COVID-19: A crisis unfolding

Executive Summary

The recent outbreak of the novel coronavirus disease (COVID-19) has in every measure fulfilled the criteria of being an unprecedented crisis in recent economic history. The assessment of the economic costs of the pandemic, is leading the policy makers and central bankers of the world to revise their fiscal and monetary policy stance, respectively. The global response to avoid the spread of COVID-19, has been to shut down entire cities and provinces, shut down all operations as far as possible, of hotels, trade, transport, all cultural and sports events, everything possible to avoid social congregation. This would lead to significant impact on economic growth worldwide and estimates point to a decline in global growth by at least 2%, making global growth as low as 1%. Some notable developments regarding the crisis are:

- The G20 nations have resolved to collectively inject USD 5 trillion into the global economy to fight the COVID-19 crisis.

- Unfortunately, this crisis comes at a time when the central banks have already exhausted most of their arsenal on fighting the global slowdown the economies were facing world over in the midst of the trade wars, geopolitical conflicts and regionalist policies implemented by governments.

- The Indian central government and the Reserve Bank of India have acted in quick succession to take measures to quell the significant loss to economic growth by taking a set of measures.

- The Indian government announced a fiscal stimulus of Rs.1.7 lakh crore and the RBI cut the policy repo rates by a more than expected 75 basis points.

- Though these measures are aggressive, we believe that both the government and the central bank will need to do more in order to create stability on economic, social and financial fronts.

COVID-19: A crisis unfolding

The recent outbreak of the novel coronavirus disease (COVID-19) has in every measure fulfilled the criteria of being a black swan event in recent economic history. The crisis is still unfolding and the situation created by it is ominous in terms of the economic and social costs that it entails, strangling the world economy into a recession. The virus originated in China, in the city of Wuhan in the Hubei province sometime in December, and since then more than 1.87 million people have been infected, more than 116,037 deaths have been reported, and over 434,840 people are reported to have recovered.

The World Health Organisation (WHO) has already declared it as a pandemic, and urged governments to ensure medical infrastructure to fight the disease. Since no known medical cure exists, the only remedial measure so far has been social distancing. This is often imposed by the state, which has led to economic activity coming to a standstill.

The financial markets had lost confidence by the uncertainty, with asset price volatility reaching levels of the 2008 financial crisis, and more and more likely to breach it by a long chalk. Growth seems to be reaching new lows in a global economy which was already reeling with trade wars, increased noise against global trade, and slow growth. Global growth is likely to be losing steam and would be printing at less than 1% in 2020. The assessment of the enormous economic costs is leading the policy makers and more specifically the central bankers of the world to revise their monetary policy stance.

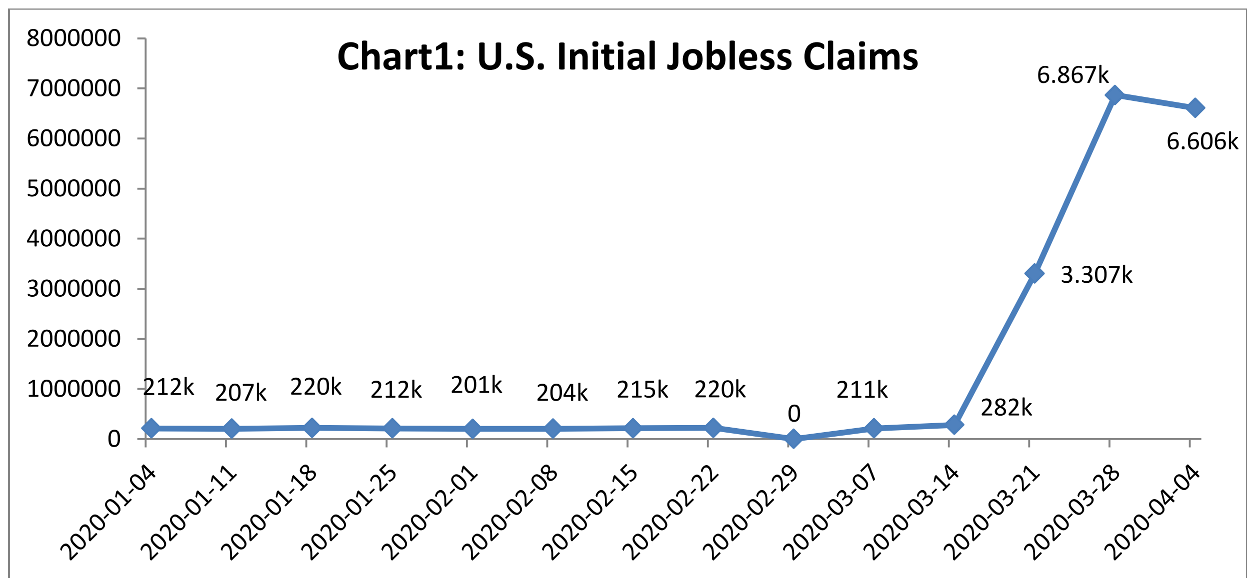
Global Response to the Crisis: The global response to COVID-19 has been to shut down entire cities and provinces, shut down all operations as far as possible of hotels, trade, transport, all cultural and sports events, everything possible to avoid social congregation and to consequently avoid the spread of the disease. This would lead to significant impact on headline growth for the global economy and most estimates point to a derailing of global growth by almost 2%,. This would lead global growth to print below 1%.

