Ministry Of External Affairs
Government Of India

ECONOMIC DIPLOMACY & STATES DIVISION

MONTHLY ECONOMIC REPORT

AUGUST 2020

CONTENTS

STATE OF THE ECONOMY

The COVID-19 pandemic has adversely affected every single economy across the globe, with its repercussions being visible in every sector. In a country as densely populated and vast as India, the Government of India had no option but to enforce a nation-wide lockdown in March 2020, to curb the spread of the virus . The lockdown resulted in a sharp contraction in the economy in the April – June quarter, but also ensured that the pandemic induced death rate in India has been among the lowest in the world. However, in the July-September quarter , with gradual unlocking of the economy, India has witnessed a V-shaped recovery, the proof of which is evident in its micro-economic indicators including auto sales, tractor sales, fertilizer sales, railway freight traffic, steel consumption and production, cement production, power consumption, e-way bills, GST revenue collection, daily toll collections on highways, retail financial transactions, manufacturing PMI (purchasing managers' index), performance of core industries, capital inflows and exports.

As India emerges from this crisis, it is pivotal to concentrate on the calibrated reconstruction of the economy and to cultivate resilience for any uncertainty in the near future. Some areas that may require specific attention include agrarian supply chains, factor markets, infrastructure, ICT, start-ups, financial inclusion, skilling, and health care. Progress in these areas will sustainably boost economic growth in years to come.

IMPACT OF LOCKDOWN:

Economies all over the world have contracted during the April-June quarter, due to the pandemic-imposed lockdown. Advanced economies of countries like the US, UK, Canada, Japan, France etc. have also suffered in varying proportions. The US economy has contracted by 9.1%, UK, France, Spain, Italy and Germany by 21.7%, 18.9%, 22.1%, 17.7% and 11.3% respectively with the overall Euro area contracting by 15% and Japan contracting by 9.9%. Relative to these advanced nations, India's GDP contraction at 23.9% is slightly higher.

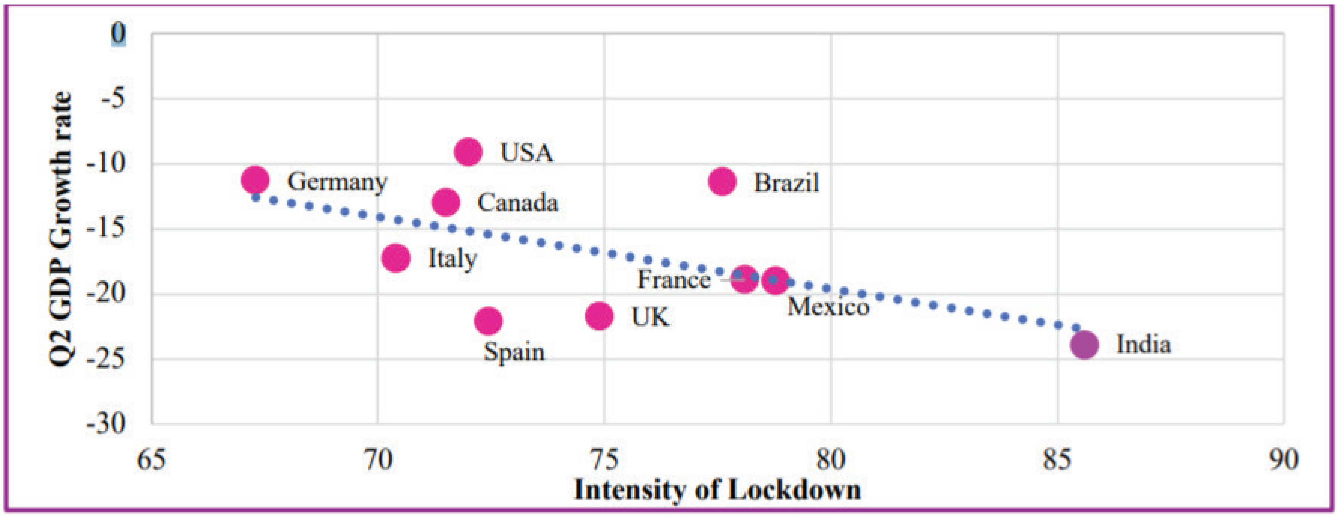


Fig 1. GDP contraction in various economies

To curb the spread of the disease, the Government of India enforced one of the most stringent lockdowns in April, which continued for two months. With the economy brought to a complete halt its contraction was inevitable. This contraction, in the months of April and May was followed by a slight recovery in June, as the country unlocked in the second quarter.

