

# COVID-19: Indian economic forecast amidst uncertainties





# The journey from 'respond' to 'recover'

More than six months of living with COVID-19, yet the future of the pandemic remains uncertain making it difficult for businesses to plan their way forward. As world leaders and businesses respond to this crisis, they will require resilience to prepare for the uncertainties in the months ahead to recover and then thrive (figure 1). One of the ways to prepare is to equip oneself with as much knowledge as possible and plan the way forward. Scenario analysis is an effort to use

current information to anticipate probable outcomes based on underlying assumptions.

Dr. Albert Einstein had famously said, "knowledge of what is, does not open the door directly to what should be". This analysis based on assumptions made today does not provide certainty to how the world will shape up in the near future. However, businesses can use these forecasts as a guidance for strategic, financial, and operational planning over the next 18–24 months.

**Figure 1. The economy is in the phase of learning to emerge stronger**



Source: Deloitte resources

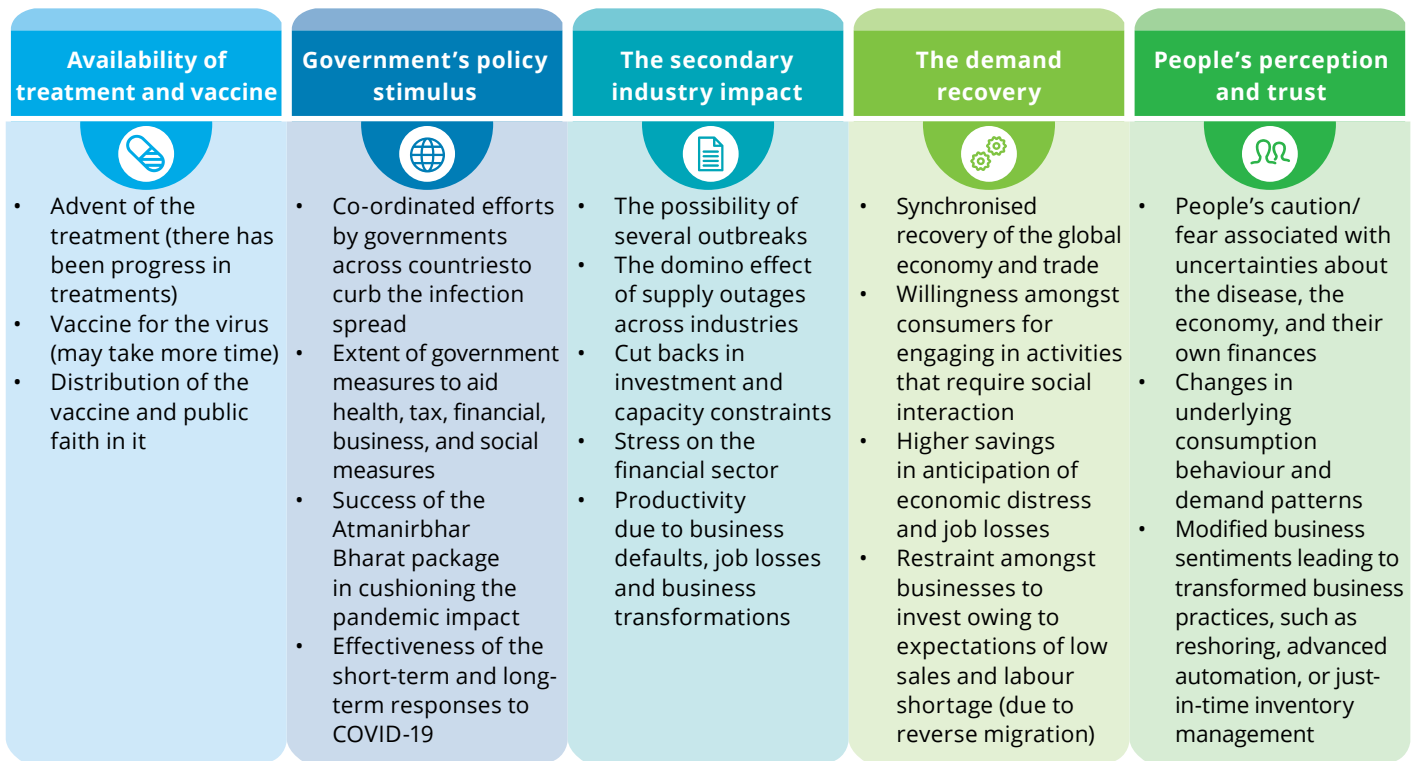
# The 'high five' that will shape the path to recovery

In our previous version (in April), we examined the possible ways COVID-19 is likely to affect the economy through four transmission vectors, the supply-side disruption, the global and domestic demand side fallout, the banking and financial sector stress, and the oil price vulnerability.<sup>1</sup> We examined these to gauge the impact the pandemic may have on lives, businesses, and the economy and how business leaders and policymakers can respond to this crisis.

