IPL), Indian Super League (ISL), Premier Badminton League (PBL), among others. The conduct of these tournaments is also jeopardised with the second wave. The market size of these sporting leagues is estimated to be over INR 40 trillion. MICE (Meetings, Incentives, Conferences, Events) activities in India, with the estimated market size of over INR 375 billion, are likely to witness a similar contraction.

## *Corporate Strategy Needs Rework*

The first wave, the second wave and a likely third wave give sufficient reasons for corporates to reorient their longer-term operational strategy. The most serious challenge comes in managing employee chains (Figure 1). Due to the high levels of infectivity of the Coronavirus, especially during the second wave, it is likely that an employee at any node of the pyramid may get the disease. This not only compromises on-going operations but also puts undue pressure on other employees, thus adversely influencing an organisation's overall productivity. To mitigate this risk, it is important that companies have a back-up employee for every assignment, either by repurposing the existing pool of employees or hiring fresh ones – both of which are costly exercises. It also becomes incumbent on organisations to provision insurance, masks, sanitation, and comply with public orders.



## *Human Capital Impact Will Sustain*

Due to the first wave, schools and colleges were shut down across the country. The Central Government and various states governments decided to reopen them in a phased manner once the first wave receded. However, as cases surged again in 2021, many states decided to shut down educational institutions. Such temporary closures can have major implications for students as it is difficult to engage them in remote learning initiatives. Therefore, it can lead to an increase in dropout rates and substantial economic losses, which can have a long-term impact on human capital formation in India.

The first wave led to a loss of 0.5 years of learning-adjusted years of schooling (LAYS), which is estimated to result in a lifetime earning loss of over USD 400 billion. The second wave will likely have a homologous impact on schooling. Hence, on a cumulative basis, India stands to lose at least USD 800 billion in the long-term. Apart from these monetary personal losses, loss of educational attainment will have considerable intergeneration effects as well. As per estimates if the parents are unable to complete tertiary education, which is likely to be the case for a considerable fraction of the population, the chance that their child will complete university goes down by 20-25 percent.

## *Additional Strategies*

Covid is not a temporary disruption, it is here to stay. India has already seen two waves and is expected to be hit by a third one. Therefore, it is now time to rethink administration and business. This requires coordination at all levels – governments, corporates, societies and households. In this context, we suggest additional measures for governments and corporates to put in place, in table 5.

**Table 5: Additional Strategies for Governments and Corporates**

**Governments**

1. Improve healthcare research and infrastructure
2. Improve (beneficiary) identification for targeting healthcare and social welfare interventions
3. Limit the size of gatherings, allow limited size gatherings only under strict tracing protocol
4. Make rule-based restrictions on group/contact activities to incentivize social-distancing. For example, make a four-tier restriction plan, with tier-4 as complete lockdown. A locality will fall under either of these tiers based on the number of critical cases
5. Fast-track digital adoption in the country
6. Facilitate business adaptation/transition due to Covid
7. Rework income distribution to help the poor and vulnerable, as they bear a disproportionately larger burden

**Corporates**

1. Promote work from home and/or provision for up to one-third attendance in office
2. Ensure employees furnish a proof of immunity or undergo periodic health check-ups
3. Establish trust in inter-corporate transactions/transfers through Covid-guarantees, wherever possible

**Authors**
Vikash Gautam, Aman Grover



**contactus@koanadvisory.com | www.koanadvisory.com**