The lockdown period gave some respite to ramp up the health and testing infrastructure in the country. Due to timely tracing, treatment and reporting, the number of people recovering from the virus is continuously rising and the active cases are 21% of the total cases in the country. This has enabled India to restrain pandemic induced death rate to one of the lowest in the world. India's case fatality rate was at 1.78% as of 31st August,`2020 as compared to 3.04% in the US, 12.35% in the UK, 10.09% in France, 1.89% in Japan and 13.18% in Italy.

With India unlocking, the worst seems to be behind us as high-frequency indicators show an improvement from the month of June from the unprecedented trough the economy had hit. Economic data indicates a growing convergence with previous year's activity levels on several indicators. Broad-based resurgent growth in several high-frequency indicators such as PMI Manufacturing, eight core, E-way bills, Kharif sowing, power consumption, railway freight, cargo traffic and passenger vehicle sales bodes well for prospects of growth recovery.

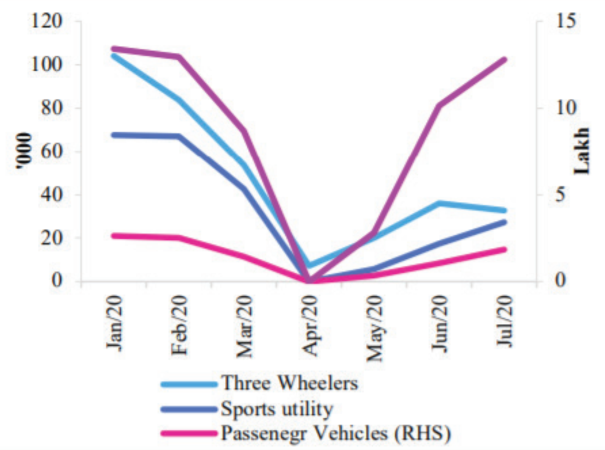
Estimates released by the Ministry of Statistics and Programme Implementation showed that India's Gross Domestic Product (GDP) growth rate had contracted by 23.9% for the April to June quarter in FY 2020-21. In Gross Value Added (GVA) terms, the economy had contracted by 22.8%. On the demand side, private consumption spending fell by 26.7%. On the GVA side, the decline was broad-based with the deepest fall of 50.3% experienced in construction followed by services like trade, hotels, transport and communication, manufacturing, and mining. Agriculture emerged as the bright spot with a healthy growth rate of 3.4%.

HIGH-FREQUENCY INDICATORS OF ECONOMIC RECOVERY:

With the gradual unlocking of the economy in July 2020, the second quarter saw a V-shaped recovery, which was evident in its high-frequency indicators, few of which are given below:

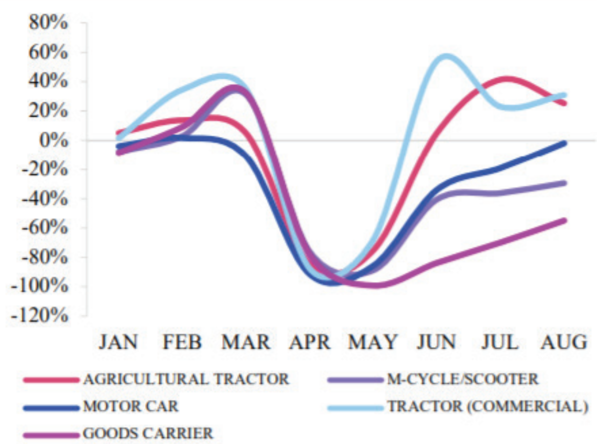
1. **Rural Demand:** After the gradual unlocking of the economy, there has been a rise in the sales of the passenger vehicles, like small cars, two-wheelers, and SUVs in July, making it nearly the same as last year's figures. Another indicator of a boost in rural demand, is the increase in sale of fertilizers and registrations for commercial and agricultural tractors.

Figure 2: Auto Sales



Source: IHS Markit

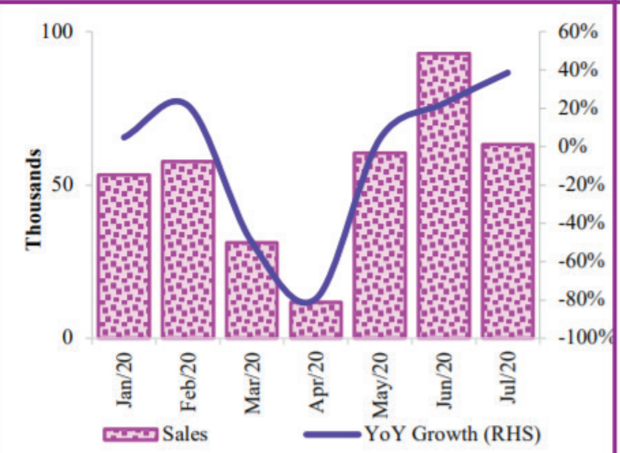
Figure 3: Growth in Vehicle Registration