The recovery, on the other hand, will depend on five factors (Figure 2):

- a. **Availability of a treatment and vaccine** – It will determine the time and the pace of the economic recovery. Today, no specific treatment can cure this disease but drugs that can reduce the recovery time or prevent the disease from getting critical in certain cases are available.<sup>2</sup> However, inventing the accepted vaccines is likely to take longer. Even if there is a vaccine by end of this year, it may take some time to manufacture and deploy the vaccine globally.<sup>3</sup>

**Figure 2. The five factors that will drive recovery**



Source: Deloitte Research

1 Deloitte, "COVID-19: Likely case scenarios for Indian economy", April 2020, Deloitte India, COVID-19, <https://www2.deloitte.com/content/dam/Deloitte/in/Documents/tax/in-tax-covid19-likely-case-scenarios-for-indian-economy-noexp.pdf>

2 World Health Organisation, COVID-19, Questions and Answers, [http://www.emro.who.int/health-topics/corona-virus/questions-and-answers.html#:~:text=There%20is%20no%20specific%20treatment,can%20be%20highly%20effective.](http://www.emro.who.int/health-topics/corona-virus/questions-and-answers.html#:~:text=There%20is%20no%20specific%20treatment,can%20be%20highly%20effective.;); and

Scott Stump, 'Coronavirus vaccine by January is 'doable,' Dr. Anthony Fauci says', Today, April 30, 2020, <https://www.today.com/health/coronavirus-vaccine-january-doable-dr-anthony-fauci-says-t180358>

3 IBID, <https://www.today.com/health/coronavirus-vaccine-january-doable-dr-anthony-fauci-says-t180358>

b. **Government's policy stimulus measures** – In this rapidly evolving crisis, governments around the world are working on short-term and long-term responses. They are announcing a wide range of health, tax, financial, business, and social measures to help people and businesses respond to and recover from the impact of COVID-19. The extent and effectiveness of the measures will determine the economic revival, as nations prepare to move towards a new normal on the other side of the pandemic.

c. **The secondary industry impact** – A few sectors, such as hospitality and manufacturing, felt the immediate impact of the virus as people stopped availing certain services, and supply chains were disrupted worldwide due to movement restrictions. As economies staggeringly open up, there has been an immediate increase in activities—factories are coming back to life, workers are resuming work, and shops are opening up. However, it is unlikely that industrial activity and capacity building will suddenly bounce back to pre-crisis levels as long as there are uncertainties around the following:

- The possibility of several outbreaks
- The secondary impact of supply-chain disruptions spilling across industries
- The impact on productivity due to business defaults, job losses, and business transformations
- The stress on the financial sector leading to slow credit growth

d. **The demand recovery** – This pandemic has created an unprecedented shock to both supply as well as demand, equally and simultaneously. As the virus continues to spread rapidly, consumers are taking precautions before engaging in activities that require social interaction. The rural demand may hold up for some time because of better rainfall and government support to employment in rural

areas. However, urban demand may impact the demand for more discretionary goods, such as automobiles. Urban consumers are likely to save more in anticipation of economic distress and job losses.<sup>4</sup> Low demand for big-ticket items will likely prevent businesses from incurring capital spends expecting lesser sales of goods, in addition to the shortage of labour (due to reverse migration), creating a vicious circle of low demand and supply.

The global economic growth and trade will influence domestic demand as well. A coordinated effort to curb the infection spread will translate into a synchronised recovery across the world. However, there is less evidence suggesting harmonised efforts in curbing the spread. Different countries are at different stages of the infection. The emerging nations are behind the advanced nations in terms of the infection spread and its economic impact. The possibility of several outbreaks may only make it harder for a coordinated effort, thereby, delaying the recovery process.

- e. **Peoples' perception and trust** (toward the disease, the economy, and their finances) – In addition to the contagion of the virus, there is another contagion—caution and fear (amongst economic players that may modify their behaviour).<sup>5</sup> Caution arises due to the perception people have about the following:
- The virus and its spread
  - How the governments and businesses are serving their needs and safeguarding their space and information
  - The economic outlook and its implication on their financial security<sup>6</sup>

**Caution amongst consumers may change the consumption behaviour and demand patterns, while businesses may modify business practices, leading to rapid automation, reshoring, or just-in-time inventory management.**

4 Deloitte, Deloitte state of consumer tracker, <https://www2.deloitte.com/us/en/insights/industry/retail-distribution/consumer-behavior-trends-state-of-the-consumer-tracker.html>

5 Joshua M Epstien, "Are we already missing the next pandemic?", Politico, March 31, <https://www.politico.com/news/magazine/2020/03/31/coronavirus-america-fear-contagion-can-we-handle-it-157711>; and Austan Goolsbee and Chad Syverson, "Fear, lockdown, and diversion: Comparing drivers of pandemic economic decline 2020", June 2020, Working paper, University of Chicago, [https://bfi.uchicago.edu/wp-content/uploads/BFI\\_WP\\_202080v2.pdf](https://bfi.uchicago.edu/wp-content/uploads/BFI_WP_202080v2.pdf)

6 Dr. Daniel Bachman, "The US economic forecast, Q2 2020, Deloitte, <https://www2.deloitte.com/us/en/insights/economy/us-economic-forecast-united-states-outlook-analysis.html>

# Scenario outlook for India

To assess the possible path to recovery, we made several assumptions with respect to the five factors to get to four possible scenarios (Figure 3 mentions a summary of these). Each set of assumptions are incorporated into our forecast model based on the Global Economic Model by Oxford

Economics<sup>7</sup> to create four economic results, ranging from a moderate economic impact with gradual recovery (most likely case) to severe economic damage with sluggish recovery (extreme worst case with low likelihood).