As a coordinated response is the need of the hour the G20 nations have resolved to collectively inject USD 5 trillion into the global economy to fight the COVID-19 crisis. The resolution also included working alongside multilateral bodies like the IMF and the World Bank, United Nations. This action came with a significant lag as already more than 50000 people had died and almost a third of the world's population was locked down in their homes causing an unprecedented shock to the world economy. The core of the G20's first virtual summit was large-scale fiscal support targeted at getting economic

growth back on track. This would also create a recovery path for the job losses and business shut-downs.

Fiscal stimulus and relief packages announced as response the crisis: National Governments around the world have announced aggressive fiscal measures for the relief for the unemployed, and the underprivileged as that segment of the economy will be the hardest hit.

To see the unprecedented short-term impact of the crisis we take a look at the U.S. Initial Jobless claims which individuals file to get unemployment benefits from the Federal government. The U.S. initial jobless claims post the spreading of the crisis, printed at a mammoth 3.28 million week ending 21st March and had climbed to almost 6.64 million as on 28th March,2020. To put these numbers in perspective, till now the record high of jobless claims had been in 1982 at 695,000. Economic sense indicates that any government package is not enough to fulfil the economic gap that the effects of the COVID-19 will create in the near term.



Fiscal measures doled out by major governments are as follows:

US Federal Government: In response to the crisis, the Trump administration has signed a USD 2.2. Trillion package signing a bipartisan deal, making it the largest of its kind in modern American history. The package is intended to help the jobless, small businesses and the corporates regain the lost ground due to the crisis. The package will mean direct pay-outs and benefits to the jobless and huge funds to support businesses. The measure which was approved unanimously by both parties and the senate is unprecedented in sheer size and scale and is a mammoth effort to bring the economy back on track.

Some perspective on the package would clear the scope of the fiscal measure as the USD 2.2 trillion in sheer amount is more than double of USD 800 billion package passed by the Congress after the Global Financial Crisis in 2009. The size of the current package is estimated to be at 50% of the total federal budget of USD announced for FY21 by the Trump administration.

The details of the legislation are as follows:

- direct payments of USD 1,200 to millions of Americans, including those earning up to USD 75,000,
- an additional USD 500 per child.
- It would substantially expand jobless aid, providing an additional 13 weeks and a four-month enhancement of benefits,
- extended the payments for the first time to freelancers and gig workers
- The measure would also offer USD 377 billion in federally guaranteed loans to small businesses
- and establish a USD 500 billion government lending program for distressed companies reeling from the impact of the crisis, including allowing the administration the ability to take equity stakes in airlines that received aid to help compensate taxpayers.
- It would also send USD 100 billion to hospitals on the front lines of the pandemic.

Source:Senate Approves $2 Trillion Stimulus After Bipartisan Deal- Emily Cochrane and Nicholas Fandos- New York Times

The announcement comes on the back of another package which the Trump administration had announced weeks ago: This included a US$8.3 billion Coronavirus Preparedness and Response Supplemental Appropriations Act and US$104 billion Families First Coronavirus Response Act providing 0.5 percent GDP for health care, sick leave, small business loans, and international assistance.

