MYND BULLETIN

A simplified view of impact of Covid-19 Pandemic on Indian Industries

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AV OVERVIEW

With the number of COVID-19 cases leaning dangerously more than 3,145,407 and the worldwide death toll crossing more than 221,283. The World Health Organization (WHO) declared the virus outbreak a pandemic in the second week of March 2020, four months after the novel virus first made headlines.

Nearly 28 countries currently are under partial or Complete lockdown, and businesses across the globe are operating in fear of an impending collapse of global financial markets. This situation, clubbed with sluggish economic growth in the previous year, especially in a developing country like India, is leading to extremely volatile market conditions. Let's understand how the coronavirus is impacting business and subsequent tax reforms in India. With rising unemployment, interest rates, and fiscal deficit, the economy in India has seen better days. Adding fuel to this fire is the novel Coronavirus that is sending tremors down Indian trade markets dependent on China for imports.

Opportunity in a crisis

Like India, several international economies are becoming cognizant of the risk they face by being overly dependent on one market. Making the current situation a learning opportunity, CXOs of Indian multinationals, who recently attended the annual meeting of the Confederation of Indian Industry (CII), believe this is the time India can work on capturing potentially 40% of their competitor's market share by looking at indigenous production of goods, furthering the country's Make in India campaign.

	Output compression Q1 FY 2021 vs Q4 FY 2020,[1] %	GDP share, %	Bank credit FY 2019, %[4]	Employment FY 2018, millions	
Airlines and hotels	–70 to –75	2	1[5]	8[7]	
Auto and advanced industries	–50 to –60	2	1	•	
Construction and real estate	–50	8	11	54	
Textiles	–50	2	3	•	
Freight and logistics	–40 to –45	8	2[6]	22[6]	
Metals and mining	–35 to –40	7	7	•	
Oil and gas	–20 to –25		2	•	
Power	–20 to –25	2	9	3[8]	Manufacturing
Consumer and retail	–20 to –25	11	11	47	56
Chemicals	–15 to –20	2	1	•	
Agriculture	–15[2]	15	18	205	
IT services	–10 to –15	5	0	4	
Pharmaceuticals	–10 to –15	1	1	•	
Telecommunications	0 to –5	2	2	1[9]	
Total		67[3]	69	402[10]	

Source: McKinsey

Industries captured in this newsletter

Automobile Sector

How bad has the supply disruption from China been?

China accounts for 27 per cent of India's automotive part imports and major global auto part makers such as Robert Bosch GmbH, Valeo AS and ZF Friedrichshafen AG have factories located in the Hubei province. Owing to the closure of the factories of these companies, there has reportedly been a delay in the production and delivery of vehicles like Bharat Stage Four (BS-IV) compliant models.

How bad has the impact been on demand?

In March 2020, all OEMs witnessed a sharp drop in wholesales due to COVID-19 related lockdown and BSVI transition. COVID-19 led to supply chain disruptions and production halt in the latter half of March 2020.

In case of PVs, OEMs like MSIL, Hyundai and Toyota outperformed its peers, driven by early shift to BSVI and low BSIV inventory. While MSIL dispatched c.77,000 units in the domestic market with sales declining 48% YoY, sales of Toyota/Hyundai declined 45%/41%, respectively. In 2Ws, OEMs faced issues over existing BSIV inventory with the dealers, which was exacerbated by COVID-19 related lockdown and a limited relief from SC on sale of BSIV inventory.

According to a report released by the Fitch Solutions, vehicle production in India is likely to contract by 8.3 per cent in 2020 following an estimated 13.2 per cent decline in 2019. Covid-19 will also make the transition to BSVI emission norms difficult.

What’s the near-term outlook for the auto sector?

HDFC Securities says the auto industry in India is expected to witness multiple disruptions, from Mobility services and Electric Vehicles in the medium term. It said EVs are at the startup stage of the S-Curve, while shared mobility is in the growth stage. However, sustained profitability is essential to ensure scale and longevity of operations and business models will continue to evolve on the roadmap to profitable growth.

Aviation Sector

How severe is the lockdown impact on airlines?