Source: SIAM

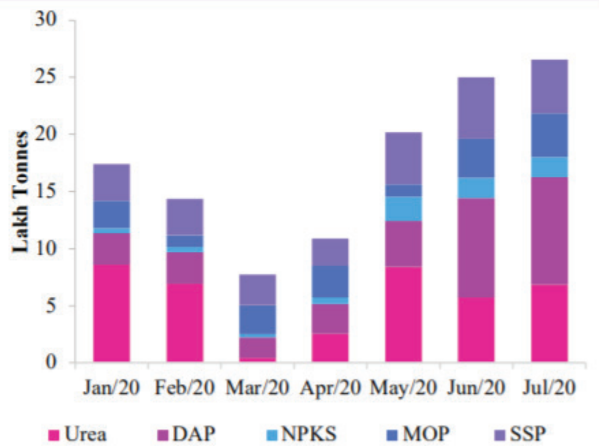
Figure 4: Strengthening prospects of rural demand

Tractor Sales



Source: Tractor and Mechanization Association

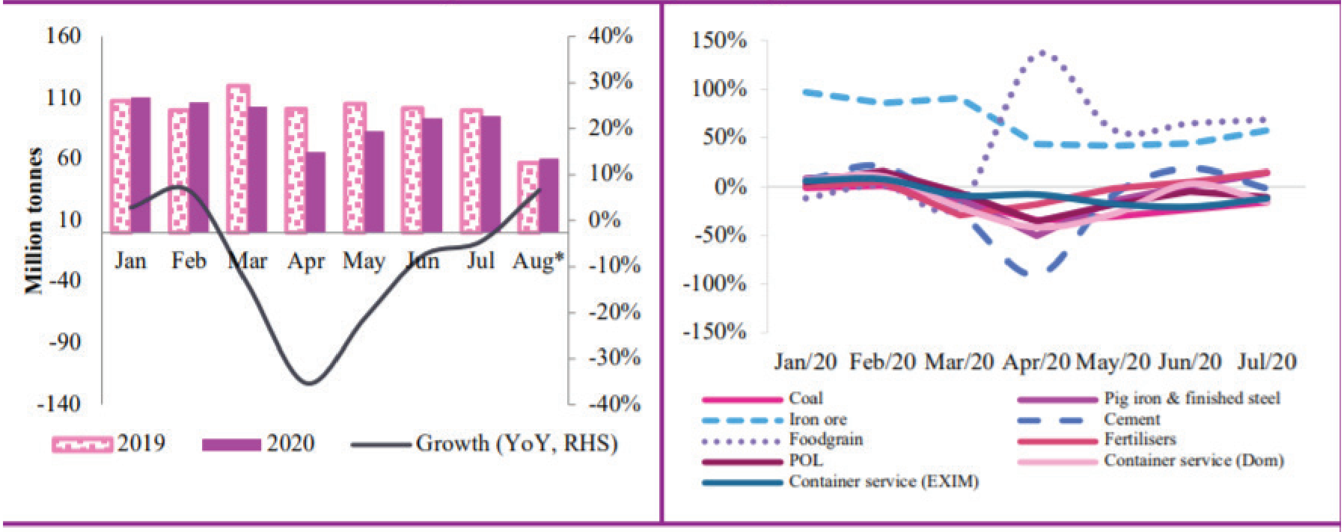
Fertilizer Sales



Source: Department of Fertilizers

2. **Railway Freight Traffic:** A recovery in railway freight traffic was seen, driven by the movement of steel, iron ore export, coal, food-grains, fertilizers, and EXIM container services. However, there was a decline in the growth of cement, petroleum products, and domestic container services. There has been an increase in the number of railway bookings in the months of July and August, particularly in the Northern Zone and sub-urban regions of Central and Western zones.