The Government of Japan adopted two emergency response packages (on February 13 and March 10), for a total amount of ¥446 billion (0.1 percent of GDP). The packages included:

- measures to contain the spread of the virus and enhance preparedness of the healthcare system (around ¥62 billion, or 0.01 percent of GDP);

- aid to households (about ¥223 billion, or 0.04 percent of GDP) such as enhanced paid-leave and compensation to working parents affected by the school closure; as well as
- Measures to mitigate the economic impact (about ¥142 billion or 0.03 percent of GDP) including subsidies to firms who maintain employment during scale down of operations.

Japan has also announced a mammoth stimulus of ¥108 trillion (USD 990 billion), worth ~20% of the country's GDP to fight the onslaught of the COVID-19 crisis. Of which, direct fiscal spending will be around ¥39.5 trillion.

Individual nations in the European continent have been following a more bottom-up rather than a top down approach, with the fiscal spending in similar combinations across geographies. A combination of short time work schemes, guarantees and liquidity support for companies facing financing problems. Direct fiscal stimulus, be it for health care sector or cash-out for smaller companies as adopted first by the German government. On average the governments have adopted a fiscal stimulus of 2% of GDP and guarantee schemes of 13% of GDP. European finance ministers had agreed to activate the so-called escape clause, allowing countries to escape the 3% deficit limit without triggering an elaborate fiscal procedure. Similarly governments from all over the world have poured in with fiscal stimulus packages to help the underprivileged and the small businesses that are to be hit hardest by this crisis. Governments are giving relief to various economic segments mostly in the form of tax deferrals, direct benefits to small and medium business and unemployment benefits.

Monetary policy responses as taken by the major central banks are given below:

Monetary policy responses to the crisis have been aggressive on the part of the central bankers. This will be an extremely challenging times for both the central banks as well as the governments since, this crisis comes at a time when the central banks have already exhausted most of their arsenal on fighting the global slowdown that the economies were facing in the midst of the trade wars, and geopolitical conflicts.

US FED: In light of the developing COVID-19 crisis and its evolving risk to economic activity the FED, in two unscheduled meetings on 3rd March, 2020 and one on 15th March, 2020 cut the target range for US FED Funds rate by 50 basis points to 1-1.25% and then again in an unscheduled meeting on the 15th March 2020, the Fed slashed its target range by a full percentage point to 0-0.25% from the earlier 1-1.25%. Overall, the Fed has cut its target for the Fed funds rate by a whopping 150 basis points in 2 weeks,

and its interest rates have reached the zero bound. US 10 year bond yields touched levels below 1% which had not happened even in the 2008 financial crisis.

This is in addition to the fact that it had to convene two unscheduled meetings to implement the cuts, when the scheduled policy meeting was just two weeks away, signifying the intensity of the current crisis. Even though the Federal Reserve cut rates by 150 basis points, additional measures were announced to support credit flow to the economy. These included as a first step to but Treasury Securities and Mortgage backed securities by USD 500 billion and USD 20 billion respectively.

These measures were announced along with the second rate cut on 15th March 2020, Less than a week later the US Federal Reserve announced that it would:

- Support credit flow to the economy by buying bonds and mortgage backed securities.
- The Federal Reserve would be buying corporate mortgage backed securities (CMBS), which shall be included in the agency mortgage backed security purchases.
- This was also followed by a slew of other measures like announcing the Term Asset Backed securities loan facility (TALF) wherein Asset backed securities (ABS) issuance will be enabled backed by student loans, auto loans credit card loans, loans guaranteed by the Small Business Administration (SBA).

The PBOC (People's Bank of China): As early as 3rd December the PBOC governor Yi Gang had made a speech saying that the PBOC had avowed to stay away from the so called "quantitative easing" and negative interest rates. Chinese growth was undergoing a slowdown before the COVID-19 crisis broke out. Since then, the PBOC cut the Required Reserve Ratio by 50 basis points on 1st January, 2020. The PBOC kept infusing liquidity with a view to support markets which had by then tumbled as the COVID-19 spread fast.

Again it cut other policy rates like the medium term loan facility rate to financial institutions by 10 basis points from 3.25% to 3.15%. This was done after the central banks of Philippines and Thailand had cut their policy rates by 25 basis points as the entire Asian continent was anxious about the economic consequences of the crisis. There is now clamour for more monetary easing as the Chinese Premier Xi Jingping has called for more monetary easing and the PBOC has responded by saying that it is ready to ease further.

The ECB: The ECB did not cut rates any further. As mentioned above the central banks especially in the developed world are in an unusual position of already having interest rates near the zero bound. Not much can be done in terms of interest rates at least in Europe where the ECB has already maintained negative interest rates on the deposit facility at -0.5%.