**Figure 3. Underlying assumptions behind the Indian economic forecast**

	<b>Scenario 1: Recovery cushioned by policy stimulus of 10.5 percent of GDP in FY2021 (Most likely)</b>	<b>Scenario 2: Slower recovery with limited policy stimulus in FY2021 (Mid case)</b>	<b>Scenario 3: W-shaped recovery post several infection outbreaks, with policy stimulus for two years (Worst case)</b>	<b>Scenario 4: Sluggish recovery post several infection outbreaks, with limited policy stimulus in FY2022 (Extreme worst case)</b>
<b>Description</b>	<ul style="list-style-type: none"> <li>Low possibility of several outbreaks</li> <li>Curve flattens globally by 2020 end</li> <li>Deep recession in the US</li> <li>China rebounds back sooner</li> <li>Movement restrictions in India lasts through 2020</li> <li>Government stimulus of 10.5% of GDP in FY2021</li> </ul>	<ul style="list-style-type: none"> <li>Same as Scenario 1</li> <li>Limited fiscal stimulus in FY2021</li> </ul>	<ul style="list-style-type: none"> <li>Several outbreaks worldwide</li> <li>Global containment by late 2021</li> <li>India reaches peak for the first wave by Q3 FY2021, but is hit by the second wave in Q4 FY2021</li> <li>Movement restrictions in India through 2021-2022</li> <li>Government stimulus of 10.5 percent of GDP in FY2021 and FY2022</li> </ul>	<ul style="list-style-type: none"> <li>Same as Scenario 3</li> <li>Government stimulus of 10.5 percent of GDP in FY2021 but limited stimulus in FY2022</li> </ul>
<b>Medical advances</b>	<ul style="list-style-type: none"> <li>Some progress in treatment and drugs available that prevents the disease from progressing or reduces the recovery time</li> <li>Vaccine is available not before April 2021</li> </ul>	<ul style="list-style-type: none"> <li>Same as Scenario 1</li> </ul>	<ul style="list-style-type: none"> <li>Treatment and drugs remain largely ineffective to larger population</li> <li>Vaccine is available not before 2022</li> </ul>	<ul style="list-style-type: none"> <li>Same as Scenario 3</li> </ul>
<b>Industry impact (Supply Side)</b>	<ul style="list-style-type: none"> <li>Deep production cuts in EU/US leading to supply chain disruptions</li> <li>Disruptions multiplies across sectors</li> <li>Capacity constraints due to social distancing norms, cut back in investments, labour shortages</li> <li>Multiple industries, especially SMEs, hurt leading to defaults and adding stress to financial markets</li> <li>Impact on productivity remains muted</li> </ul>	<ul style="list-style-type: none"> <li>Same as Scenario 1</li> </ul>	<ul style="list-style-type: none"> <li>Severe breakdown of supply chains worldwide</li> <li>Several SMEs shut down</li> <li>Government bails out numerous industries</li> <li>More government involvement in the economy, industry</li> <li>Several small banks liquidate; RBI's balance sheets deteriorate</li> <li>Productivity falls worldwide</li> <li>New low-level production capacity in industries</li> </ul>	<ul style="list-style-type: none"> <li>Same as Scenario 3</li> </ul>

<sup>7</sup> Global economic model by Oxford Economics is an econometric platform that is used to provide projections for macroeconomic variables. The platform provides the facilities for several economies, including India.