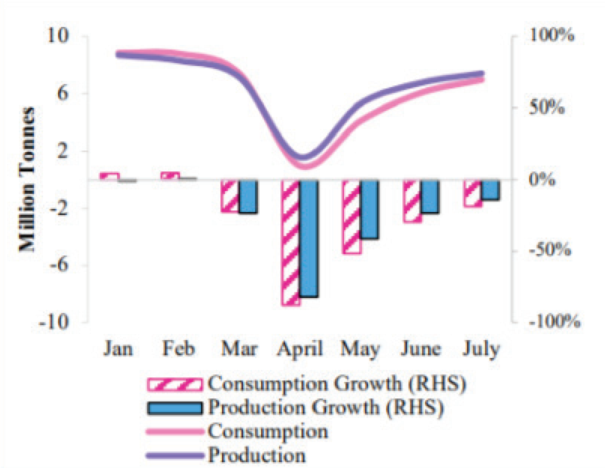
Figure 5: Railway Freight Traffic



Source: Ministry of Railways, Data till 20th August

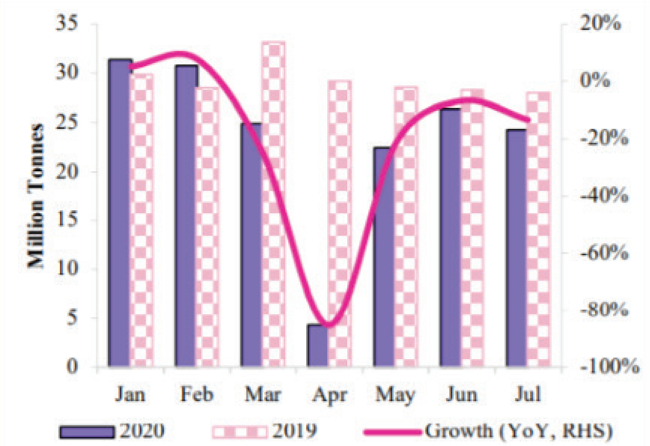
3. **Steel Sector:** The steel sector saw a V-shaped recovery in July, as construction activity has picked up pace, which erased most of the contractions that happened in April.

Figure 6: Steel Consumption & Production



Source: Joint Plant Committee, M/o Steel

Figure 7: Cement Production



Source: DPIIT, Ministry of Commerce

4. **Power consumption, E-bills & Toll collections reverted to baseline:** The consumption of power seems to be reverting to last year's levels, reaching 97% of previous levels in August 2020. The continuous generation of E-bills is a strong indicator of revenue collections, supply chain corrections and logistics growth, which augurs well for economic normalcy. In terms of value, e-way bills generated reached Rs. 13.8 trillion in August (97.2% of last year's value). Toll collections on highways have also picked up a significant pace in the last three months, reaching 85% of pre-COVID (February) levels in August. However, the re-imposition of local lockdowns and flood situations in some states, brought another halt and interrupted the recovery in the first half of July.

