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The COVID 19 Pandemic and its Global Economic Implications

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The recent manoeuvres by the Indian government to caution markets from opportunistic Chinese investors, is one among the many measures taken by governments worldwide, to take control of the post pandemic economic outlook. The ramifications of the highly contagious virus have already sent the global economy into a tailspin, with early signs worldwide indicating contraction in the economy. Preliminary estimates do little to comfort the situation. The International Labour Organization for instance, estimates that 25 million jobs will be lost worldwide with losses in labour income amounting to USD 860 billion to USD 3.4 trillion. And the United Nations Conference on Trade and Development has pitched global losses to the tune of 9 trillion dollars[1]. If adequate fiscal responses are not taken, the global economy could contract upwards of 3 per cent due to the pandemic[2]. As businesses continue to bleed due to sharp losses in revenue, widespread unemployment would result. This is not helped by the fact that even before the onslaught of the pandemic, the global economic output was on a decline and a recession had not been ruled out.

In light of this, it is important to take stock of vulnerable sectors of the economy and prepare for an economic slowdown, post the health emergency.

Potential Areas of Concern

Businesses and Developing Countries

The WTO forecast expects all regions except Africa, West Asia and the Commonwealth of Independent States to incur double digit decline in exports in their 'optimistic' outlook and are confident of the slump and its repercussions being far worse than the 2008 financial crisis.

Restrictions on movement have seen a severe crunch in labour supply, transport and travel and this is particularly worrying for developing countries which are replete with labour intensive industries. To make things more difficult, risk aversion among investors has led to a sudden stoppage in capital flows to emerging markets. Demand from high income countries, for goods and raw materials has decreased drastically, thus affecting manufacturing industries in developing countries. UNCTAD projects that developing countries would collectively lose USD 800 billion in export revenue in 2020.

Among the most affected sectors, are tourism and travel related industries, hotels, restaurants, consumer electronics, financial markets and transportation. The countries most vulnerable to an economic downslide are those who are deeply interconnected with China, particularly South Korea, Japan and Australia. Developing countries are projected to take the biggest hit, due to the prevalence of low social protection and a high proportion of job losses amongst migrant workers. Further, the restrictive measures taken by advanced economies have already started impacting less developed countries due to lower trade and investment.

Businesses in the last few weeks have seen a need to re-invent and re-configure themselves in real time. Several have opted to modify their supply chains and turn into manufacturers of PPE and ventilators, while small local restaurants have turned themselves into retailers. However, the space for such manoeuvrability is low and most businesses face severe crunches.

For instance, IT firms which play a major role in the Indian economy, may also face a lot of stress as a major portion of their businesses come from Europe and North American countries. Further, trade in services, in which India has a high global share as an exporter[3], maybe severely affected by transport and travel curbs.

Governments and Crisis Management

Governments worldwide are likely to increase spending, in order to restart and keep afloat their economies. This would significantly involve bailing out banks and firms and thus cutting down on productive spending, due to limited revenue sources. Foreign portfolio outflows would further result in depreciation of local currencies, thus increasing the cost of servicing dollar denominated debt. UNCTAD pegs the net debt and equity outflows to USD 59 billion since February. The Indian government may face the better end of the stick in this regard, since most of its borrowings are in rupee denominated debt. However, nearly 80 countries have already approached the IMF for assistance, including Pakistan.

Stimulus packages have been announced by governments worldwide, including the $22.5 billion package announced by the Finance Minister for the Indian economy. Japan, South Korea and Italy have announced similar stimulus packages in light of the situation. This puts a certain amount of liquidity back into the market.

However, care must be taken that the incentives do not benefit those who are already well capitalized. The burden of the slowdown has been taken on disproportionately by the unorganized workforces across the world. This comprises casual, self employed and daily wage workers who live hand to mouth. There have been talks in academic circles of an EBI or Emergency Basic Income, as opposed to a UBI or Universal Basic Income, to keep the economy afloat, in order to claw its way out of the recession.

Banking Sector

Central banks across the world have announced rate cuts to put more money in the hands of people. India's measures in this regard have been attentive to the crisis at hand. The RBI recently reduced its repo rate to 4.75%. This does not mean much for businesses in the short run, as they cannot plan for the future amidst the crisis and will be cautious of borrowing or scaling up their operations, considering the demand slowdown. However, this move was aimed to benefit the government as it has reduced the government's borrowing cost and hence altered the fiscal deficit calculation. Further, a lower repo rate may have the overall effect of reducing interest rates in the system and allowing entrepreneurs or households to take loans for working capital or homes and vehicles in the medium term.