Instead, the ECB has unveiled a package of liquidity measures to counter the economic effects of the crisis. Measures include

- Additional Long term refinancing operations (LTROs). Targeted longer term Refinancing operations III (TLTROs) These operations will support bank lending to those affected most by the spread of the coronavirus, in particular small and medium-sized enterprises. The interest rates will 25 basis points below the average rate applied in the Euro System's main refinancing operations.
- A temporary envelope of additional asset purchases worth €120 billion will be added until the end of the year, ensuring a strong contribution from the private sector.
- This is in addition to the existing asset purchase programme (APP), and will support favourable financing conditions for the real economy in times of heightened uncertainty, according to the ECB.
- The ECB has also announced an asset purchase program of €750 billion (USD 820 billion) termed as the Pandemic Emergency Purchase Programme (PEPP), which comes on top of the already existing asset purchase program.
- This would entail the ECB buying sovereign as well as corporate bonds.
- The ECB would also include Greek bonds in this asset purchase program for the first time.
- The total support by the ECB to European nations through various bond buying purchases now stands at a whopping €890 billion (USD 985 billion). The size of this bond buying pace far outpaces the measures taken during the Global Financial Crisis (GFC).

Bank of England: United Kingdom is under duress post the implementation of Brexit, with uncertainty surrounding growth and employment along with economic prospects as the trade deal with the European Union has yet to be finalised. Amidst this the striking of the COVID-19 solicited an immediate and aggressive response, and the Bank of England promptly cut policy interest rates to 0.1% as a boost to give credit growth a fillip. The bank had already cut interest rate by 50 basis points to from 0.75% to 0.25% and cut it further to 0.1%. Though the statement makes it clear that COVID-19 is a

temporary economic shock, the effects and the magnitude remain uncertain. This was coupled with easing targeted lending to small business under the Term Funding scheme with additional incentives for Small and Medium-sized Enterprises (TFSME).

Bank of Japan: After almost three decades of struggling with non-effectiveness of monetary policy there was no margin for the BoJ to announce a rate cut as its interest rates are already negative, with its short term interest rate target at -0.1%. The Bank of Japan instead went on to increase the quantum of asset purchases but with little effect.

Smooth Dollar Funding: To ensure smooth functioning of the FX markets and the flow of dollars in this crisis the six big central banks i.e. The Bank of Canada, the Bank of England, the Bank of Japan, the European Central Bank, the Federal Reserve, and the Swiss National Bank have announced a coordinated action to enhance the provision of liquidity via the standing U.S. dollar liquidity swap line arrangements. These central banks have agreed to lower the pricing on the standing U.S. dollar liquidity swap arrangements by 25 basis points, so that the new rate will be the U.S. dollar overnight index swap (OIS) rate plus 25 basis points. The new pricing and maturity offerings will remain in place as long as appropriate to support the smooth functioning of U.S. dollar funding markets[1]

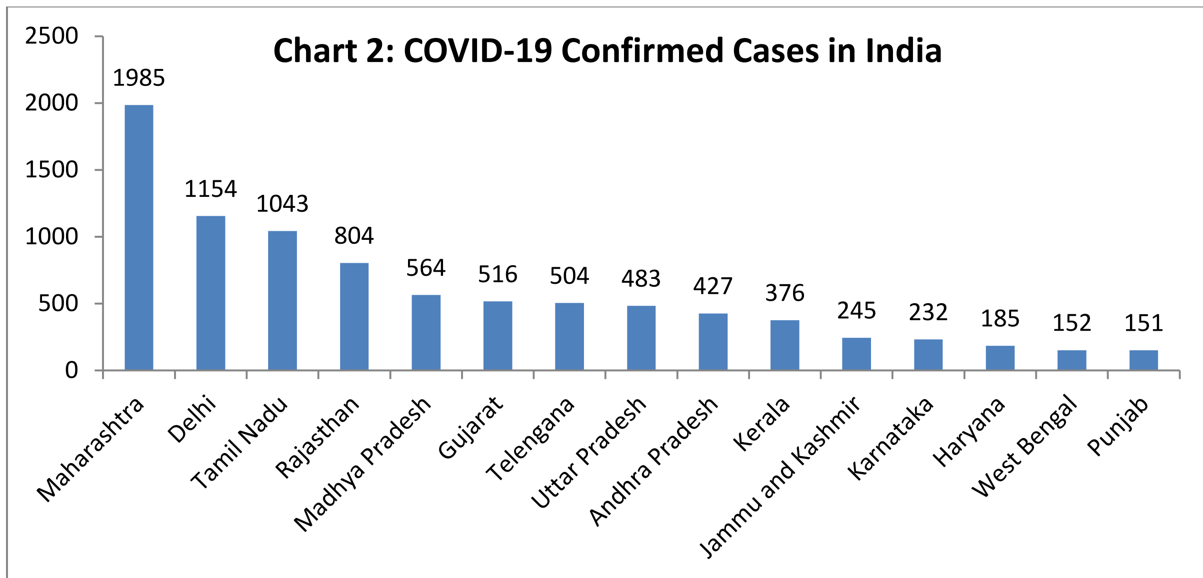
These measures and the coordinated policy actions by other central banks are signal enough, that the measures are already more than what the central banks did at the time of the Global Financial Crisis in 2008. What is worrying is that despite the measures taken by the various central banks to support economic growth, financial markets seemed to take no comfort in the easing and monetary support and continued to fall sharply during the recent weeks.

