

# Impact of Covid-19: Dim prospects of two external resources for India

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April is the month when International Monetary Fund and World Bank usually discuss their first of the two respective biannual reviews of world economy, at their meetings held in Washington, D.C., USA. The next round of bi-annual meetings will be held in October. The regional development bank for Asia, Asian Development Bank held its annual meeting on May 1-3. We now have all the reviews on hand.

For five years, prior to 2019 the world economy was registering healthy growth, as the ill effects of the global financial crisis, also known as Great Recession: 2007-2009, were fading away except in India. What started with sorts of recovery of Indian economy was adversely impacted by both internal and external shocks contributing to decline in its growth well before 2019. The causes include (i) the sudden disruption in economic activities provoked by demonetization in late 2016; (ii) their lingering impacts for next two years; (iii) mounting nonperforming assets of bank and non-bank financial institutions and (iv) persisting poor export performance. Added to these domestic factors, a confidence crisis resulted in the pulling out of hot moneys by overseas investors in equity and short-term bond markets, which was compounded by the falling external value of the rupee.

The Wuhan-originated Covid-19 virus claimed the first known victim in the most advanced country, USA on January 29, 2020 in Seattle, Washington State, USA. The spread of the virus rapid, as visitor arrivals from Europe brought in the same virus. So, both the east and west coasts saw the beginning of the epidemic in USA leading to worldwide pandemic, indicating the rapid progress of globalization. It not only facilitated greater freedom of movement of labor and capital and all other factors of production across international borders but also the deadly virus.

Aside from loss of lives due to the pandemic, mostly partial and hence half-hearted and ineffective lockdowns followed by fall in production, and resultant lays-off led to decreases in personal incomes and reduced consumption. They all speeded up the contraction of demand in 2020. Reduced savings as well growing reluctance to invest when returns are uncertain added more to economic woes.

While world output in 2020 contracted by 3.5% (**Table 1**), Economic growth of Asia as a region shrank only by 0.25%. The reason is China, the second largest economy of the world

and the largest economy in Asia is reported to have not only survived but thrived. It expanded by 2.3%, which reduced Asia's contraction to a smaller degree. ADB's May 2021 Asian Development Outlook (ADO) reports that South Asia, as a sub-region recorded the biggest contraction in 2020. India, which is the largest economy in South Asia, with its 8.5% contraction pulled down the sub-region's growth rate of real GDP, although Bangladesh performed a lot better.

**TABLE 1. Real GDP Growth Rates: World, Low & Middle Income Countries and South Asian Countries**

Region and Countries	2018 (actual)	2019 (estimate )	2020 (forecast)
<b>World</b>	2.98	2.34	-3.5
<b>LMICs</b>	4.43	3.62	-5.5
<b>South Asia</b>	6.10	4.14	-8
<b>Bangladesh</b>	7.86	8.15	2.4
<b>Bhutan</b>	3.05	5.50	-1.8
<b>India</b>	6.12	4.18	-8.5
<b>Maldives</b>	8.12	7.00	-18.5
<b>Nepal</b>	6.70	6.99	-1.9
<b>Pakistan</b>	5.84	0.99	-1.5
<b>Sri Lanka</b>	3.51	2.28	NA

Source: IMF World Economic Outlook , April 2021; World Bank, World Economic Overview and World Bank: World Development Bank Indicators

## Emergence of new variants

Although it seemed the global spread came under control in late 2020, new variants of Covid-19 emerged in the last quarter of Europe giving rise to fresh outbreaks. Asia's incidence of Covid-19, which reached the peak with new cases of 106,000 per day in September 2020, fell to 32,000 by the end of February 2021. Discovery of vaccines toward the end of 2020 and their approval instilled hopes. India's vaccination production started in earnest. India, however with false signs of dip in new infections, shipped 64 million dozens of vaccines indigenously manufactured to friendly countries in Latin America and far off African countries, as well as neighbours. It was deceptive. The lull was broken in late March 2021. New cases came to be reported. They were rising since mid April 2021. It is now close to 400,000 on a daily basis, and the rural areas are increasingly under threat. The share of rural districts has risen to 49% in May compared to 37% in March.