Aviation is among the worst-affected sectors amidst the Covid-19 crisis that has taken the scale of a pandemic. According to the International Air Transport Association, airlines globally can lose in passenger revenues of up to $113 billion due to this crisis.

Airfares have also come under pressure due to nearly 30 per cent drop in bookings to virus-affected destinations. As a result, airfares to such destinations have fallen by 20-30 per cent. Domestic traffic growth is also gradually being affected with domestic travellers postponing or cancelling their travel plans. Some companies have reported more than 30 per cent drop in domestic travel this summer compared with last year. Airfare in the popular domestic routes have been reduced by 20-25 per cent and airfares are expected to remain subdued for the summer season as well. Cash reserves of airline companies are running low and many are almost at the brink of bankruptcy. Moreover, the crisis could lead to loss of jobs and pay cuts. Some airlines have asked many of their employees to go on leave without pay. Air Deccan has suspended operations and sent employees on unpaid leaves.

What is the near-term outlook for airlines?

While some airlines did started accepting advance bookings in anticipation of easing of the lockdown after April 14, but had to cancel all the bokings after the announcement of the second phase of the lockdown. Motilal Oswal said post the lockdown, domestic operations (mainly on key/metro routes) should see a staggered start to operations.

Indian carriers are using a hawk-eyed approach in resuming domestic operations; however, the rate of PLFs will be a key concern. The brokerage said its airfare tracker suggests average yield across metro routes has declined by ~30% year to date for both 30-day/15-day ticketing windows.

For Indian carriers, Q1 is typically the strongest period while Q2 is a weak quarter. As the lockdowns/shutdowns are playing out in Q1, the brokerage expects gradual improvement in the dynamics of the Indian aviation industry only from Q3 of FY21.

Healthcare

The healthcare sector is at the epicentre of this unprecedented global pandemic challenge, and the private sector has risen to the occasion, by offering to the government all the support it needs, be it testing support, preparing isolation beds for the treatment of Covid-19 positive patients or deploying equipment and staff in identified nodal hospitals

Will private healthcare providers benefit?

While the private healthcare sector is fully prepared for every eventuality, it is also a reality that, unlike other sectors, the sector is facing a twin-burden:

a) Investing additional manpower, equipment, consumables and other resources to ensure 100 per cent preparedness for safety in the hospitals and eventual treatment of patients, if needed.

b) Experiencing a sharp drop in OP footfalls, elective surgeries and International Patients.

The industry has been witnessing loss of business and this trend is expected to continue for the near future (at least 3-6 months), and the fact that the sector's costs are predominantly (around 80 per cent) fixed, it is expected that there will be losses and severe impact on cash flows.

It is likely that whenever the government announces any fiscal stimulus, this industry will be looked at favourably. The industry is also likely to benefit from increase awareness about healthcare and the more government focus that this endemic is likely to result in.

What is the impact on India's medical devices industry?

The medical devices industry has also taken a hit. The country imports consumables, disposables and capital equipment including orthopaedic implants, gloves, syringes, bandages, computed tomography and magnetic resonance imaging devices from China. Due to the current crisis in China, the medical device manufacturers across India are finding it difficult to source important raw materials and electronic components from Chinese factories.

Hospitality & F&B

Budget reallocations, diversion of marketing spends, postponing investment plans, and consolidation are among the measures which the hospitality and food & beverage (F&B) industry players are embarking on to deal with the fallout of the lockdown in the country.

According to Noesis Capital Advisors, a hotel investment advisory firm, FY20 financial performance of this industry will be 15 per cent lower from their budgeted targets. Post nationwide lockdown, “10 per cent of inventory is operational and for this limited inventory, occupancy level is 20 per cent,” said Nandivardhan Jain, CEO, Noesis Capital Advisors.

According to Hotelivate, a hospitality consultancy firm, losses for Q4 FY20 and Q1 FY21 are estimated at about ₹620 crore.

Impact on FY21

According to industry experts, this calamitous phase is likely to last at least for the first half of FY21. Thanks to the hesitation to travel, the first quarter will witness the worst impact, despite the lifting of the lockdown. It’s forecast that players are staring at losses of between 30 per cent and 50 per cent. “Overall, Q1 will see a slide of 30-35 per cent on y-o-y basis,” said Bakaya of Sarovar Hotels.