India's Case Study on the spread of the disease: Flattening the Curve

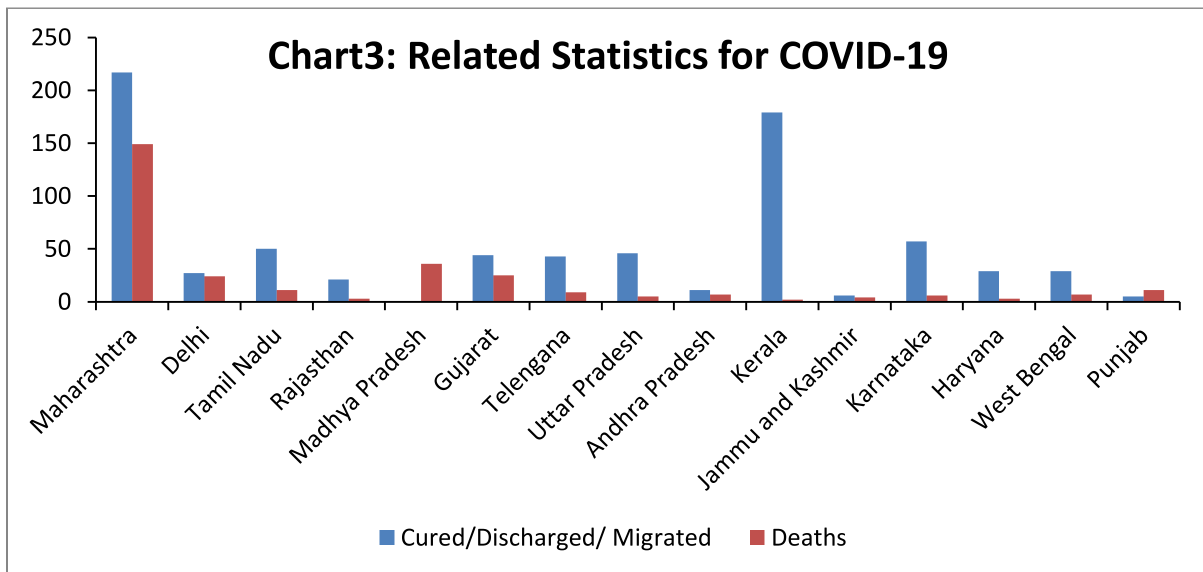
While the virus outbreak started off in Dec-19 in Wuhan, China, India reported its initial three cases in the state of Kerala in Jan-20. However, number of positive cases reported in India rapidly increased in Mar-20. Till March 23, 2020 total number of positive cases within the country has crossed the 500 mark. The worst affected states are Maharashtra and Delhi with 1985 and 1154 positive cases respectively. According to the Union Ministry of Health and Family Welfare, India has not moved entirely to stage III- i.e., "Community Transfer Stage". Although some hotspots like Delhi and Mumbai may be on the verge of reaching the Community Transfer Stage. With current decision of lockdown

[1] Bank of Japan Press release.

of entire nation for 21 days and only essential services allowed to function, the Government is taking pro-active steps to combat the deadly virus. The Prime Minister has announced Rs 15,000 Cr fund to test Corona, isolation beds, ventilators and other essential facilities needed to battle the virus. The latest statistics for the most affected 15 states are given below:



Source: Ministry of Health & Family Welfare



Source: Ministry of Health & Family Welfare

Indian Economy and Macro parameters: The prime difference in the ongoing crisis and any other financial crisis is that this is a crisis much like a war with serious effects

affecting the real economy, as opposed to spillover effects of the financial crises into the real economy which result primarily in constraints on credit and liquidity. To that extent, this crisis is far more potent in terms of the shock it would give the Indian economy in terms of growth. Simple back of envelope calculations point to around Rs.40-50,000 crore per day loss assuming a complete lock down of all economic activity.