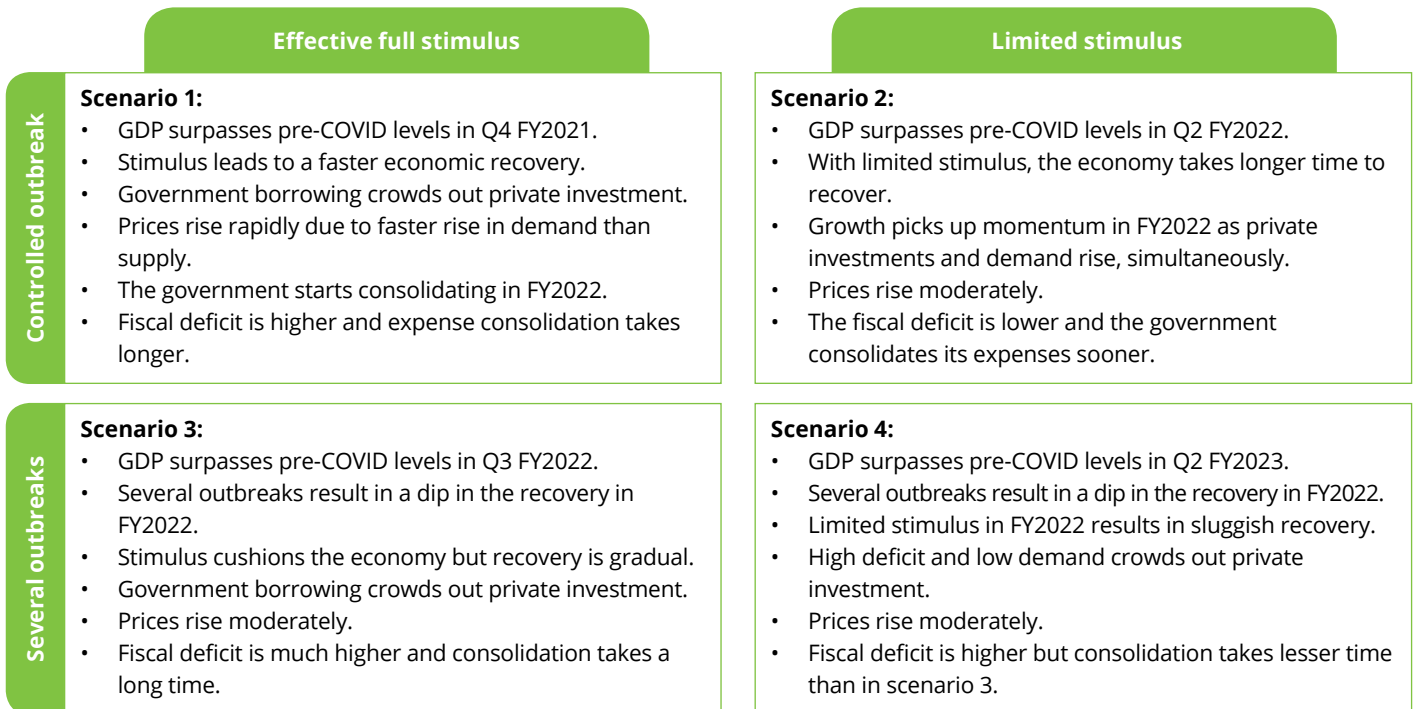
	<b>Scenario 1: Recovery cushioned by policy stimulus of 10.5 percent of GDP in FY2021 (Most likely)</b>	<b>Scenario 2: Slower recovery with limited policy stimulus in FY2021 (Mid case)</b>	<b>Scenario 3: W-shaped recovery post several infection outbreaks, with policy stimulus for two years (Worst case)</b>	<b>Scenario 4: Sluggish recovery post several infection outbreaks, with limited policy stimulus in FY2022 (Extreme worst case)</b>
<b>Policy measures</b>	<ul style="list-style-type: none"> <li>Effective implementation of Atmanirbhar Bharat package that plugs a fiscal and monetary stimulus of 10.5 percent of GDP in FY2021</li> </ul>	<ul style="list-style-type: none"> <li>Automatic stabilisers with a limited effective Atmanirbhar Bharat stimulus</li> </ul>	<ul style="list-style-type: none"> <li>Additional announcements with a fiscal and monetary stimulus of 11 percent of GDP in FY2021 and even higher stimulus in FY2022</li> </ul>	<ul style="list-style-type: none"> <li>10.5 percent of GDP stimulus in FY2021, but limited continued policy support in FY2022</li> </ul>
<b>Demand recovery</b>	<ul style="list-style-type: none"> <li>Sharp decline in demand in EU/US</li> <li>High unemployment, household debt, lengthier lockdowns impact consumer spending</li> <li>Consumers put off big-ticket purchases, such as automobiles and home renovations</li> </ul>	<ul style="list-style-type: none"> <li>Same as Scenario 1</li> </ul>	<ul style="list-style-type: none"> <li>Severe global recession for two years</li> <li>High unemployment, increased household debt leading to social unrest</li> <li>Demand continues at less than potential levels</li> </ul>	<ul style="list-style-type: none"> <li>Same as Scenario 3</li> </ul>
<b>People's perception and trust</b>	<ul style="list-style-type: none"> <li>Uncertainties about the disease, the economy, and their own finances heightens and keeps consumers mildly anxious</li> <li>No significant reshoring activities</li> </ul>	<ul style="list-style-type: none"> <li>Uncertainties about the disease, the economy, and their own finances increases anxiety</li> </ul>	<ul style="list-style-type: none"> <li>Complete lack of trust leading to heightened consumer and investor anxieties</li> <li>Significant reshoring activities</li> </ul>	<ul style="list-style-type: none"> <li>Same as Scenario 3</li> </ul>
<b>Sustainable recovery begins from</b>	<ul style="list-style-type: none"> <li>Q4 FY2021</li> </ul>	<ul style="list-style-type: none"> <li>Q2 FY2022</li> </ul>	<ul style="list-style-type: none"> <li>Q3 FY2022</li> </ul>	<ul style="list-style-type: none"> <li>Q2 FY2023</li> </ul>

Source: Deloitte Research



The possible outcomes of these four scenarios are summarised in Figure 4. The extent of the outbreak (controlled versus several), influenced by medical advances, will likely determine whether the economy will bounce back quickly or keep stumbling with every outbreak. The size and effectiveness of the policy stimulus, both fiscal and monetary, will ascertain how much of the economic demand, supply, and sentiments is cushioned by the impact of the pandemic.