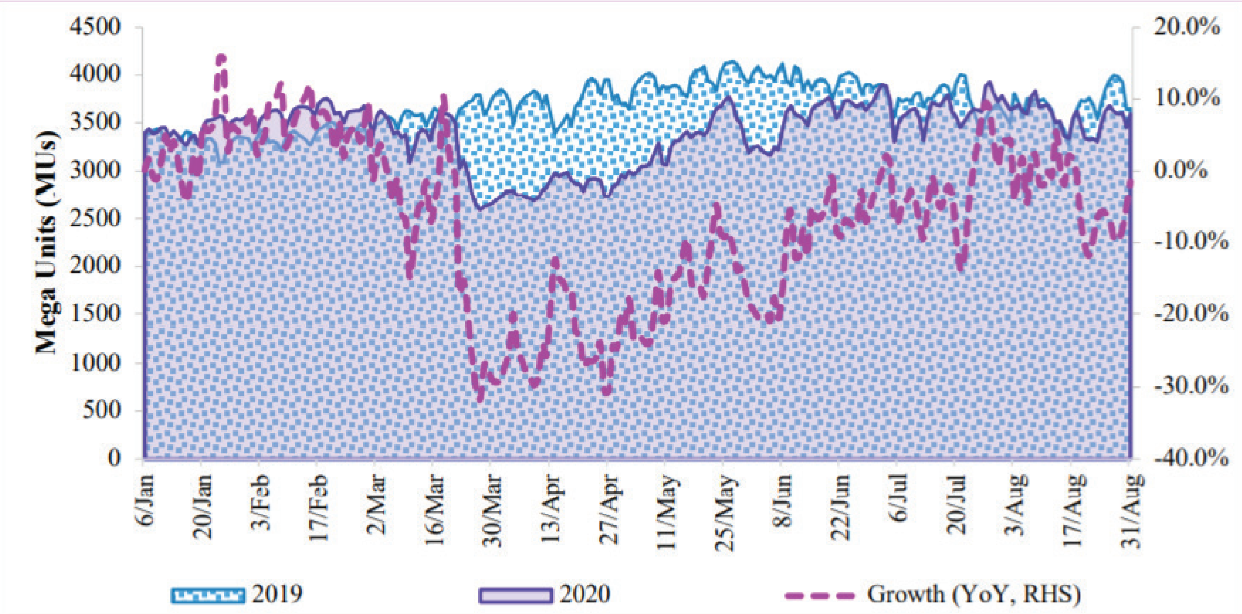


Fig. Power Consumption

5. **Increased digital transactions, UPI payments & broadband services:** An optimistic scenario is emerging for digital retail transactions, UPI payments and broadband services growth. With the unlocking of the economy, the logistics sector saw some movement, which brought an increase in e-retail. As a result, retail payment transactions via NPCI platforms bounced back in June and July, after the dip during the lockdown months of April and May. UPI payment transactions hit an all-time high of Rs. 2.9 trillion in value and 1.5 billion in volume terms in the month of July. Broadband subscriber base also grew in May after dipping in April.

Figure 12: NPCI Retail Financial Transactions

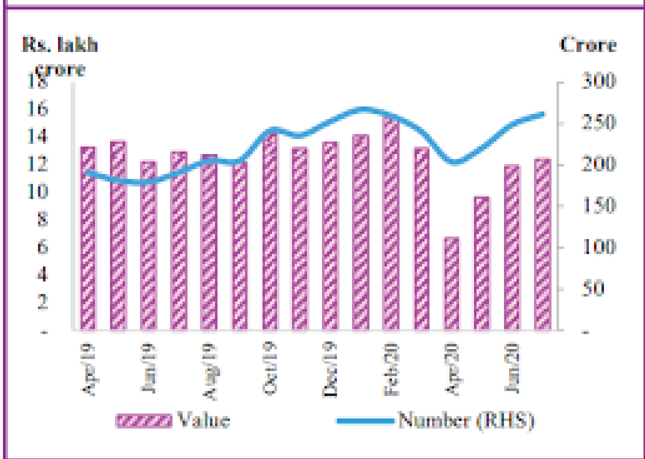
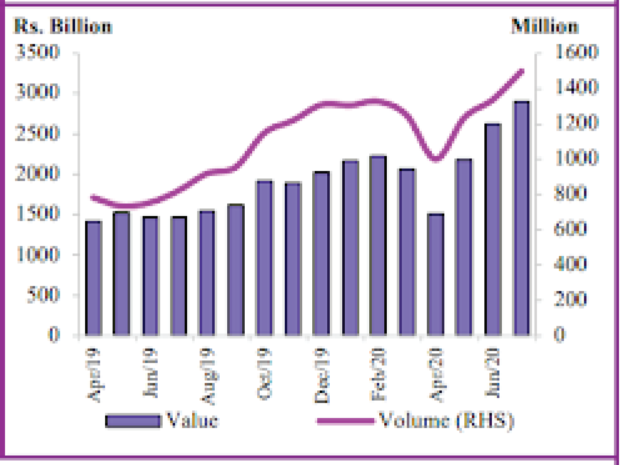


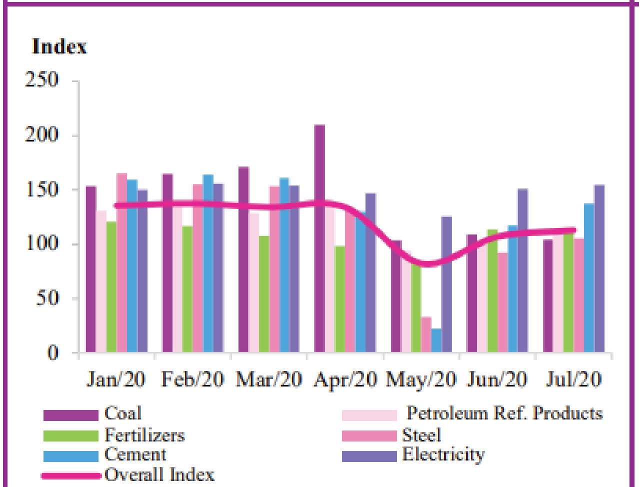
Figure 13: UPI Payment Transactions



Source: NPCI

6. **Industrial production:** Industrial production is deemed as the engine of growth for any economy. In the April to June quarter, the industrial production in India saw a decline of 38.1%. This however started improving gradually towards the close of the quarter. Consumer non-durables output sharply turned around to double digit growth, likely driven by release of pent-up demand and rebuilding of inventories. Contraction in consumer durables, capital goods and infrastructure output also significantly eased. This was further augmented in July with contraction in core industries output easing to 9.6 % in July as compared to 12.9% in June.

