Brickwork Ratings expects economy to contract by 5.5% in 2020-21 due to COVID-19-related challenges

Brickwork Ratings, Mumbai, 02 June 2020: The GDP data released on 29 May by the Ministry of Statistics and Programme Implementation (MOSPI) is disappointing. The fourth quarter GDP is estimated at 3.1%; and with substantial revisions in the estimate for earlier quarters, the full-year growth estimate for fiscal 2020 has been revised downwards to 4.2%, which is the lowest in the last 11 years. The estimates are confusing as much as they are disappointing. First, the substantial revisions make the job of estimation very unpredictable. Second, the trend in quarterly data shows that the economic slowdown has been sharp and steady, indicating that the policy response has not been effective. Third, there was a sharp downturn in the economy even before the COVID-19 crisis, and the lockdown has only exacerbated it. It was only in the last week of March that the lockdown was enforced, and therefore, its impact on the slowdown in the fourth quarter was marginal. Finally, with the economy slowing down in the background, the impact of COVID-19 will be unprecedented, and the economy is likely to record a sharp contraction; as the lockdown will continue in major hubs of economic activity where Coronavirus cases are concentrated, the recovery will be prolonged.

Says Mr. Rajat Bahl, Chief Ratings Officer, Brickwork Ratings, “Economic revival will crucially depend on proactive intervention by the central and state governments, but unfortunately, the stressed fiscal situation of the country limits their ability. The government has announced a Rs 20.97 lakh crore stimulus package, but according to BWR estimates, the fund infusion through fiscal operation is likely to be just around Rs 1.8 lakh crore in the current fiscal”.

Measures to ensure liquidity by pushing banks to lend to MSMEs and NBFCs or by reducing policy rates by the RBI may yield results only in the medium term, and immediate results often require government spend to create demand-side stimulus. Even when MSMEs start operating with the liquidity support provided by banks, bringing back migrant labour (those who moved from urban areas) will pose a serious challenge after the lockdown is lifted.

Says Dr. M Govinda Rao, Chief Economic Advisor, Brickwork Ratings, “With constraints faced on both supply- and demand-sides, resuming economic activities will remain a challenge. Making liquidity available to businesses does not mean that they will avail it. They have to overcome supply chain disruptions and labour shortage besides liquidity concerns. Mounting unemployment issues, financial stress, the dislocation of labour, and collapsing domestic and global demand will place manufacturing under severe stress. The construction sector will suffer from not only the non-availability of labour, but also due to a lack of demand. Sectors such as transport and hotels will show a sharp contraction even after the lockdown is lifted as people will refrain from undertaking travel and tourism. Unfortunately, pessimism pervades on the economic front, and there are no prospects of a V-shaped recovery”.
Agriculture sector growth is likely to be positive with the predictions of a normal monsoon this year, and some growth is likely through the public administration expenditure front. Trade, hotels and transport will be the most adversely affected as people are unlikely to undertake leisure travel for considerable time period. The manufacturing sector also will be badly hit, and after the lockdown is lifted, if these industries are unable to cope with challenges such as supply chain disruptions, labour shortage and new operating guidelines amid the loss of revenue, there could be a substantial contraction in the second and third quarters as well. We could expect only some recovery in the last quarter of this fiscal, taking cues from the government’s measures materialising through a pick-up in credit and an improvement in demand. Of course, the picture can change somewhat if the government decides to pump in fiscal stimulus, but a substantial increase in public spending is unlikely due to resource constraints.