**Figure 4. The possible outcomes of the four scenarios**



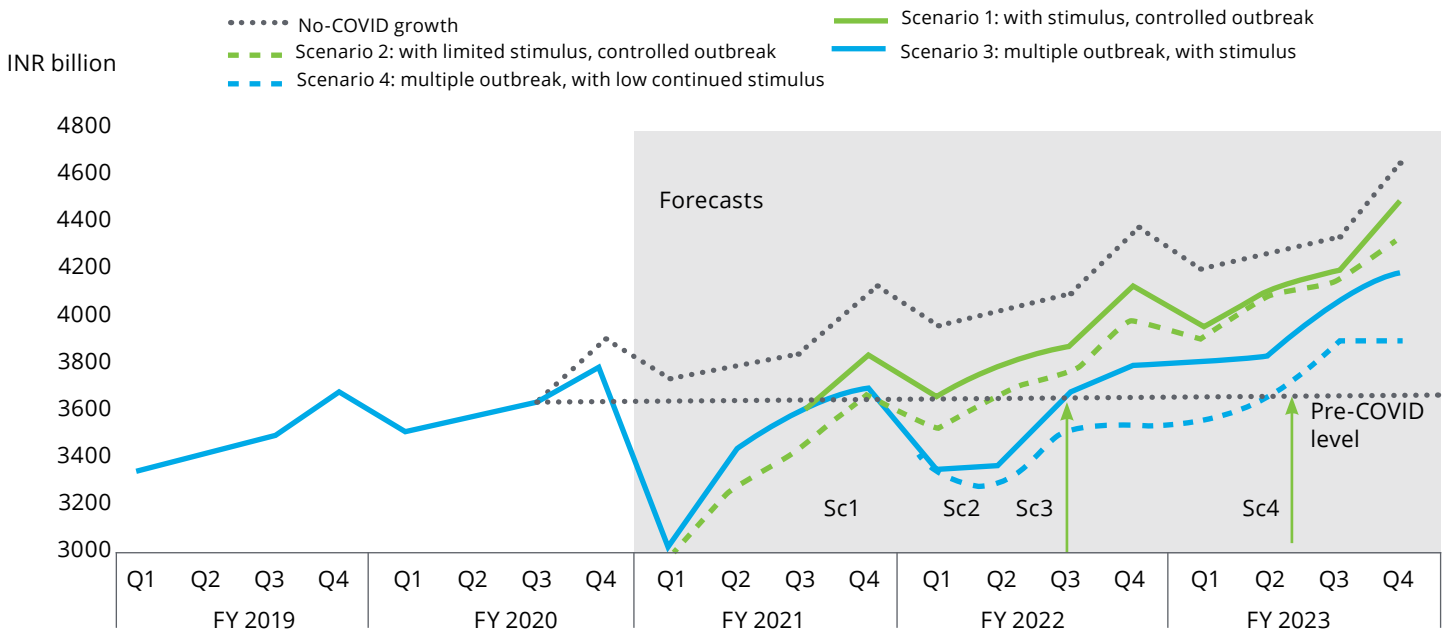
Source: Deloitte Research





**Gross Domestic Product (GDP):** The forecast model suggests that even under the most likely scenario (Scenario 1), the absolute value of real GDP may cross the GDP level of the Q4 of FY2020 almost after a year (Figure 5). **In other words, recovery will not get underway until the start of FY2022. The real GDP is likely to be at a substantially lower level than the pre-COVID trend** (the dotted line) as seen in Figure 5. Under the most likely scenario (Scenario 1), the real GDP level will likely be at least 4 percent below the pre-COVID trend at the end of the three-year outlook.

**Figure 5: Real GDP under four scenarios**



Source: Central statistics office, India; Deloitte Research



**Consumer spending:** Due to the restrictions on movements, social interactions, and consumers' fear of contracting the infection, consumer spending collapsed post the first lockdown. While spending on essential items grew at a healthy pace (as people stockpiled household items, groceries, and medicines) spending on discretionary goods (such as automobile purchase) and hospitality services (such as travel and restaurants) were pushed out for a future date.