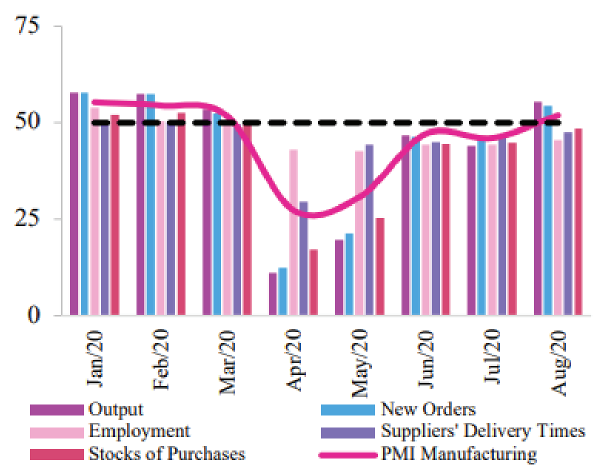
Figure 14: Core Industries Performance



Source: DPIIT

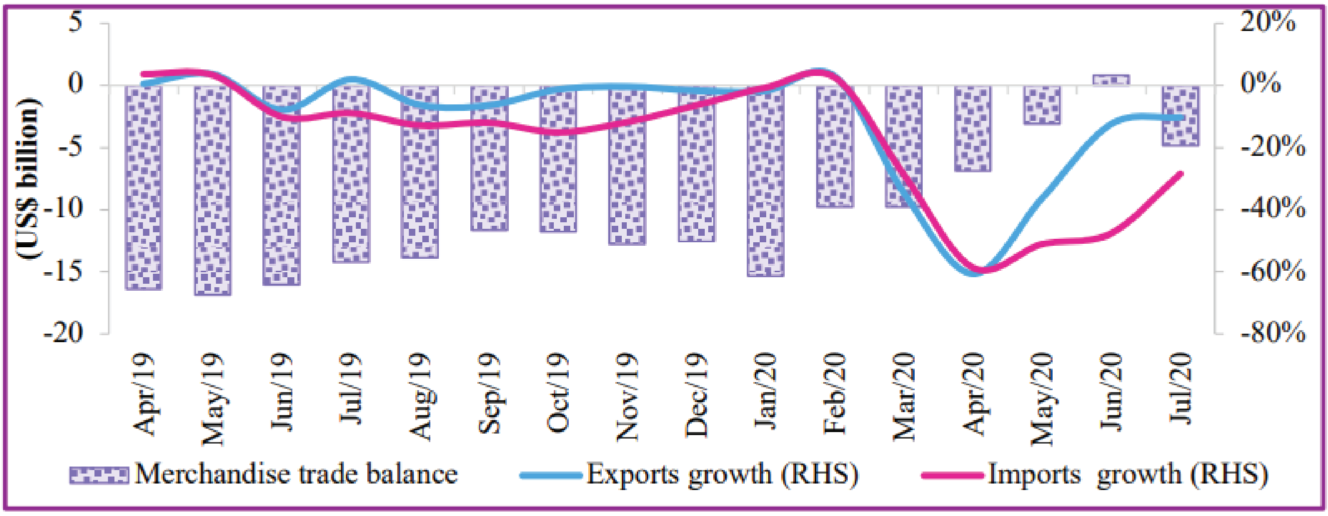
7. Manufacturing Purchasing Managers' Index (PMI): This indicator, after a slight decline in July, expanded in August for the first time since lockdown presenting optimistic recovery prospects for the manufacturing sector. This is in line with the recovery in global activity for the first time in six months. With the gradual recovery of the global economy, business optimism also recovered globally to its highest in the past 15 months during July, inching closer to its pre-pandemic level. The global manufacturing index reached a twenty-one-month high of 51.8 in August.