Survival

According to industry experts, this is the survival of the fittest. Thus, while many businesses will go belly-up, some will merge with larger companies.

On the flipside, real estate prices are expected to be lower due to slow pick-up in demand (and expected property tax rebates). Thus, hotels that are renewing their leases this year will benefit, according to Kaul of Frost & Sullivan.

India pharma's global standing

The Indian pharma industry has been a world leader in generics both globally and in domestic markets contributing significantly to the global demand for generics in terms of volume. Made-in-India drugs supplied to the developed economies such as the US, EU and Japan are known for their safety and quality. In recent years, India has seen increasing competition from China, which it has been able to leverage due to its inherent cost advantage, manufacturing intermediates and APIs at a cost much lower than those in India which has resulted in a gradual increase in API imports from China to India and this in turn has led to killing of domestic manufacturing capacity for certain key APIs and their advanced intermediates.

Supply chain disruption for India pharma

Any disruption in supply chain of APIs can result in significant shortages in the supply of essential drugs in India. Some of the critical APIs for high-burden disease categories such as cardiovascular diseases, diabetes and tuberculosis are listed in the National List of Essential Medicines (NLEM). In fact, the current market is largely dependent on China for many antibiotic APIs manufactured by the fermentation route such as penicillin, cephalosporins and macrolides.

The increased dependency of low-cost API is mainly attributed to China's extensive efforts towards developing economies of scale, easing regulations for bulk drug manufacturers, availability of low-cost utilities, building process efficiencies and supporting manufacturers in the form of subsidy, low taxes and fiscal incentives. India has significantly lost out on the API manufacturing owing to the inadequate government support and API focused infrastructure coupled with complexity in getting approvals for setting up a manufacturing plant, delayed pollution clearances, high cost with low availability of utilities, regulatory and price control regime are some of the key challenges faced by the bulk drug industry.

Power Sector

The long-term impact of the current situation would only become apparent with time. Nevertheless, some early impacts of COVID-19 on the Indian power sector are already becoming evident. This article identifies these early impacts to create a basis for future discussion to aid in mitigating adverse effects and better preparing the power sector for such events in the future.

COVID-19 impact on the power market

Until now, the trade in the wholesale market is in four market segments

1) Day-Ahead Market 2) Term Ahead Market and

3) Renewable Energy Certificates 4) Energy-saving certificates

Recently, the Central Electricity Regulatory Commission (CERC) finalized the regulations for implementing real-time markets. This half-hourly market will enable intra-day trade of electricity, allowing adjustment of generation and consumption profile during the day. Before the COVID-19 pandemic, it was announced by CERC that the real-time market would be operational from April 1st, 2020. However, the starting date has now been delayed by two months to June 1, 2020. According to media reports, due to the COVID-19 pandemic, some required trials could not be completed. This delay in the real-time market implementation is likely to have a serious, adverse impact on the Indian power market. Another impact of the COVID-19 pandemic on the power markets is in terms of the market dynamic. It can be observed that there is a dip in the clearing volume and the market-clearing price, which coincides with the gradually increasing shutdown measures taken by the government as a response to COVID-19. Thus, the reduction in demand due to the lockdown is reflected in the volumes traded on the electricity market and the clearing price.

Future Steps

Currently, we are at an early stage of discussion on the impacts of COVID-19 on the Indian power system. This article takes steps in identifying and documenting the early impacts that are evident for the grids as well as the markets. As more data becomes available, a quantitative analysis needs to be done to understand the severity of the issues identified. Furthermore, more discussion needs to take place on: firstly, mitigation of any long term risk to the Indian power sector and secondly on making Indian power sector better prepared for such crisis in the future.