Considering the frequent revisions in the GDP data, which portray a further downward revision for 2019-20, and the agriculture sector being the only bright spot, we expect India’s economy to witness a contraction in GDP at around -5.5% in FY 2020-21 (see Annexure on the next page for details).
The detailed analysis of the impact of lockdown on various sectors of the economy is presented below, along with BWR’s estimates on growth outlook for each sector for the fiscal 2020-21:

Annexure: Expected Impact of Lockdown on the Major Sectors of the Economy and Outlook for 2020-21 (at constant prices)

|------|------------------------------------------|-----------------------------|----------------------|----------------|----------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| I    | Agriculture, forestry and fishing        | 19,48,110                   | 14.6%                | 4.0%           | 3.0%           | ● The rural economy is relatively less impacted by the lockdown, and the prediction of a normal monsoon provides the hope of better farm output.  
● Migrant workers moving from urban to rural areas may prove positive for agriculture as they are more likely to undertake agriculture-related work, and hence, more agricultural land will be utilised for cultivation.  
● Horticulture, poultry, fishing and aquaculture may see some loss due to logistic issues and fall in exports. |
| II   | Industry                                 | 40,15,068                   | 30.2%                | 0.9%           | -6.7%          | The industrial sector may take a long time to recuperate from the damage of production disruption due to the lockdown.                                                                                                                                                  |
|      | Mining and quarrying                     | 3,55,680                    | 2.7%                 | 3.1%           | 1.0%           | ● Mining operations (coking coal, iron ore mining or the production of steel and ferroalloys) remain undisrupted as the central Indian mining states have deployed a slew of legislations to continue mining activities.  
● They come under essential services, which constitute supply-critical raw material for steel making.  
● If there is a lack of demand due to the economic slowdown, generating huge inventories doesn’t make sense, and hence, the sector may see subdued growth. |
|      | Manufacturing                            | 23,17,280                   | 17.4%                | 0.0%           | -10.0%         | ● Restarting manufacturing industries post lockdown is a big challenge as the small and medium industries are likely to face labour shortages in addition to many other operating issues.  
● Many factories were shut completely for at least one month and resumed operations only partially with a 25% capacity.  
● Following instructions by the union home ministry to exercise due precaution and social distancing measures to combat the spread of Covid-19 may be a difficult task for labour-intensive manufacturing companies.  
● With mounting losses due to lower production and demand, the contraction in the manufacturing sector is likely to be huge, and the irony is that they account for a large part of domestic economic activities. |
|      | Electricity, gas, water supply and other utility services | 3,08,832                   | 2.3%                 | 4.1%           | -3.0%          | ● With manufacturing activities at a standstill, electricity consumption contracted significantly in April.  
● Post the lockdown, there may be a resumption in demand, but only gradually.                                                                                                                                                                                  |
|      | Construction                             | 10,33,276                   | 7.8%                 | 1.3%           | -3.0%          | ● The construction sector largely depends on governments spending on infrastructure and real estate business.  
● Capital expenditure is likely to go down this fiscal due to fiscal constraints.  
● Real estate is one of the worst hit sectors, and a delay in project completion, coupled with a demand slowdown, given the fall in income, may halt growth in the sector.                                             |
<table>
<thead>
<tr>
<th>S No</th>
<th>Economic Activity</th>
<th>Amount in Rs crore</th>
<th>Share in GVA</th>
<th>2019-20</th>
<th>2020-21</th>
<th>Assumptions</th>
</tr>
</thead>
<tbody>
<tr>
<td>III</td>
<td>Services</td>
<td>73,37,941</td>
<td>55.2%</td>
<td>5.5%</td>
<td>-6.0%</td>
<td>The services sector is expected to deal with serious financial stress</td>
</tr>
</tbody>
</table>
|      | Trade, hotels, transport, storage and communication | 25,77,945 | 19.4% | 3.6% | -15.0% | • Except telecom services, all other services are severely hit by the pandemic.  
• The suspension of the transportation of non-essential services and complete shutdown of aviation and hospitality since March have created irreversible losses.  
• Above all, people will refrain from undertaking travel and tourism which may take at least a year to get back to normalcy. |
|      | Financial services, real estate and professional services | 29,15,680 | 21.9% | 4.6% | -3.0% | • The digitisation of commerce and business operations has been gathering pace; however, financial services may take time to adapt to new business models.  
• Mounting NPAs and the lack of demand for credit from certain sectors and overall risk aversion among lenders may create serious asset-liability mismatches. |
|      | Public administration, defence and other services | 18,44,316 | 13.9% | 10% | 2.0% | • Government expenditure is likely to continue, given the necessity of the situation.  
• Essential services fall under this; hence, these may continue to witness positive growth. |
|      | Gross Value Added (GVA): I+II+III | 1,33,01,120 | 100% | 3.9% | -4.9% | • Except agriculture, all other sectors are likely to contract from their current levels with virtually no activities happening during the lockdown period since March.  
• Although some sectors may gradually start functioning, the severity of the pandemic is likely to last for a few more months.  
• Hence, we expect a fall in gross value added, considering the first quarter of the current fiscal is showing severe contraction and some revival is expected only in the second half of FY21 |
|      | Gross Domestic Product (GDP) | 1,45,65,951 | 4.2% | -5.5% | Real GVA estimated to decline by -4.9% in 2020-21, and real GDP by -5.5% due to huge losses in net indirect taxes |

