1. Dressing a Wounded Economy

Context:

- The Impact of the Corana virus pandemic is now felt by almost every country. First, there are the health effects of the virus, and second is the economic impact of the various actions that have to be taken to combat the virus.

The Economic Impact on India:

- The Economic Impact can be traced through **Four Channels:**
  1. External demand;
  2. Domestic demand
  3. Supply disruptions
  4. Financial market disturbances

External, Domestic Demand

- The economies of the developed countries slow down, their demand for imports of goods will go down and this will affect our exports which are even now not doing well.
- Not only merchandise exports but also service exports will suffer. Besides these, the IT industry, travel, transport and hotel industries will be affected.
- The only redeeming feature in the external sector is the fall in oil prices. India's oil import bill will come down substantially.
- But this will affect adversely the oil exporting countries which absorb Indian labour. Remittances may slow down.

Supply Disruptions:

- Supply disruptions can occur because of the inability to import or procure inputs.
- The break in supply chains can be severe. It is estimated that nearly 60% of our imports is in the category of 'intermediate goods'.
- Imports from countries which are affected by the virus can be a source of concern.
- Domestic supply chain can also be affected as the inter-State movement of goods has also slowed down.

Financial Markets Issues:

- The stock market in India has collapsed. The indices are at a three-year low.
- Foreign Portfolio Investors have shown great nervousness and in this process the value of the rupee in terms of dollar has also fallen.

- The stock market decline has a wealth affect and will have an impact on the behaviour of particularly high wealth holders.

How to Deal the Situation?

- The two major tools that are available are monetary policy and fiscal actions.
- **Monetary Policy:**
  - ✓ Monetary policy in a situation like this can only act to stimulate demand by a greater push of liquidity and credit.
  - ✓ The policy rate has already been brought down by 135 basis points over the last several months. Beyond a point, a reduction in interest rates does not work. It is the environment of the overall economy that counts.
  - ✓ The RBI needs to go beyond cutting policy rate. A certain amount of regulatory forbearance is required to make the Banks Lend.
- **Fiscal Policy:**
  - ✓ Even without the pandemic, the fiscal deficit of the Central government will turn out to be higher than that indicated in the budgets
  - ✓ Revenues are likely to go down further because of the virus related slowdown in economic activity. But the virus has to be fought and brought down. All expenditures to test and to take care of patients must be incurred.

The Job Sector:

- Mostly daily-wage earners and non-permanent/temporary employees who have been thrown out of employment is a serious concern.
- In this, the business units to keep even non-permanent workers on their rolls and provide them with a minimal income.
- There is also a thought of government providing cash transfer to individuals.
- Provision of food and other essentials must be made available to the affected as is done at the time of floods or drought.

Conclusion:

- The fiscal deficit is bound to go up substantially. The higher borrowing programme will need the support of the RBI if the interest rate is to be kept low.
- Monetisation of deficit is inevitable. The strong injection of liquidity will store up problems for the next year. Inflation can flare up. The government needs to be mindful of this.

Source: The Hindu