With growing demand for vaccination, India is now experiencing supply shortages in vaccine. A State Bank India (SBI) study released on May 6 says that 160.5 million doses of vaccine have been administered; 131 million with one dose and 31.5 million fully vaccinated taking both doses. The percentage of people who have taken both double doses to total vaccination covering the eligible adult population is now around 19.5%. The daily vaccine doses given are now at an average of 17 lakhs per day. At this rate, SBI predicts that the country would only be able to vaccinate 15% of population by October 2021. For herd immunity, it is required that vaccination should take place at around 55 lakhs daily in September and October, 2021. This confirms a similar research finding by a IMF 2020 study, though in the context of a global scale, that a complete global coverage by the middle of 2021 is unlikely.

### Drying up of two external sources

In the past, when both domestic demand and supply forces were weak, there were some favourable external demand and supply forces, coming to rescue. Not any more: the once dominant foreign aid on annual basis, without any apparent quid pro element, in terms of pure grants from government to government is now phased out by advanced countries, except in dire circumstances such as earthquakes and tsunamis. The other is foreign direct investment (FDI) which is a private sector affair, is subject to severe fluctuations. We refer here to FDI by foreign manufacturing and service providing companies who add to physical investment in capital goods and contribution to training and transfer of skills. FDI is subject to conditions of political stability and confidence in the economy and in the government of the host country. The flow of hot money, in search of favourable interest rate differential in the short run (less than a year) financial assets is a different animal. It is in equity or short term bonds. Now the trend, in the context of Covid-19 is that overseas private investors are pulling out their short term equity and bond moneys for seeking “healthier” economies.

That brings us to the discussion of two remaining external resources. They are inward remittances\* and tourism. We will deal with remittances this time, reserving the topic of tourism earnings for next issue. **Table 2** provides data on remittances and FDI for the world as a whole, world’s all low and middle income countries\*\* and South Asia as a whole. Inward remittances are far greater than FDI for all South Asian countries except Maldives, which is an upper middle income country. It receives tourism infrastructure oriented FDI and in information and telecommunication sector, far greater than remittances, as Maldives’ migrant stock is the smallest among SAARC countries.

### Inward remittances

India has been the largest recipient of remittances, followed by China for the past several years. In the pre-pandemic 2019,

**TABLE 2. External Resources available for Developing Countries (US dollars and percent of GDP) Pre-pandemic period**

	2018	2019
<b>World</b>		
FDI ( US\$ billion)	1110	1630
FDI (% of GDP)	1.2	1.8
Remittances (US\$ billion)	639	656
Remittances (% of GDP)	7.5	7.6
<b>LMICs</b>		
FDI ( US\$)	610	542
FDI (% of GDP)	1.9	1.7
Remittances (US\$ billion)	486	503
Remittances (% of GDP)	1.5	1.6
<b>South Asia</b>		
FDI ( US\$ billion)	49	57
FDI (% of GDP)	1.4	1.4
Remittances (US\$ billion)	132	140
Remittances (% of GDP)	3.8	3.9
<b>Bangladesh</b>		
FDI ( US\$ billion)	2.4	1.91
FDI (% of GDP)	0.9	0.63
Remittances (US\$ billion)	15.6	18.36
Remittances (% of GDP)	5.68	6.1
<b>Bhutan</b>		
FDI ( US\$ billion)		
FDI (% of GDP)	0.003	0.001
Remittances (US\$ billion)	0.058	0.057
Remittances (% of GDP)	2.38	2.24
<b>India</b>		
FDI ( US\$ billion)	42.11	50.11
FDI (% of GDP)	1.56	1.76
Remittances (US\$ billion)	78.79	83.33
Remittances (% of GDP)	2.9	2.91
<b>Maldives</b>		
FDI ( US\$ billion)	0.576	0.961
FDI (% of GDP)	10.85	17.03
Remittances (US\$ billion)	0.004	0.004
Remittances (% of GDP)	0.79	0.78
<b>Nepal</b>		
FDI ( US\$ billion)	0.068	0.185
FDI (% of GDP)	0.28	0.6
Remittances (US\$ billion)	28.43	26.92
Remittances (% of GDP)	8.29	8.24
<b>Pakistan</b>		
FDI ( US\$ billion)	1.74	2.21
FDI (% of GDP)	0.55	0.79
Remittances (US\$ billion)	21.93	22.24
Remittances (% of GDP)	6.74	8.6
<b>Sri Lanka</b>		
FDI ( US\$ billion)	1.614	0.756
FDI (% of GDP)	1.8	0.9
Remittances (US\$ billion)	7.04	6.5
Remittances (% of GDP)	7.96	8.03