Retail

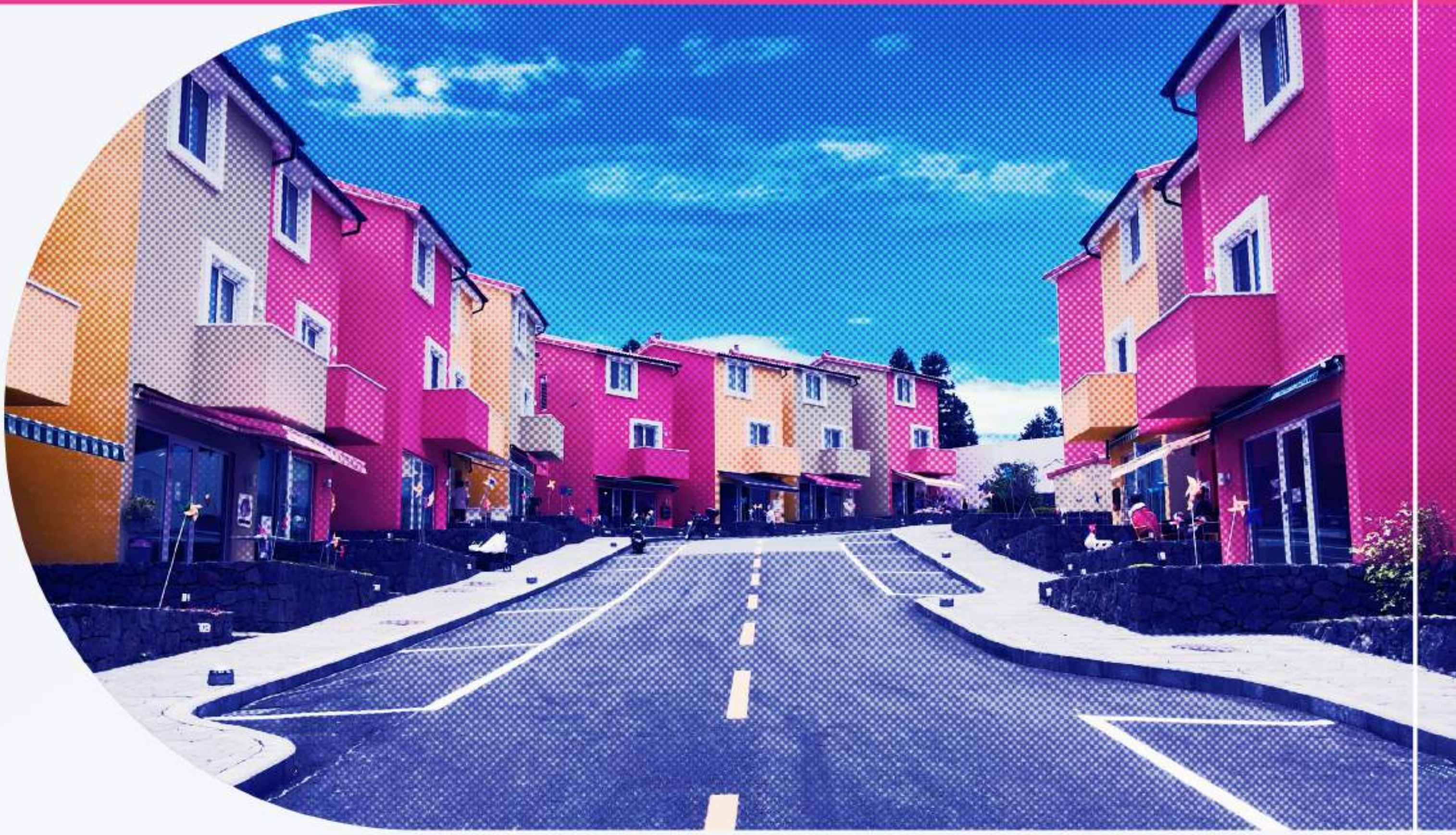
The outbreak of coronavirus is having a severe impact on people, economy and business. As responsible corporates, all retail players are adopting necessary preventive actions to ensure safety of their employees and customers. The end objective is to ensure easy and uninterrupted availability of essential food and grocery products at affordable prices so that people don't panic. During these critical times, it is imperative for all stakeholders to come together. Given the widespread effect of Covid, business across sectors is looking gloomy, impacting economy at large. Shutting down of malls and shops has severely hurt business for all retailers. This could lead to major job losses as companies won't be able to sustain this for too long.