Before the onslaught of the crisis, the banking sector in India was already stretched thin with the collapse of IL&FS, DHFL and Yes Bank. The RBI's moratorium on loan repayments[4] as well as measures to increase primary liquidity[5] with banks is a means to cushion cash flow pressures for firms and individuals.

Oil Prices

Crude oil has also been caught in the diminishing demand spiral. The downward pressure on the demand for commodities has impacted oil prices, which have been on a low since the beginning of the year. The negative supply shock has come from a reduction in labour force, travel restrictions, and capital while the fall in demand has taken place due to global and regional pressures.

This could however, bode well for countries like India as they have a chance to soften their current account deficit by lowering its import bill. India could also use this opportunity to shore up its strategic reserves.

Agricultural Sector

FAO has warned the international community about a shift in the supply and demand for food. World agricultural prices are likely to increase due to stockpiling by households of staples like wheat and rice, as well as restrictions on exports by food exporting countries like Vietnam and Thailand.

Agriculture is the bread and butter for close to 47% of the Indian population. The restrictions imposed have left close to 30 million agricultural labourers who live by their daily income, out of work. This is magnified by the fact that India lacks farm mechanisation, with almost 60% of the farm activities still being manually executed.

In recent weeks, although there has been an increase in the retail prices of fruits and vegetables by 20-30%, there has been a simultaneous crash in wholesale prices of the same, by 15-20%. The increase in prices is largely due to logistics mismanagement, but the fall in income for the farmer is due to lack of procurement by buyers and subsequent post-harvest losses. Immediate measures need to be taken to support farmers in their time of need.

The Way Ahead

The Economic Intelligence Unit's (EIU) Uncertainty Index pitches the COVID 19 crisis as the pandemic with the most amount of uncertainty as compared to crises like SARS, Ebola or the Avian Flu. This sums up why it is so difficult to chart out a crisis management strategy to combat the fallouts of the disease. The crisis is unique in the sense that it is multi-dimensional; it is a global health crisis and an economic crisis rolled into one. Further, it involves a demand and a supply side shock. Sustained periods of low demand and weak supply can lead to structural unemployment, declining capital stock as well as conservative approaches to markets.

Something that has become apparent in the course of the pandemic is the lack of global leadership provided to counter a crisis of this magnitude. In particular, the WHO has seen a severe dent in its credibility due to accusations levelled against it by the US, as well its delayed and overcautious response to the pandemic. Efforts to quell the virus have lacked a global consensus and have varied in the degree of seriousness exhibited by countries in dealing with the crisis. This throws an open challenge to multilateral institutions to re-invent themselves to stay relevant in changing times. There is a need to have co-ordinated action on this front as most of the potential risk points will start to flare up over the next few months, when global lockdowns loosen. UN-DESA has estimated the need for a global effort amounting to as much as 10 per cent of the global GDP, to tide over the effects of the crisis.

In the short term, we need to leverage both public and private resources, while providing logistical support to farmers to move their produce to the markets. Lenient and flexible loan repayment timelines also need to be made in order to allow firms and individuals to stay afloat.

In the long run however, more fundamental changes need to be looked at. Leveraging automation and AI in supply chains would help create long term resilience in future situations. Healthcare expenditure must also be progressively augmented much beyond the current 1.28% of the GDP[6], in order to combat future calamities such as this. Projections imply that the global economic recovery will not take place till 2021, which puts a greater onus on governments and multilateral institutions to make this transition as swiftly as possible.

(Disclaimer: The views and opinions expressed in this article are those of the author and do not necessarily reflect the position of the Centre for Air Power Studies [CAPS])

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Notes

[1]IMF projections. http://www.china.org.cn/business/2020-04/15/content_75934841.htm

[2] IMF Economist Gita Gopinath states that the global economy could lose 9 trillion dollars due to coronavirus. https://www.businesstoday.in/current/economy-politics/international-monetary-fund-gita-gopinath-warns-global-economy-can-lose-usd-9-trillion-due-to-coronavirus/story/401121.html

[3] India's contribution is $214 million or 3.5% of the global export, as of 2019.

[4] RBI permitted banks a three month moratorium on loan repayments.

[5] RBI has reduced the Cash Reserve Ratio to 3%, thus freeing up 1.37 trillion rupees for banks to lend.

[6] Figures cited in National Health Profile Data 2019