**Note:** No data for 2020 yet.  
See text for preliminary estimates



the top three remittance recipient countries were India (\$83.1 billion), China (\$68.4 billion) and Mexico (\$38.5 billion). India's migrant stock is the second largest, next to China. The blue collar workers' remittances are more regular and steady, although in smaller in size. They are intended for supporting their families left behind in India. They contribute to poverty reduction. They also finance education of the young ones and medical expenses of the aged in the family. Occasional but far more sizeable amounts are sent by highly qualified professionals of Indian origin and those residents working on temporary basis in advanced countries.

All remittances, being in foreign exchange, are real resources. They are additions to India's foreign exchange reserves. In the context of declining export earnings, remittances have emerged to be a major support to India's balance of payments. Current account deficits have remained smaller and manageable. In the absence of remittances, the deficits would have led to far greater pressure, resulting in bigger depreciation of the rupee.

Preliminary estimates reveal remittances to low and middle income countries (LMICs) would fall from the record high, \$554 billion in 2019 to \$508 billion in 2020 and to \$470 billion in 2021, resulting in the sharpest decline in recent years. The current oil crisis is now emerging as a supply-propelled crisis, which started as a demand oriented crisis following the falling incomes and consequently leading to drop in production and rise in unemployment and layoffs. With the cancellation of major events such as Dubai Expo 2020, many lost jobs in 2020. About 400,000 Keralites, working in the Middle East were reported to have returned home. Remittances to India are expected to fall by about 25%.

Only two countries in South Asia, Bangladesh and Pakistan experienced rise in inflows of remittances in 2020. In July 2020, they witnessed surges. Their overseas migrants who had saved money for travel to Mecca might have decided to send it home because of steep reduction in the issue of visas by Saudi Arabia. Instead of spending on pilgrimage, migrants sent money to home countries..The World Bank called this as

Haj effect, enabling rise in remittance inflows for both, and Bangladesh in particular, recording a 53% increase in 2020.

As uncertainties are continuing, India should not tinker with remittance inflows. Banks and other financial institutions may look upon remittances as a source of making money to reduce losses due to NPAs. Any attempt to exploit Indian migrants and overseas citizens of Indian origin by imposing fees on remittances for conversion into rupees and another conversion into foreign currency for long term deposit and other such "innovative measures" for increasing revenue would be counterproductive. A decade ago, the government introduced the service tax in 2012 but had to withdraw it due to protest and pressure from NRIs. The Aesop story on the goose and the golden egg is well known. There will be no more golden eggs!

Last month, on April 1, the government shocked the nation with a poor decision, amounting to further reduction in the real interest rate for savers in the midst of rising fears of inflation. The interest rate on Public Provident Fund was lowered from 7.1% to 6.4%, and that on National Savings Certificates from 6.8% to 5.9%. Following a hue and cry in social media, it was withdrawn next morning. Government gave a lame excuse : "Orders were issued by oversight". ■

\*World Bank (2019) defines the term remittances as the sum of personal transfers and compensation of employees. Personal transfers include all current transfers in cash or in kind between resident and nonresident individuals, independent of the source of income of the sender.

\*\*Low income countries are those with annual per capita incomes below US \$1036. Lower-middle income countries are those with annual per capita incomes ranging from \$1036 to \$4045; and upper middle income countries are those with annual per capita incomes ranging from \$4046 to \$12,535. The high income countries are those with annual per capita income exceeding \$12, 535. All are in 2020 prices.

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