Carrying on the lock down for extend periods, as has been done now for 3 weeks, would push India into sub-4.5% growth for FY20.For the Q4FY20 growth estimates, the print should be within 2.5%-3%, assuming the first round effects of the national lockdown will affect output in the last week of March 2020. With almost all the sectors being affected by the lock down including to a lesser extent agriculture and allied activity, manufacturing as plants are being shut or being run at minimum capacity, though activity would be ongoing.

As the GDP is looked at industry wise, all the segments will face a short run economic shock whether it is industry, agriculture or services. As noted earlier with a crisis of this magnitude and most of working population locked down, our growth estimates on a conservative basis reach to a level of 3.0% for Q4FY20, with downside risks to the headline.

The agricultural sector has faced severe price volatility due to unseasonal rains, destruction of crops due to rains and locust attacks in some parts of the country. Now, the farms are facing oversupply with no resource for crops to reach markets in the midst of a lock down. This might not augur well for food inflation in the near future, as it may delay harvesting procedure creating temporary food shortages, spiking prices. The very thin silver lining to this dark cloud is that the IMD has projected a normal monsoon this year in the absence of the El-Nino, which should augur well for agriculture, assuming that by that time India would have successfully flattened the curve and the menace altogether.

Overall, CPI inflation should reach to about 3% by Q3FY21, owing to a sharp fall in consumption demand for various non-essential commodities and also supply side disruptions caused in almost all commodities. Though the assessment of the balance of risks to headline inflation would be premature at this stage since, the usual forces of demand and supply dynamics are way out of the normal conditions for the inflation trajectory to be projected with reasonable confidence.

Manufacturing sector was reeling with the effects of the slowdown much before the outbreak of the crisis.The present situation will affect industrial output as factories are

mostly closed or operating on minimum capacity. Though this seems to be a temporary scenario the numbers would surely be heading underwater at least for a quarter. Construction and other services like trade, hotels and transport are already severely affected and we expect a decline in these sectors touching double digits. Electric supply, gas and water may not see reduction in output per se and in fact overall consumption might be balanced as offices and industries remain closed while household consumption would peak during the time since most of the country is on a work from home mode.

The worst sector to be affected by the crisis is the services sector where industries like the hotel and tourism related economic units have already started laying off staff looking at the extant business conditions. This also falls in line with all the three major rating agencies cutting growth forecasts for India quite sharply to just above 5% for FY21 from earlier estimates of around 6%, which is still an optimistic estimate.

While as an aftermath of the 2008 crisis, with world awash with liquidity, and the search for yields, India saw a boost in foreign investments, both in foreign direct investments (FDI) and in foreign institutional investments (FII). This time looks different, as investors are making capital fly to safe haven assets like the US treasuries, as the month of March saw the highest sell off by foreign investors, in recent times. This would delay the government's plan of making India a USD 5 trillion economy, as domestic savings are clearly falling short to fund the country infrastructure expenses.

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Need of Greater Fiscal-Monetary policy coordination: The Indian central government has announced a 21 day lock down period and urged people to stay at homes. In addition the government has announced Rs.15,000 crore worth of government spending toward healthcare. The central government was also quick to announce a fiscal package of Rs.1.7 lakh crore to support the poor under the Pradhan Mantri Garib Kalyan Yojana. Recall that in the budget presented on the 1st of February,2020 the Finance Minister Ms. Nirmala Sitharaman had taken the liberty to enhance the fiscal deficit by 0.5% of GDP to 3.8% from the earlier targeted 3.3%, as the economy needed government spending to support growth. This additional spending of Rs.1.7 lakh crore will add roughly 0.8% to the existing fiscal deficit taking it to 4.7% from the current 3.8% of GDP. This is assuming that the additional funds are over and above the earlier budget estimates. This transgressing of the fiscal red line will prop up growth in the short term as government spending seems to be the only avenue for rescuing the headline GDP to some extent. The salient features of the scheme are given below:

- Insurance cover of Rs.50 Lakh per health worker fighting COVID-19 to be provided under Insurance Scheme

- 80 crore poor people will to get 5 kg wheat or rice and 1 kg of preferred pulses for free every month for the next three months
- 20 crore women Jan Dhan account holders to get Rs 500 per month for next three months
- Increase in MNREGA wage to Rs 202 a day from Rs 182 to benefit 13.62 crore families
- An ex-gratia of Rs 1,000 to 3 crore poor senior citizens, poor widows and poor disabled individuals.
- Government to front-load Rs 2,000 paid to farmers in first week of April under existing PM Kisan Yojana to benefit 8.7 crore farmers
- Central Government has given orders to State Governments to use Building and Construction Workers Welfare Fund to provide relief to Construction Workers

Other Fiscal Measures:

- Till now Ministry of Finance has also announced relief measures related to Statutory and Regulatory Compliance. Some of the important reforms included are:
- Last date for income tax returns for FY2018-19 extended from March 31, 2020 to June 30, 2020.
- For delayed payments of advanced tax, self-assessment tax, regular tax, TDS, STT, CTT made between March 20, 2020 and June 30, 2020 reduced interest rate of 9% to be charged instead of 12%/18% per annum.
- For GST returns due in March, April and May 2020 can file GSTR by last week of June 2020. However, 15 days after the due date reduced interest rate of 9% would be charged down from the current 18%.
- Relaxations given for three months in financial services including: no fee to be charged to debt card holders for withdrawing cash from other bank’s ATM; waiver of minimum bank balance and reduced bank charges for digital trade transactions.

Monetary Measures:

With about 40 central banks around the world cut interest rates mostly in Mar-20 amid the ongoing COVID-19 pandemic, RBI was expected to follow suit in the upcoming monetary policy meeting scheduled for April 3, 2020. As expected the RBI advanced its scheduled meeting on 1st April to the last week of March and announced the following measures to mitigate the economic impact of the COVID-19 crisis:

Monetary Measures:

The Repo rate has now been cut by 75 basis points and stands at 4.4% as compared to 5.15% earlier.

The Reverse Repo rate has cut by 90 basis points and stands at 4%. This asymmetrical LAF corridor has been created so that banks are incentivized to on-lend credit to productive sectors of the economy rather than parking the excess funds with RBI in the LAF window.

Liquidity Measures:

- The RBI again took a leaf out of the ECB's book and announced a Targeted Long term refinance operation (TLTRO).The RBI will conduct auctions of targeted term repos of up to three years tenor of appropriate sizes for a total amount of up to ₹ 1,00,000 crore at a floating rate, linked to the policy repo rate.
- Liquidity availed under the scheme by banks has to be deployed in investment grade corporate bonds, commercial paper and non-convertible debentures over and above the outstanding level of their investments in these bonds as on March 25, 2020.
- Eligible instruments comprise both primary market issuances and secondary market purchases, including from mutual funds and non-banking finance companies. Investments made by banks under this facility will be classified as held to maturity (HTM) even in excess of 25 per cent of total investment permitted to be included in the HTM portfolio.
- Exposures under this facility will also not be reckoned under the large exposure framework.
- CRR cut by 100 basis points and now stand at 3% of Net Demand and Time liabilities (NDTL), for a period of one year. This would release primary liquidity worth Rs.1,37,000 crore in the banking system. This is expected to release liquidity uniformly across the banking system in proportion of the liabilities of the constituents rather than in relation to holdings of the excess SLR.
- Also minimum daily CRR balance to be maintained is reduced from 90% to 80% beginning March 28th to June 26th,2020.

These liquidity measures will release an estimated Rs 3.74 lakh crore in the banking system. Eventually, the central government and the RBI will have to act in accordance of the greater fiscal and monetary coordination given the fact that still greater support will be required in terms of government spending for health care, rural and urban poor, as

the crisis unfolds. While fiscal profligacy in these times will be taken with a more liberal view, the crucial question remains, what part of it shall be apportioned to market borrowings? Assuming that 100% of these extra support measures are to be absorbed by the debt market, the RBI will have to conduct many more OMOs, at least worth worth Rs.1.5-2.5 lakh crore in FY21 and possibly increase the amounts as the situation evolves, to keep the market borrowing costs reasonable for the government.