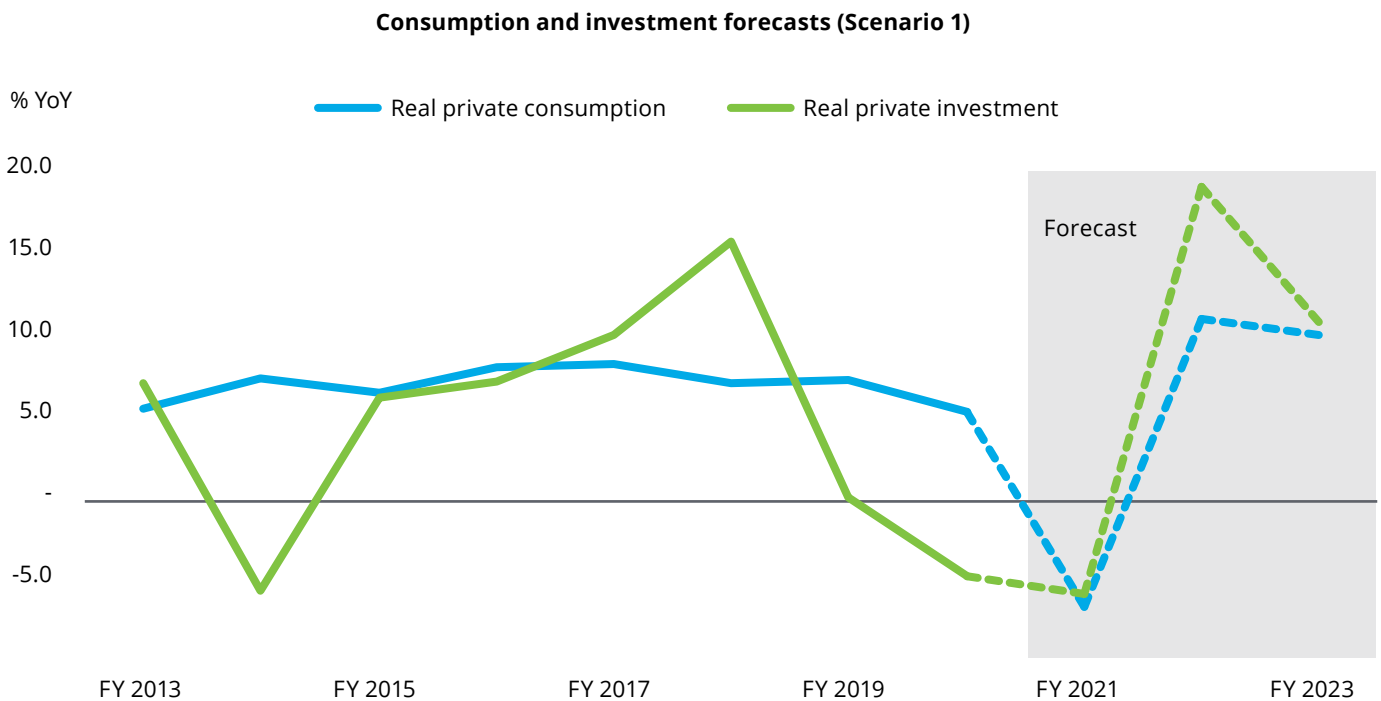
Today, as the lockdown is being lifted partially and consumer sentiments are gradually improving, the rising number of infections will likely influence the spending decisions of consumers in the coming months. Discretionary purchases are likely to get postponed as consumers are worried about their ability to meet short-term and long-term obligations and their future purchasing power. With financial and economic uncertainties here to stay, demand will likely decline for

most of the FY2021. Once the infection spread is perceived to be under control (as assumed in Scenario 1), the consumer spending may gain strength in FY2022 due to pent-up demand (Figure 6).

**Business investment:** Even before the COVID-19 pandemic, private investment has been declining for a while. The slowdown in the economic activity for eight consecutive quarters took a toll on business sentiments and investment decisions. Consequently, in FY2020, private investment contracted by -4.3 percent year-over-year.

Post COVID-19, the trend of contracting investment will likely get amplified because of uncertainties around the demand for goods, operational disruptions, capacity required to meet the demand, and credit availability. The forecast assumes that business spending will contract in FY2021 and recover once demand picks up sustainably (Figure 6).

**Figure 6. Two key drivers of growth are likely to remain sluggish in FY2021**



Source: Central statistics office, India; Deloitte Research

**Prices:** On the one hand, the supply chain disruptions (post the lockdown of the economy to contain the spread of the infection) are likely to raise prices due to supply shortages it creates (even as industrial activity picks up post the easing of restrictions). On the other hand, job losses, movement restrictions, and low demand for discretionary goods are likely to keep prices low. The relative strength of these two opposing factors will determine the direction of the price movement.

