The economic situation is grim

The financial sector, in particular, is vulnerable

On Saturday, finance minister Nirmala Sitharaman announced that the government was extending its credit facility, originally announced for medium and small enterprises to private professionals such as doctors and chartered accountants. This, the minister said, was being done after stakeholder consultations. The decision is an indicator of the stress faced by professionals such as doctors and accountants, as economic activity is far from normal and new Covid-19 cases continue to rise in most parts of the country. But this is not the only indicator of a troubled economy. The Goods and Services Tax (GST) collection in the month of July dropped to ₹7,422 crore from ₹90,917 crore in June. In July 2019, this number was ₹1.02 lakh crore. Most analysts have been warning that economic revival has started plateauing in July after showing a brief spike due to lockdown induced pent-up demand in June. Ms Sitharaman herself said that the “government is cautious about overstating the green shoots of a recovery visible in the economy”.

As Covid-19 cases continue to climb and large parts of the country experience intermittent lockdowns, the pandemic’s economic challenge will only get more difficult. Supply chains remain disrupted; demand continues to be low; unemployment is still high; and the Centre’s budgetary numbers may not quite hold because of both revenue shortages and new expenditure commitments. Among the most complex challenges will be loan-default related difficulties in the financial sector, especially once the ongoing moratorium comes to an end. Any large crisis on this front will necessitate a bailout and impose an additional strain on the government’s already stretched fiscal resources. A sudden withdrawal of credit relief can make firms unviable, and trigger an inflationary shock as productive capacity suffers.

These questions will hopefully be discussed at the Reserve Bank of India’s Monetary Policy Committee meeting this week. Signalling on this front will matter more than any decision on policy rates, which many private forecasters believe will see a pause. It will also be interesting to see whether the MPC makes a GDP forecast for this year and whether there has been any revival in consumer confidence after lockdown restrictions have been eased.