Tax revenues are going to be severely affected for the center as well as the states and that too will impel the government to borrow higher than budgeted borrowings for FY21. Tax collections had been contracting in FY20, and are slated to decline sharply in FY21, not coming anywhere close to budgeted revenue numbers. In light of this, the Government and RBI can think of various options. The problems for state borrowings has already been highlighted in the increased borrowings in the first auctions of State Development loans with yields on state borrowings reaching levels of 8%, almost 130 basis points over the G-secs. In light of the situation, there have been suggestions by state ministers to allow the states and the center to borrow directly from the RBI, and also to allow private placement of government debt which would open a long closed chapter in India's bond market history.

Monetizing the deficit has been stopped since borrowing from RBI in ad-hoc treasury bills stopped in 2002. Eventually the situation might come to crossing the line in sand, and since the RBI governor has stated in the recent MPC minutes published for the March 27, 2020 policy, "*the RBI will continue to remain vigilant and will not hesitate to use any instrument – conventional and unconventional – to mitigate the impact of COVID-19, revive growth and preserve financial stability.*", It cannot be said with certainty, whether RBI and the government will make the decision to privately place debt at least for a temporary period with RBI.

Even though there has been a string of liquidity measures by the RBI, to boost credit growth, the banking sector has not been able to cope with the lack of credit demand in the economy. Credit growth has now dwindled to single digits in the wake of the rising NPA issues in the bank balance sheets. The recent debacle of a private sector bank going down, leading to a government/RBI managed bailout,lent another blow to investor confidence in the banking system. Unfortunately for the RBI, it has to rebuild the trust of the economy in the banking sector with these kind of credit events coming up now and then beginning with the IL&FS default, the NBFC liquidity crisis and now the private banking space undergoing turbulence. Though, we believe that the recent moderation in credit growth is a two-fold problem:

- Banks are not willing to lend to projects with the balance sheet constraints extant due to their already existing NPAs
- Corporate Loans have moderated due to lack of greenfield projects and lack of growth owing to the slowdown

These measures will incentivize borrowers to take on new projects, but the question still remains whether lenders would be enthusiastic to on lend to the good projects given the present situation of uncertainty. The recent measure the central bank has taken like Operation Twist, which was clearly aimed at reducing the borrowing costs for corporates, would work only for the premium credits in an effective manner in the current crisis as bankers will now see a looming debt crisis in the offing especially as households/corporates will face increased risk of unemployment/layoffs.

These liquidity and credit measures would have to be continued by the RBI, along with its usual battery of OMO purchases expanded in line with the government's fiscal expansion to keep the interest rates within bounds, and monetary policy transmission made more effective so that the rate cuts meet the intended purpose.

Further in terms of fiscal monetary co-ordination, this year the fiscal deficit would most likely reach 5%, assuming the additional 1.7 lakh crore announced by the government is funded through market borrowings. In that case, the RBI will have to ramp up its OMO purchases, as excessive liquidity has not really translated itself into additional risk appetite by banks and participants as far as G-sec yields are concerned, with the policy repo and the 10 year G-sec still yielding a carry of roughly 170-180 basis points. To bolster additional risk appetite and demand for G-sec, the RBI could offer a temporary (at least 3 year) window for sovereign assets bought by banks which would be categorized in Held-to-Maturity classification making it attractive for banks to invest. This facility could be extended for 2% of NDTL over and above the current SLR holding of 18%. This will subsidize banks which are the largest holders of G-sec in the country, and also take some burden of financing the deficit from RBI's shoulders.

Conclusion: The COVID-19 crisis has created an unprecedented moment in history, which hopefully is never to be experienced. With a human tragedy which is spreading fast, governments and central banks have to think out of the box for their respective economies to get through these times with as little loss as possible. Governments from all around the world have come forward in terms of fiscal measures to the extent and proportion of their economic capacity and central banks have turned to the "whatever it takes" mode to save the financial and credit markets from coming to a standstill.

The Indian Government and the RBI have acted in quick succession by announcing various fiscal and monetary measures to quell the impact of the crisis and stand ready to do more so that the loss to economic growth is mitigated as far as possible. We expect the central government to announce more relief measures, even though smaller than the one announced recently targeted to specific sectors like the travel industry, the services sector overall , and also expect the RBI to follow with more monetary easing as the need evolves with another round of easing in rates and possibly more asset purchases.

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