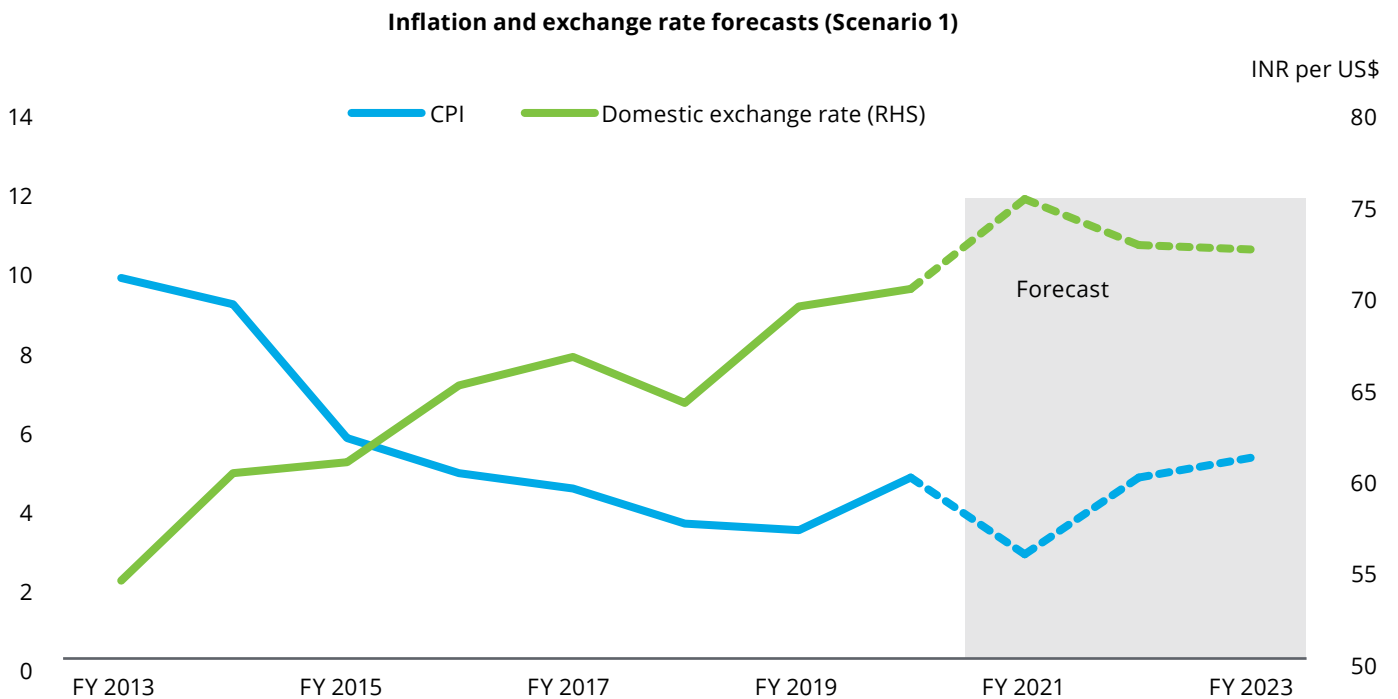
Recent data suggests that while the supply side is limping back up, the demand side remains highly uncertain which will likely keep prices low. Consequently, core prices have eased in recent months, although food prices have remained high. With a good rainfall this monsoon, the pressure on food prices will likely ease as well. Therefore, we expect overall prices to decline in the next few quarters (Figure 7).

However, **once the recovery begins under the most likely scenario (Scenario 1), prices will escalate faster. This is because pent-up demand backed by high government spending will cause demand to overshoot supply.**

**Exchange rate:** Indian rupee has been under pressure, as global sentiments remain weak. The domestic currency has depreciated sharply against the US Dollar, which in turn, has appreciated because of safe-haven flows after the pandemic led to a sharp decline in global economic activity and high volatility in the global financial market. India experienced a strong capital outflow (similar to other emerging nations) on fears that growth in India is likely to suffer as well. After a steep depreciation, the rupee has gained some ground and has been recovering.

However, the fear of slow global recovery and the rising number of infections, together with the escalating tensions between the US and China are likely to keep the dollar strong and the domestic currency vulnerable in FY2021 (Figure 7). If India rebounds sustainably by early FY2022, as forecasted in Scenario 1, revival in capital inflows and better investor sentiments will strengthen the rupee.