Channel checks indicate severe disruption for consumer companies too with a sharp 50%+ drop in sales during the ongoing lockdown. While staples are relatively less affected and should recover, paints and retailers may see the impact continuing beyond the lockdown.

Major earnings cuts ahead

Emkay Global says the fall in crude prices and moderating agri-input prices should drive margin gains for most staples. But, it cut earnings estimates by 3-15% due to the impact of the disruption and a slow recovery.

Real Estate



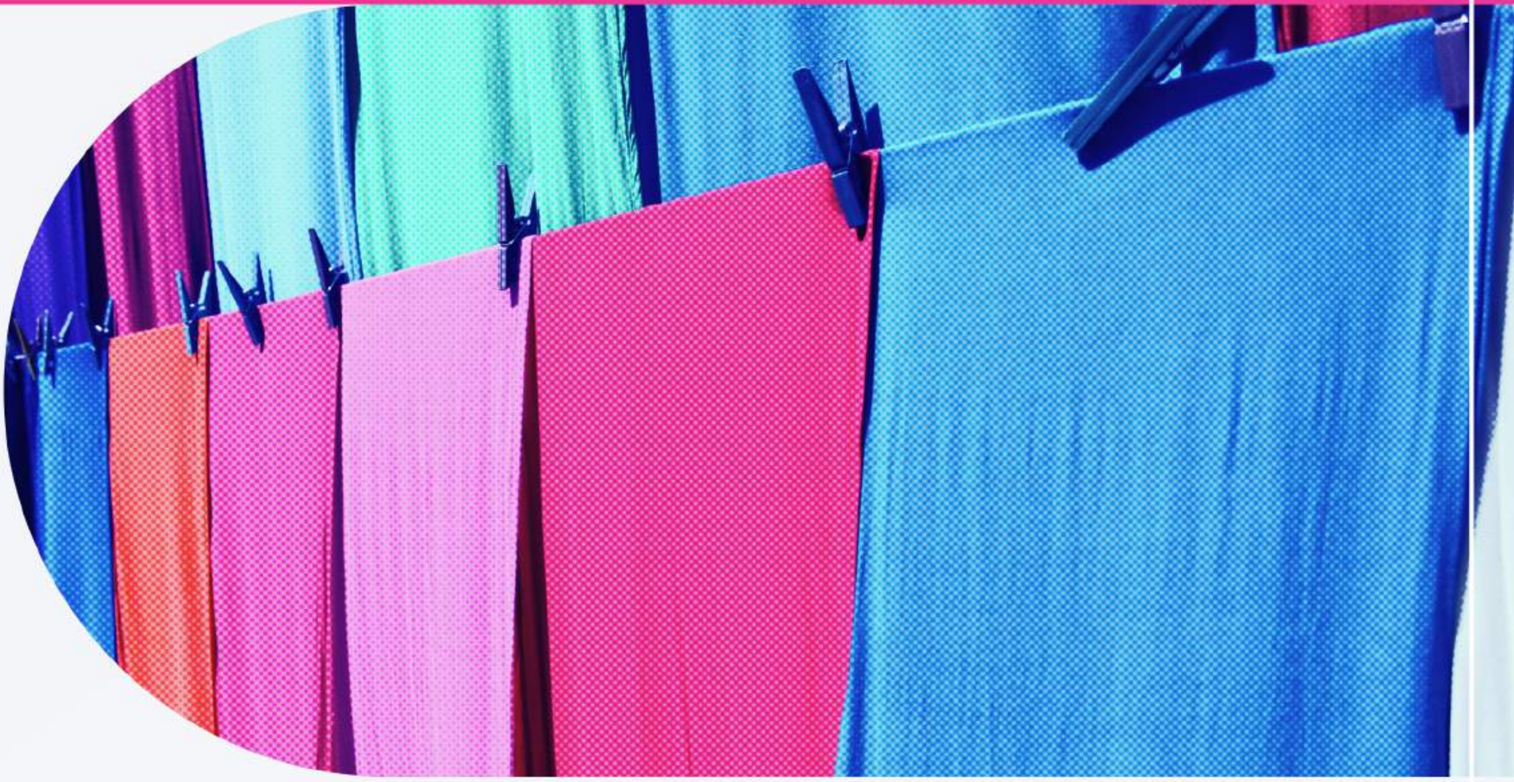
Deepak Parekh, Chairman of mortgage lender Housing Development Finance Corporation (HDFC) said the real estate prices in the country would correct by up to 20 per cent in the wake of coronavirus pandemic and the resultant nationwide lockdown.