Figure 15: PMI Manufacturing

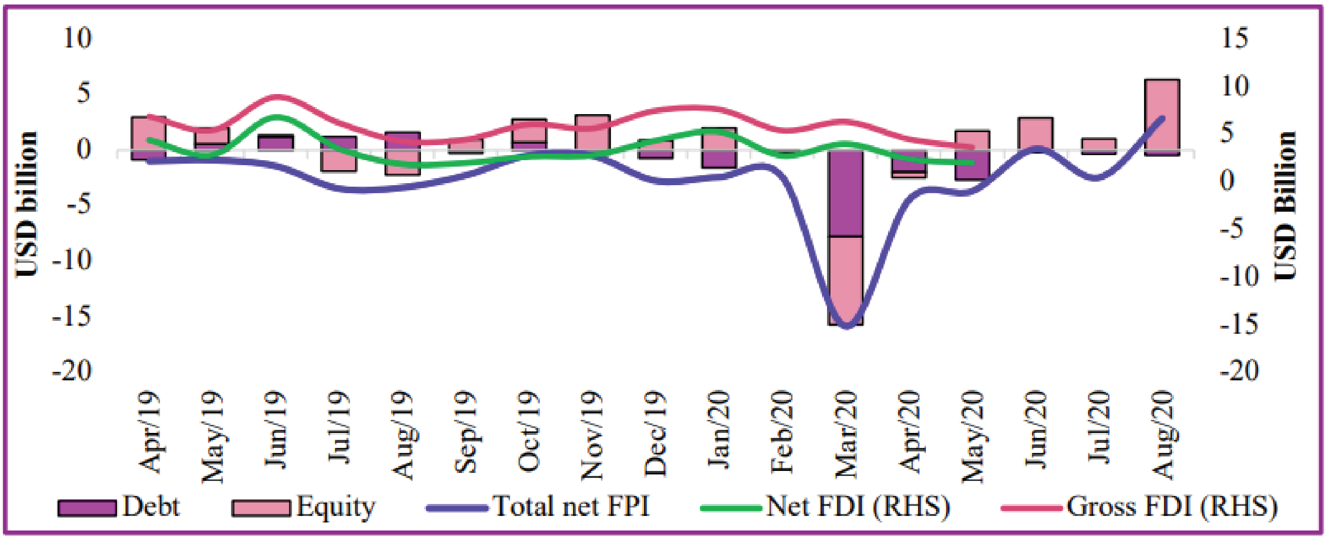


Source: IHS Markit

8. **Exports are recovering faster than imports:** India's export sector remains resilient. Merchandise exports witnessed broad-based rebound in the last three months, inching closer to pre-Covid levels in July. Exports of food items and pharmaceutical products showed increasing momentum in July owing to higher global demand of these essential products. Recovery in imports, however, remained relatively less uniform in July, suggestive of weak domestic demand for certain items.



9. **Increase in FDI and FPIs:** Net foreign direct investment (FDI) moderated to US$ 4.4 billion in April-May 2020 from US$ 7.2 billion a year ago. On the other hand, India garnered the highest foreign portfolio inflows in the first half of 2020 compared to its emerging market peers. This optimistic foreign investor sentiment continued in July and August when the selling spree in debt markets also reversed, further boosting market confidence.



The trend in the above given micro-economic indicators establish that India is well on its path to a V-shaped recovery. Residual uncertainty persists because of the effect created by the pandemic on the precautionary motive to save which sharply affects the demand for discretionary goods and services. Unlike previous crises that originated from economic factors, the uncertainty in the current crisis stems from health factors originating from the pandemic. The arrival of the COVID vaccine would signal the end of this uncertainty and bring back discretionary consumption to pre-COVID levels.

DOMESTIC MACRO-ECONOMIC REVIEW

Agricultural sector: The agriculture sector, supported by a healthy south-west monsoon, has been the single most resilient and fulfilling sector, through this global crisis. This year, the cumulative monsoon rainfall was 9.2 per cent above the long-period average (LPA), which bodes well for the kharif crops. Kharif harvest in the third quarter contributes to almost one-third of the GVA in agriculture in India. A bumper kharif harvest will, therefore, provide the much-needed boost to GDP in the year 2020-21.

Modest Resumption in Services: PMI services index have improved in August to 41.8 over 34.2 in July. Movement of other high frequency indicators of services sector activity also suggest modest resumption of economic activity.

Cargo traffic & Aviation activity on an upward trajectory: Cargo traffic volumes also bounced back appreciably in July with iron ore, fertilizers, coal (thermal and steel) and containerised cargo driving the improvement. With festivals around the corner, domestic civil aviation activity is also increasing, which may further boost economic growth.

Oscillating recovery in oil markets: Global oil markets continued to remain vulnerable to risks of prolonged second wave of COVID-19 pandemic. Crude oil prices recovery remained volatile in August with easing OPEC+ supply cuts, dim demand, and weather concerns in US markets. India's crude oil price rose only moderately from US$ 42.98 per barrel as on 31 July to US$ 44.41 per barrel as on 31 August. India's consumption of petroleum products was dampened by 3.7%.

Government consumption demand provides necessary pandemic proofing: Government consumption spending has provided a measure of relief, with central government's revenue expenditure, net of interest payments and major subsidies, having risen by 33.7 % in Q1 of 2020. The interruption in economic activity due to COVID-19 has led to a shortfall in revenue collections. Net tax revenue collections stood at 12.4% of Budget Estimates compared to 20.5% in the corresponding period of previous year. Personal Income Tax collections up-to July end amounted to Rs. 0.91 trillion, compared to Rs. 1.29 trillion in the corresponding period of previous year.

