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COVID-19 and Its Impact on the Indian Economy

Devendra Kumar Verma*

Ph.D. Scholar, Department of Agricultural Economics and Management, Rajasthan College of Agriculture, MPUAT, Udaipur-313001, Rajasthan, India

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*Corresponding Author
Devendra Kumar Verma*

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INTRODUCTION

We are in the middle of a global Covid-19 pandemic, which is inflicting two kinds of shocks on countries: a health shock and an economic shock. Given the nature of the disease which is highly contagious, the ways to contain the spread include policy actions such as imposition of social distancing, self-isolation at home, closure of institutions, and public facilities, restrictions on mobility and even lock-down of an entire country. These actions can potentially lead to dire consequences for economies around the world. In other words, effective containment of the disease requires the economy of a country to stop its normal functioning. This has triggered fears of a deep and prolonged global recession. On April 9, the chief of International Monetary Fund, Kristalina Georgieva said that the year 2020 could see the worst global economic fallout since the Great Depression in the 1930s, with over 170 countries likely to experience negative per capita GDP growth due to the raging coronavirus pandemic.

Impact of the crisis

Overall macro impact

The countrywide lockdown has brought nearly all economic activities to an abrupt halt. The disruption of demand and supply forces are likely to continue even after the lockdown is lifted. It will take time for the economy to return to a normal state and even then social distancing measures will continue for as long as the health shock plays out. Hence demand is unlikely to get restored in the next several months, especially demand for non-essential goods and services. Three major components of aggregate demand-consumption, investment, and exports are likely to stay subdued for a prolonged period of time.

In addition to the unprecedented collapse in demand, widespread supply chain disruptions will continue for a while due to the unavailability of raw materials, exodus of millions of migrant workers from urban areas, slowing global trade, and shipment and travel related restrictions imposed by nearly all affected countries. The supply chains are unlikely to normalise for some time to come.

Agriculture and Rural Activities

The agriculture sector is critical as large number of workers and the entire country's population are dependent on this sector. The performance of agriculture is also key to the state of rural demand. In the preCovid-19 period, agricultural GDP experienced an average growth rate of 3.3% per year in the six-year period 2014-15 to 2019-20 with intermittent fluctuations22. The provisional estimates of the National Statistical Office (NSO) show that GDP growth in agriculture has increased from 2.4% in FY19 to 4% in FY20. It was also relatively better at 3.5% in Q3 of FY20. However, the terms of trade have moved against agriculture during 2016-17 to 2018-19 due to bumper crop and horticultural production which caused a decline in food prices. Terms of trade for agriculture seems to have improved in 2019-20 as the nominal agricultural GDP growth was 11.4% as compared to real growth of 4%.

Informal sector

India has a very high share of informal employment in total employment. The share, which includes agricultural workers, has declined marginally from 94% in 2004-05 to 91% in 2017-18. Out of a total of 465 million workers, 422 million were informal workers in 2017-18. Even in non-farm sector (manufacturing and services), the share of informal workers was around 84% in the same year. There are significant inequalities between informal and formal sector workers. The informal/unorganised workers do not have access to any social security benefits and also face uncertainty of work. Out of the total workers, the shares of self-employed, casual and regular workers respectively were 51.3%, 23.3%, and 23.4%. Most of the self-employed and casual employees are informal workers.

Financial markets and institutions

As the ramifications of the health shock and the repercussions of the country-wide lockdown become clear with each passing day, the risk aversion of the banking system will get significantly aggravated. As more and more firms struggle to stay afloat and are unable to repay their dues amidst the massive demand and supply disruptions, corporate delinquencies will go up and the level of NPAs in the already fragile banking system will increase precipitously. Moody’s Investors Service has already changed the outlook for the Indian banking system to negative from stable, as it expects deterioration in banks’ asset quality due to disruption in economic activity.

What kind of policy support is needed?

The immediate objective of the policy responses to the economic impact of Covid-19 is to ameliorate the effect of the shock on economic agents in both the formal and the informal sectors and to help them tide over the crisis. Against the background of a weak economy, the twin shocks of Covid-19 and lockdown are operating at two levels:

- Creating supply-side disruptions
- Triggering reduction in aggregate demand
- Mass exodus of migrant workers from urban areas: Many firms will not be able to find the required number of workers, and hence production will be constrained even if they do not face a demand shortage. This will be acute in sectors such as construction, logistics (last-mile delivery of goods), unskilled manufacturing, etc., where large number of migrant workers are employed.
- Restrictions on international trade: The pandemic has disrupted global supply chains. To the extent that international transport of

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goods is adversely affected, importing firms will face supply constraints.

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