**Figure 7. Inflation may rise post recovery, as the economy gets overheated; rupee will likely strengthen in FY2021**



Source: Central statistics office, India; Deloitte Research

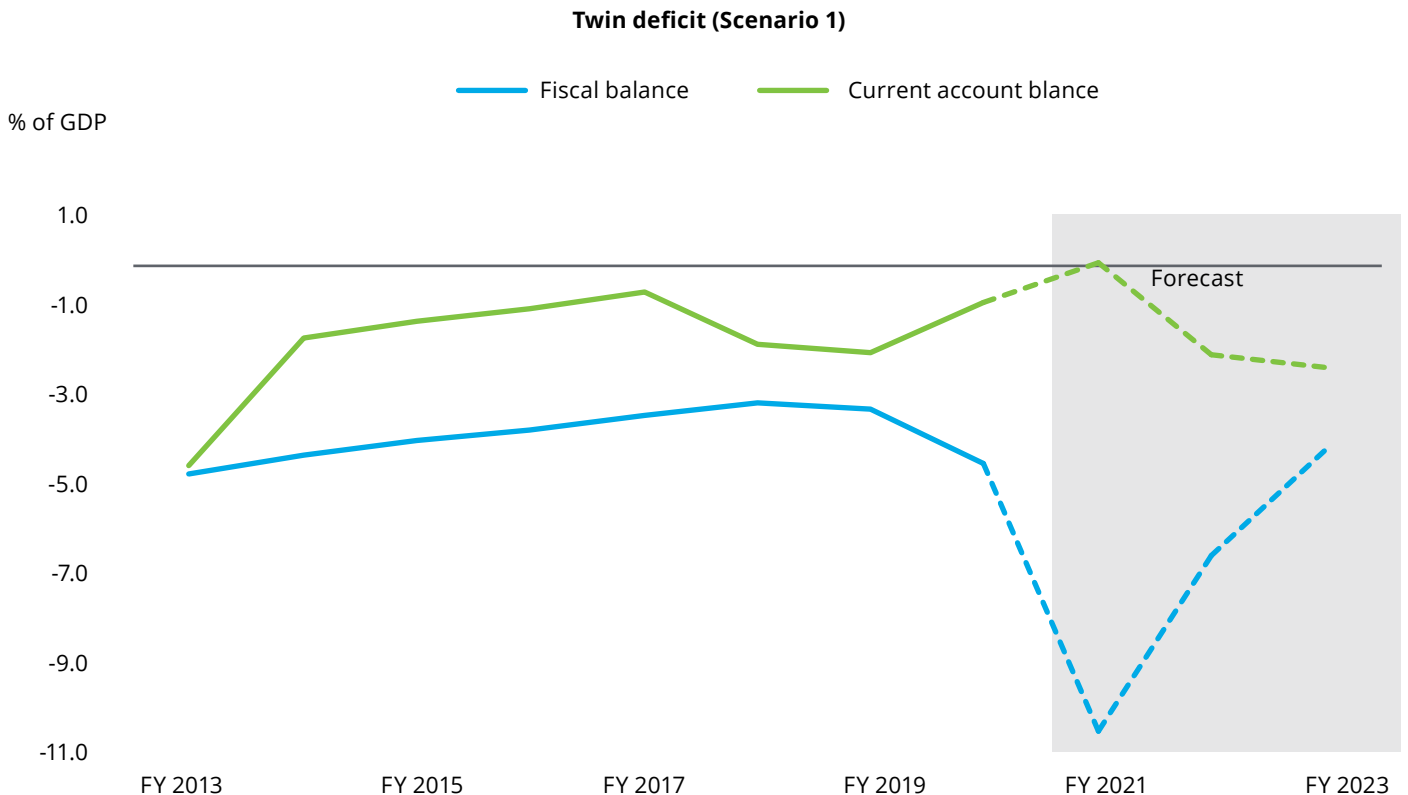
**Government spending:** To tackle such an unprecedented situation, the Indian Government announced a fiscal and monetary package of 10.5 percent of GDP, including direct transfers to the vulnerable section of the population, easing liquidity in the market, and addressing a mix of short-term and long-term challenges through reforms. If the entire amount is utilised effectively in FY2021, as assumed in Scenario 1, the additional government spending, together with a fall in tax revenue due to low GDP, will likely result in the fiscal deficit exceeding the target rate in FY2021 (Figure 8).

**Foreign trade:** In 2019, global trade remained muted because of uncertainties around the US-China trade relations and fear around reverse globalisation, as evident from the falling share of exports in global GDP.<sup>8</sup> India witnessed a decline in both

exports and imports, with the latter falling faster than the former due to the sustained economic slowdown. A fall in the merchandise trade deficit, along with an increase in services trade surplus and income receipts from abroad, drove the improvement in the current account in the fourth quarter.

Due to the COVID-19 pandemic, world trade is set to plummet between 13 percent and 32 percent in 2020, as predicted by the WTO.<sup>9</sup> This would translate into low exports in India. However, imports are likely to fall faster because of poor domestic demand, rupee depreciation, and low crude oil prices. Overall, the current account may turn positive in FY2021 (Figure 8). With an economic bounce-back in FY2022 (Scenario 1), higher domestic demand will likely cause imports to rise faster, pushing the current account back to the negative territory.

**Figure 8. Fiscal deficit may spike because of low tax revenues and higher government spending; current account may turn positive in FY2021**



Source: Central statistics office, India; Deloitte Research

<sup>8</sup> DG Azevêdo, "Trade set to plunge as COVID-19 pandemic upends global economy", World Trade Organisation, April 2020, [https://www.wto.org/english/news\\_e/pres20\\_e/pr855\\_e.htm](https://www.wto.org/english/news_e/pres20_e/pr855_e.htm)including India.

<sup>9</sup> IBID



# What can the industries infer from these scenarios?

The emerging trends of lead and lagged high-frequency indicators since the onset of COVID-19 suggest that the impact on the economy has been quite hard. Not only has the economic activity fallen off the cliff, but the reversal also looks slow and irregular. It is confusing for industries to chart their way ahead under these extreme uncertainties.

This article suggests the four possible ways in which the economy may recover based on four sets of underlying assumptions. The economic consequences under each scenario will likely have several implications on different industries and their path to recovery.

We are optimistic about the outlook and foresee a scenario (with a greater probability) where the infection spread is

controlled and the Indian government is able to cushion the economy's decline. India is expected to gradually, but steadily, rebound back in FY2022. A quick economic recovery will likely have a moderate impact across all industries and may lead to a relatively uniform revival, with a few bouncing back sooner than others.

Other scenarios may have completely different outcomes for different industries. **If the pandemic prolongs, essential goods segment of retail, the pharmaceutical industry, and the technology and communication industry will likely weather the storm in due course of time.** However, the hospitality and banking industry may continue to see difficult times ahead. Industries must prepare themselves for uncertain times, while hoping for the best.



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