Prices of real estate have to come down, and will come down," Parekh said in an address to real estate developers at a webinar organised by the National Real Estate Development Council (Naredco). "I believe Naredco's estimate is around 10-15 per cent. One must be prepared for even 20 per cent," he added.

For potential home buyers, who have job security or cash flows, it will be an excellent buying opportunity, he said. "Real estate is an immensely important asset class, and the value of global real estate was more than the value of all the stocks and bonds combined," he said. Parekh said Indian real estate market was already going through prolonged pain for various reasons such as economic stress in certain segments, high leverage, tight liquidity and rising non-performing assets (NPAs) in construction finance.

The global economic slowdown coupled with COVID-19 pandemic is likely to negatively impact residential real estate demand in the country this year. According to the rating agency India Ratings, residential real estate demand is expected to decline in financial year 2020-21 (FY20) after showing a slight improvement in the year 2017 to 2019.

Textile



There could be as many as one crore job cuts in the textiles sector, which has been severely hit by the ongoing lockdown, if there is no support and revival package from the government, according to apparel industry body Clothing Manufacturers Association of India. With around 80 per cent of the garment industry mostly micro, small and medium enterprises, CMAI, which has around 3,700 members employing over 7 lakh people, said most of its members do not have the kind of reserves to see them through 3-6 months of this magnitude.

Seeking a financial package from the government for the industry, CMAI Chief Mentor Rahul Mehta said interventions like wage subsidies must be taken up, otherwise there would be huge job losses.

If the garment industry closes down, it would impact the entire value chain from fabric supply industry to brand to the zipper and label industry, he said. "If you look at the entire textile industry, I see a job loss of one crore if nothing is done by the government," he added. He, however, appreciated efforts taken up by the textiles ministry such as asking all leading global companies not to cancel orders from the Indian exporters and such steps send positive vibes to manufacturers, particularly to the small ones.

Mehta said CMAI has done a survey among its members and analysed around 1,500 responses. "The responses were quite frightening. Almost 20 per cent of them said that they were thinking of closing down the business after lockdown. At least 60 per cent of them anticipated a drop in revenue to the tune of 40 per cent, which is massive, if you look in terms of number of employment," he said.

Telecom

Reliance Jio, Bharti Airtel and Vodafone Idea are expected to have added just half a million subscribers cumulatively in March, a sharp fall from the monthly average of up to 3 million additions in a good month, as the Covid-19 induced lockdowns take a toll, say industry players and analysts. They add that with no footfalls in stores and barely any mobile number portability (MNP) on, user addition numbers will remain around the sharply reduced levels for April too.

Usually, anywhere from 2.5 to 3 million net adds could be expected on an average every month. With the emergency conditions in place, operators may find it difficult to add half a million net adds in each of the months of March and April. Since the three-week lockdown was announced, they have closed their stores and all MNP activity has almost halted since there are no officers to coordinate between the telcos, the customers, and the MNP providers.

Another reason for the fall in subscribers is the slowdown in MNP. "There has been a 95% drop in portability requests from the couple of millions that the two companies would get per month. There are no office staff so work on that has almost halted," said a senior executive aware of the lags in MNP during lockdown.

Retailers say their numbers are now down to zero and it will be a while before business picks up.

Tourism

India is big on cultural and historical tourism, attracting domestic and foreign nationals throughout the year. It does not come as a surprise that a large number of confirmed COVID-19 cases in India include foreign tourists. But with visas being suspended and tourist attractions being shut indefinitely, the whole tourism value chain, which includes hotels, restaurants, attractions, agents, and operators is expected to face losses worth thousands of crores. Experts believe the tourism industry is likely to take a massive hit, and it could end up crippling the industry for the near future.

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