

The Indian economy is struggling to recover

Given the pace of vaccination and the virus mutations, it may take a while for the economy to bounce back



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The International Monetary Fund (IMF)'s July version of the World Economic Outlook Update emphasises a dangerous divergence in economic prospects between the advanced countries and emerging economies.

The global economy is projected to grow at 6% in 2021, a figure which is unchanged from the IMF's April forecast. However, this is yet another instance where averages are misleading. While the forecast for advanced countries has been revised upwards, prospects for emerging countries and particularly those in Asia are projected to be somewhat worse.

Quick pace of recovery

This divergence in the pace of recovery from the pandemic is attributed mainly to two factors. First, there has been a huge difference in the pace of vaccine roll-out between the advanced and the emerging and low-income countries. The advanced economies have allocated large sums in procuring COVID-19 vaccines on a priority basis. Even the Trump administration, not known to be one with a human face, was proactive in transferring large sums to several pharmaceutical companies as soon as the magnitude of the global health crisis became apparent. This enabled the companies to develop and produce vaccines at breakneck speed. Pre-orders have enabled the U.S. to fully vaccinate over half the total population while over 60% have received at least one dose, according to the Centers for Disease Control and Prevention. The U.K. has also done exceedingly well in its vaccination drive. The European Union countries were slow off the block, but have now started vaccinating their population at an impressive pace. Overall, over 40% of the population in advanced economies have been fully vaccinated, according to the IMF. Compare this with just 11% in emerging market economies. The advanced countries now feel that the pandemic situation is under control. At any rate, unless something goes dramatically wrong, the possibility of large-scale lock-



downs in these countries has receded.

Second, the advanced economies have been able to use their vastly superior fiscal situation to implement significantly bigger stimulus packages. Apart from allocations designed to directly support domestic industry and growth, sizeable income support measures have been provided that have both propped up consumer demand and mitigated extreme hardships to thousands of people. This kind of fiscal support promises to continue well into 2021. These measures have ensured that advanced economies do not suffer the kind of damage witnessed elsewhere and have also accelerated the pace of economic recovery. Business confidence is recovering too, partly due to the feeling that COVID-19 has been tamed thanks to the protection provided by the vaccination cover.

A laggard

The Indian economy has been one of the laggards among the emerging market economies. After the first COVID-19 wave, it contracted by over 7% during 2020-21. This earned India the dubious record of being the country with the worst performance among all major world economies. Earlier projections claimed that the economy would grow at over 10% during the current year. However, no one had taken the severity of the second COVID-19 wave into account. The dislocations caused by the pandemic have resulted in lower growth estimates for the Indian economy.

Although growth is muted and recovery is slow, retail inflation has crossed 6%, which is above the Reserve Bank of India (RBI)'s 'safe' level. Food prices too have played their

part in contributing to the overall rate of inflation. This is a serious matter since the poor are particularly hard hit if food prices cannot be controlled. The overall price situation puts the RBI in a quandary. Should it tighten monetary policy in order to contain prices but also slow down the pace of recovery? Or should it try to promote economic growth and let prices find their own level? Fortunately, crude oil prices have cooled off in international markets and this will naturally have a cooling effect on domestic prices.

Consumer spending has also been extremely sluggish and shows no signs of picking up. For instance, Google Mobility Index data showed that on July 26, visits to retail establishments including restaurants, cafes and shopping centres were down 20% compared to a pre-COVID-19 baseline. Sales of consumer durables are yet to pick up. Not surprisingly, business confidence is low and so entrepreneurs are wary of making new investments. This is evident from the fact that bank credit to the commercial sector has plummeted. The last component of domestic demand is government spending. But the government too has cut back spending as a proportion of GDP. Fortunately, Goods and Services Tax collections have been extremely good and this may induce the government to loosen the purse strings during the rest of the financial year.

Much will depend upon the progress of the pandemic in the near future. Most experts claim that a third wave of COVID-19 will soon be upon us. The peak level of infection is supposed to be significantly lower than what we experienced a couple of months ago. However, the different

variants of the virus and their differential transmission rates make it difficult to predict the spread of infection and hence the extent of economic disruption, although the current wisdom seems to be that vaccines are very effective in preventing serious illness.

Source of disquiet

This brings to the fore the very poor spread of vaccination in the country. India was known as the 'vaccine capital' of the world; yet the spread of vaccines has been abysmal. There is no doubt that the Central government was rather complacent in 2020. Unlike in the U.S., there was no attempt to accelerate production facilities in companies like the Serum Institute of India. The devastation caused by the second wave seems to have induced a sense of urgency in the Central government, which has now become more proactive. Nevertheless, it is unlikely that the Central government will be able to achieve its target of vaccinating all adults by the end of the year.

An added source of disquiet is that doubts have been expressed about the long-term efficacy of existing vaccines, particularly against mutations. Recently, Pfizer released data showing that there is a slight fall in protection against any symptomatic infection six months after immunisation, though protection against severe COVID-19 remained at nearly 97%. However, it is becoming clear that the virus is clever at evading the defences created by vaccines. In particular, there is now evidence which suggests that the Delta variant can cause breakthrough infections - several people are being infected even after being fully vaccinated. For instance, Israel, which implemented a very successful vaccination campaign, has witnessed an alarming rise in new infections. This has prompted Israel to offer a third dose of the vaccine to anyone above 60 years who was vaccinated at least five months earlier. Germany too has decided to offer booster doses to the elderly. Obviously, any need to provide booster doses will aggravate the existing shortage of vaccines in the country. This puts a question mark on whether we will soon witness the resumption of robust sustainable growth.

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