Credit for agriculture, large industry, and Micro & Small Enterprises (MSE) improved: Demand in credit from banks was dampened during FY 2019-20, growing at 6.1% y-o-y in a sharp loss of pace from 13.3% a year ago. Regional lockdowns and the consequent slowing of the economic cycle has added to weak credit demand. The increased demand in MSME credit in June may be attributed to the Emergency Credit Line Guarantee Scheme announced in May under the Rs. 20 trillion Atmanirbhar package of the Government. As on 12 August, 32.8% of the committed amount under the scheme has been disbursed in 2.27 million MSME loan accounts. 55.4%of the disbursement came from 12 public sector banks and the remaining from 24 private banks and 31 NBFCs.

Corporate results- Resilient and stressed sectors: Corporate results of Q1 2020-21 show that sectors like Pharma, FMCG and Fertilizers showed growth in revenue, operating profit, and improvement in margins. Some sectors like Cement, Cement Products and Mining also reported margin improvement over Q1 2019-20, despite a decline in revenue. The pervasive impact of COVID-19 may be seen in the broad-based rating downgrades across sectors in Q1 2020-21. Major sectors that opted for relief under moratorium on loan servicing include Metal, Power, Real Estate, Textile, Construction etc. However, some sectors like Pharma and FMCG, though not under stress opted for relief under moratorium due to uncertainty, to conserve money during such a state of economic downturn.

POLICY PRIORITIES AS INDIA UNLOCKS

As India emerges from this crisis, it is crucial to re-orient the policy matrix towards a progressive reconstruction of the economy, in order to build resilience in an ambiguous world. Some policy changes have been taken up on priority are given below:

Enhancing resilience of India's agriculture, building efficient and sustainable agrarian supply chains: Agriculture has emerged pliable and resilient in the current scenario. Aiming towards building a more efficient and sustainable economy, certain changes in policies have been reinforced. The government has announced a plethora of landmark reforms to facilitate the deregulation and liberalisation of the agricultural sector.

Deepening structural reforms in factor market and boosting infrastructure to reignite manufacturing: The fundamental change in the world order also calls for development in the approach on efficiency versus resilience of the manufacturing sector. Deep-seated and wide-ranging structural reforms in land, legal, labour and capital markets to reverse the slowdown in manufacturing are essential. The government has also provided significant impetus to mega infrastructure projects as part of the National Infrastructure Pipeline to reignite the manufacturing sector. The recent MSME related reforms to build an Atmanirbhar Bharat plays a vital role in the evolution of India's manufacturing sector.

Leveraging ICT and start-ups for reconstructing a resilient and innovative services sector: The services sector is the worst-hit during the pandemic times. Being the largest employer in the nation, it is pivotal to build sufficient flexibility for service organisations for the duration of the pandemic response, which will aid in India's economic recovery. Influencing India's ICT revolution and upscaling Digital India at an unparalleled pace is essential to the service sector.

Strengthening AtmaNirbhar's Bharat position in global value chains: Re-aligning policy incentives, will also strengthen India's position in emerging global value chains amid changing trade dynamics. In addition, India needs to secure its strengths in generic drugs and pharmaceuticals exports and regain its market share in active pharmaceutical ingredients (APIs). India can pioneer easy, affordable, and equitable access to the COVID-19 vaccine as and when it is available to administer.

Harnessing digital finance: The digital payment infrastructure created as part of JAM trinity (Jan-Dhan Aadhar Mobile) has enabled a timely and targeted fiscal relief response to the pandemic. Going forward, wide-spread distribution of online and offline digital payment infrastructure, will leash the true potential of financial inclusion in an increasingly digitised new era. Amidst this paradigm shift, expanding the digital retail space will help in regaining the pre-COVID-19 consumption momentum.

Skilling, upskilling and re-skilling for preparedness against labour market shocks: The pandemic has caused several unprecedented job losses. To deal with the same, it is essential to change structurally the employer-employee relationship. Skilling, upskilling and reskilling of the labour force is fundamental in enabling a more prepared and flexible business environment.

Preventive health care ecosystem for resilience against COVID-19: 56. India's multi-faceted health response to the COVID-19 crisis ranging from social distancing to aggressive test-track-treat strategies has provided a necessary platform to prevent any further wide-spread disease. Rigorous efforts towards building a preventive health care ecosystem will also provide the much-needed stimulus to economic activity by creating more employment and mitigating labour productivity losses.

For more information:

Ministry of Finance, Department of Economic Affairs

[MONTHLY ECONOMIC REPORT AUGUST 2020]