Economy This Week (4th May to 17th May 2020)

Economy is an important part of the UPSC prelims and mains exams; this series titled 'Economy This Week' has been initiated to address the need to read and analyse economic articles in various business-related newspapers. The round-up of the Economy/Business section news for 4th May to 17th May 2020 is given below. Business news is essential for IAS exam preparation.

1. Remittance economy on a slippery slope (LM 4/5/20)

- There are 10 million Indian workers (skilled and semi-skilled) working in the wider Gulf region.
- India has received remittances worth $ 82 bn in 2019, back to India to support their families.
- With the global oil prices plunging to their lowest, the economies are under stress. Earnings in these economies mainly come from oil exports.
- As per the IMF, the Middle East and Central Asia would be recording a negative 2.8% growth rate for 2020.
- Some of the people registered to return are dependents of the workers, some have finished their work and some have been laid off. Post the 2008 Global Financial Crisis, of the 6 lakh plus Indians, around 2 lakh returned.
- The migrants from 5 southern states support approximately 40 million Indians back home.
- Because of the pandemic, which has resulted in the free fall of crude, the remittances have declined by 23% in 2020 to $64 billion (sharpest fall in recent history as per the World Bank report).
- Kerala state:
  - It accounts for every fourth migrant in the Gulf region.
  - Its remittances crossed ₹ 1 trillion in 2019 and made up 36% of Kerala's GDP and 60% of the state's debt.

2. Stimulus and rating agencies (LM 4/5/20)

- With the rising economic disruption caused by the pandemic, there are warning signals of deteriorating financial situation and possible credit rating downgrade.
- All the three rating agencies have slashed their GDP forecasts for India.
- Fitch has already warned that further deterioration in the financial sector would pressure the sovereign credit rating in the light of limited fiscal headroom India had when it entered into the crisis.
- In this situation, it does not help that India has the lowest rating (BBB-) in the investment grade in both S&P and Fitch.
- The credit ratings have an influence on FDI and FPI. Foreign sovereign wealth funds, pension funds, etc. are bound by their rules not to invest in the non-investment grade papers (junk bonds).
- However, many experts have pointed to the outflow of foreign investors as a result of the pandemic. Hence, the credit rating should not be a priority right now.
- Having said so, the India bond market is already under pressure and another boil down in this market could dent the image. On the other hand, economy needs a stimulus and robbing the economy from that would lead to growth slowdown which would again lead to credit rating downgrade.
- One way to take care of this is that the policy makers become transparent over the fiscal numbers and make the case for stimulus and also fiscal glide path.

3. 99% of CKP Co-op bank depositors will get their deposits (BL 4/5/20)

- 99.2% of the depositors will receive full payment of their deposits from the Deposit Insurance and Credit Guarantee Corporation (DICGC).
- RBI has cancelled the license of the bank as there has been no scope of revival.
- The net worth of the company has entered into a negative territory. As on March 31st, it stood at -₹ 247 Cr.

4. SC says Coop banks on par with other lenders under Sarfaesi Act (LM 6/5/20)

- A 5-judge bench of the SC unanimously has ruled that cooperative banks were part of the Sarfaesi Act 2002 (Securitisation and Reconstruction of Financial Assets and Enforcement of Security Act).
- This is a stringent law which allows the secured creditors to take possession of the asset of a borrower who fails to pay dues within 60 days of demanding repayment.
- The bench has stated that these banks come under the category of banks as defined under Section 2(1)(c).
- As per RBI report, there are 1551 UCBs and 96612 rural cooperative banks as of March 2017. The latter group accounts for 65.8% of the total assets of all cooperative banks.
- With this ruling, the cooperative banks will be having better control over handling defaults and control over the defaulters in negotiations.

5. Reduce the preference for cash (LM 12/5/20)

- The cash held by the public has surged post the pandemic. By 24th April, there were currency notes of about ₹ 24.2 trillion that were out there in the hands of the people, this was despite the apprehension of the RBI that the notes could end up as a carrier for the virus. By end of April, there was more cash in the hands of the public than it was before demonetisation (₹ 18 trillion).
- The money (in the form of cash) is kept for three reasons:
    - To spend on consumption
    - Invest to get returns
    - Contingency needs
- With the onset of the pandemic, the supply has got disrupted and the sellers of commodities such as vegetables have been demanding payment in cash.
- People, at the hint of a problem, withdraw money from the banks and keep it in the form of cash, as nothing beats the liquidity of cash during a crisis.
- The currency demand has to come down and for this, there is a need to ensure that the digital money is also liquid.

6. Monetising the deficit is not a good idea (BL 13/5/20)

- For some time now, experts have been saying that the deficit of the government will be overshooting the budgeted numbers by a very large margin and recently, the government has disclosed that the estimates have shot by 54% compared to budgeted estimates.
- The gross borrowings are pegged at ₹ 12 lakh Cr.
- The borrowings of the government last year were as large as the savings in the households. Now if the borrowings of the government increase, it means that the demand for such securities is lower than the supply, and the central banker has no option but to purchase these securities (otherwise the rates on G-sec will soar).
- But such monetisation of the deficit is not desirable.

- The argument that with rising deficits there would be a rising interest rate is not correct. In fact, it has been seen that during crisis, the interest rates on G-sec have in fact, fallen as the private investment declines.
    - During 1999-2000 downturn, the rates on G-sec crashed from 12% to 5%.
    - During the Global Financial Crisis, the rates again declined from 9% to 5%.
    - During this cycle itself, the rates have come down from 8% (in September) to 6% now.
- With monetisation done by the RBI, the money supply in the market increases and the inflationary trend also increases.
- On the one hand, the RBI has to follow inflation targeting and on the other, it is monetizing the deficit. This would dent the credibility of the central banker and if the market feels that, then there would be certain issues.