Note: Data on GVA and GDP estimates for 2019-20 is provisional and 2020-21 growth estimates is by BWR

Source: MOSPI, CSO and BWR Research
ABOUT BRICKWORK RATINGS

Brickwork Ratings is India’s home-grown credit rating agency built with superior analytical prowess from industry’s most experienced credit analysts, bankers and regulators.
Established in 2007, Brickwork Ratings aims to provide reliable credit ratings by creating new standards for assessing risk and by offering accurate and transparent ratings. Brickwork Ratings provides investors and lenders timely and in-depth research across the Structured Finance, Public Finance, Financial Guaranty, Financial Institutions, Project Finance and Corporate sectors.
Brickwork Ratings has employed over 350 credit analysts and credit market professionals across 8 offices in India. Our experienced analysts have published over 12,000 ratings across asset classes.
Brickwork Ratings is committed to provide the investment community with the products and services needed to make informed investment decisions. Brickwork Ratings is a registered credit rating agency by Securities and Exchange Board of India (SEBI) and a recognised external credit assessment agency (ECAI) by Reserve Bank of India (RBI) to carry out credit ratings in India.
Brickwork Ratings is promoted by Canara Bank, India’s leading public sector bank. More on Canara Bank available at www.canarabank.co.in

DISCLAIMER

Copyright © 2019 by Brickwork Ratings India Pvt Ltd., 3rd Floor, Raj Alkaa Park, 29/3 & 32/2, Bannerghatta Main Rd, Kalena Agrahara, Bengaluru, Karnataka 560076. Telephone: +91 80 4040 9940. Fax: +91 80 4040 9941. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings, Brickwork Ratings relies on factual information it receives from issuers and underwriters and from other sources Brickwork Ratings believes to be credible. Brickwork Ratings conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Brickwork Ratings’ factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Brickwork Ratings’ ratings should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Brickwork Ratings relies on in connection with a rating will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Brickwork Ratings and to the market in offering documents and other reports. In issuing its ratings Brickwork Ratings must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings can be affected by future events or conditions that were not anticipated at the time a rating was issued or affirmed.

THE INFORMATION IN THIS REPORT IS PROVIDED “AS IS” WITHOUT ANY REPRESENTATION OR WARRANTY OF ANY KIND. A Brickwork Ratings rating is an opinion as to the creditworthiness of a security. This opinion is based on established criteria and methodologies that Brickwork Ratings is continuously evaluating and updating. Therefore, ratings are the collective work product of Brickwork Ratings and no individual, or group of individuals, is solely responsible for a rating. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Brickwork Ratings is not engaged in the offer or sale of any security. All Brickwork Ratings reports have shared authorship. Individuals identified in a Brickwork Ratings report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Brickwork Ratings rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time, for any reason in the sole discretion of Brickwork Ratings. Brickwork Ratings does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Neither Brickwork Ratings nor its affiliates, third party providers, as well as their directors, officers, shareholders, employees or agents (collectively, “BWR Reps”) guarantee the accuracy, completeness or adequacy of the Report, and no BWR Reps shall have any liability for any errors, omissions, or interruptions therein, regardless of the cause, or for the results obtained from the use of any part of this publication. In no event shall any BWR Reps be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs) in connection with any use of any part of the Report even if advised of the possibility of such damages. Brickwork Ratings receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities.