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LESSONS FROM THE UNPRECEDENTED PANDEMIC: AN ECONOMIST'S PERSPECTIVE

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ABSTRACT

The global economy is passing through the worst economic crisis of modern times since the beginning of 2020 due to the outbreak of an unprecedented pandemic resulting from the spread of novel Corona or Covid-19 virus. The abruptness with which this pandemic erupted and the fast pace at which its disruptive and disastrous impact spread across more than 220 countries of the world makes it a serious area of concern. The emerging challenges are even more daunting in the case of Indian economy owing to the huge population base, high population density and grossly deficient health infrastructure in India. It is against this backdrop that the present paper goes deeper into the important lessons that can be learnt from the unprecedented pandemic and analyses them from the perspective of an economist. In particular, the significance of contingency planning, building-up of reserve capacity, overcoming institutional rigidities and infrastructural bottlenecks, gradualism and cautious optimism are brought to the fore. Besides, issues relating to the demand-side as well as supply-side management of an economy as also resource mobilisation for effectively tackling the pandemic are also discussed. The whole discussion provides useful insights for public policy-making that can be reasonably expected to go a long way in improving the policy environment in the times to come.

Keywords: Contingency Planning, Reserve Capacity, Infrastructural Bottlenecks, Gradualism, Cautious Optimism.

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1.1 THE EMERGENCE OF A GLOBAL ECONOMIC CRISIS ON ACCOUNT OF PANDEMIC

In the present-day globalised world, economic crises seem to have become the order of the day. For, due to the underlying integration of global economies in the contemporary "global village", the disturbances arising in any part of the real or financial sector of an economy tend to spread very fast across other countries of the world. In recent past, the root cause of global crisis could be located in the malfunctioning of banking and financial sectors of advanced and developed economies. For instance, the "North Atlantic Financial Crisis" popularly known as the US Sub-prime Lending Crisis, emanating in late 2000s is a grim testimony to the flip side of Globalisation and amply proves that the formation of a "global village" in modern times is not an unmixed blessing.

From the beginning of 2020, the experience of global economy reaffirmed that "Globalisation" is indeed a double-edged sword in the sense that apart from its potential gains, it could quite conceivably entail huge costs for different countries of the world so much so that within a span of few months, they could be pushed into a deep recession. But this time, unlike in the recent past, the emerging global economic crisis could be attributed to a Pandemic arising out of the unprecedented spread of novel Corona *i.e.,* Covid-19 virus.

The Ministry of Finance, Govt. of India (2021a) considers this global crisis as a unique recession where 90% countries of the world are likely to experience a contraction in GDP per capita. Likewise, in the context of the enormity and all-pervasive nature of the pandemic, the Ministry of Finance, Govt. of India (2021b) observes that ever since its first outbreak, Covid-19 has infected more than 220 countries and all continents including Antarctica.

Given the huge population base coupled with a high density of population in India, there is no denying the fact that the unprecedented pandemic posed a formidable challenge for the India economy too, particularly in the light of its grossly inadequate and highly deficient health infrastructure. Nevertheless, the ongoing experience of tackling an economic crisis of such an unprecedented magnitude has taught a few important lessons to the policy-makers that can be reasonably expected to go a long way in improving the policy environment in the times to come.

The basic purpose of the present paper is to identify from an economist's perspective, the most prominent and useful lessons that can be learnt from the recent experience with the unprecedented Covid-19 pandemic so as to derive useful insights for policy making. Towards this end, Section 1.2 discusses the urgent need for contingency planning and maintaining sufficient “reserve capacity” with a view to effectively handling unprecedented, uncertain and unpredictable situations such as severe economic crises emerging out of epidemics and pandemics. Further, Section 1.3 goes deeper into the policy dilemma of choosing between lives on the one hand and livelihoods on the other, in the face of a pandemic-like situation. Utilising the sound principles of optimisation in economics against the backdrop of binding constraints, it advocates that for prudent public policy making, protection and preservation of lives shall be the first and foremost priority area for any rational planner and policy-maker. This is followed by a detailed discussion in Section 1.4 on demand *versus* supply-side management of an economy passing through an unprecedented pandemic in order to chalk out the most desirable growth path that could optimally utilise all the scarce resources available to the economy. The issues relating to the mobilisation of resources for financing various schemes and programmes of the government for combating the Covid-19 pandemic are discussed in Section 1.5. And finally, the conclusions following from the discussion of the preceding sections are recorded in Section 1.6.

1.2 THE NEED FOR CONTINGENCY PLANNING AND CAUTIOUS OPTIMISM

The global economic crisis resulting from the Covid-19 pandemic has clearly established that when it comes to the state of the economy, we can no longer afford to be over-complacent and shall resist from taking things for granted. For, the abruptness with which this pandemic suddenly erupted and the pace at which its disruptive and disastrous impact was felt across different countries, it shook the very foundations of their economies and threatened what was so far treated as something quite “normal” for any economy whether advanced, developing or even less developed.

For instance, prior to the outbreak of Covid-19 pandemic, no one could really imagine that despite such rapid advancements in science and technology in modern times, someday even the routine movement of economic agents and mobility of factors of production will have to be curtailed to such an extent that the day-to-day life of individuals itself will almost come to a standstill. In this connection, even United Nations Conference on Trade and Development (2021) concedes that nobody had anticipated the arrival of Covid-19 or its dramatic global impact. Likewise, with reference to the disastrous impact of the pandemic, the Niti Aayog (2021) observes that the Covid-19 pandemic has devastated health systems and economies alike.

From the perspective of an economist, it can be reasonably contended that the pandemic created a strange situation wherein economies were forced to operate below their production possibility frontiers, not because of inefficiencies but rather because of considerations of public health and safety. Many industrial and manufacturing units had to be temporarily shut down in order to prevent the spread of the deadly Corona or Covid-19 virus and even when they were gradually opened up later, the production remained below potential levels due to the compulsions imposed by Covid appropriate behaviour including “social distancing norms”, so crucial for putting a check on the spread of the dangerous disease.

In the light of all these adverse developments, it became very clear to the planners and policy-makers that it was no longer advisable to expect results in an economy merely relying on the prescriptions of traditional economic theory. For, the uncertainties posed by epidemics and pandemics may significantly deviate us from the attainment of various policy targets. Thus, the only viable option for effectively implementing any economic policy is to make room or provision for such uncertainties at the stage of policy formulation itself.

That is to say, the need of the hour is "contingency planning" which in turn can be accomplished by building up and maintaining sufficient "reserve capacity" to tackle any exigencies or emergency situations. A classic example in this context is provided by the acute shortage of oxygen faced during the so-called "second wave" of Covid-19 pandemic in India during April and May 2021. With reference to the impact of this second wave of pandemic in India, the Reserve Bank of India (2021a) observes that the health infrastructure of the country including supply chains and logistics of oxygen and other life-saving drugs and equipment came under intense pressure.

On the face of it, what appears surprising is that how could a shortage of oxygen occur in a country like India which is one of the prominent producers of oxygen in the world generating around 7000 metric tons of oxygen a day. Even if it is admitted that the whole of oxygen produced in a day is not "medical oxygen" and the demand for the latter may have increased manifold during the second wave of pandemic, yet the issue of acute shortage of medical oxygen cannot be fully resolved without reference to the *institutional rigidities* and *infrastructural bottlenecks*, so characteristic of the Indian economy. For, technically it is not difficult to convert oxygen into medical oxygen at a short notice, and even the soared demand for medical oxygen during the second wave of pandemic was far below the overall daily production of oxygen in the country.

A closer examination of the issues at hand reveals that the real problem was not a shortage of oxygen *per se* but rather that of a proper distribution of oxygen across regions which in turn calls for a proper infrastructure for transportation of medical oxygen from surplus to deficient areas. More specifically, most of the oxygen producing industrial plants are located in eastern States of India whereas the maximum demand for medical oxygen arose in far-off regions like Delhi and Mumbai during the second wave of Covid-19 pandemic. But neither the transport network needed for carrying medical oxygen over such long distances up to the mark, nor the system was fully equipped and geared up to meet such challenges on an urgent basis due to the lack of requisite "contingency planning". Further, the non-availability of adequate or sufficient number of oxygen containers posed as yet another binding infrastructural constraint thereby adding fuel to fire so to say.

To give an analogy, it is widely acknowledged in contemporary economic literature that despite the onslaught of a drought or 'crop failure' conditions in a particular region, the occurrence of a “famine” or mass starvation deaths can be averted by transporting food grains to that region from food grains surplus regions in time. In fact, this is the rationale behind the well-known “Buffer Stock Operations” of the Government. But why such operations have been found to be successful in the Indian economy is because of the underlying approach of “contingency planning” whereby food grains procured during bumper crop years are properly stored in the warehouses of Food Corporation of India so that they could be easily transported to food grains deficient areas in the face of drought conditions, thereby preventing a famine in those areas.

Evidently, unlike the Buffer Stock Operations wherein the required transportation and infrastructural base was well developed, the requisite infrastructural support was not forthcoming in the case of “medical oxygen” which in effect aggravated the crisis. In view of this, it becomes all the more desirable for planners and policy-makers to pay more attention to “contingency planning” *i.e.*, developing the requisite infrastructural base to tackle and effectively handle an emergency situation well in advance rather than taking things for granted. Building up a “reserve capacity” goes hand in hand with such a policy strategy in as much as the policy-maker shall be easily in a position to augment production at a “short notice” as and when the pressing need for the same arises.

If and only if the policy-makers adopt such a cautious approach based on the twin pillars of “contingency planning” and building-up of “reserve capacity”, can they afford to be optimistic for the future. In other words, the pandemic experience has thoroughly established that the need of the hour is for economic planners and policy-makers to be “cautiously optimistic” *i.e.*, strictly adhere to the approach of “cautious optimism”.

1.3 POLICY DILEMMA: A TRADE-OFF BETWEEN LIVES AND LIVELIHOODS

Under normal conditions, lives and livelihoods go hand in hand in an economy. For, the quality of life of an individual is itself conditional on his or her source of livelihood. That is why, economic theory invariably advocates placing thrust on the provision of productive and gainful employment to economic agents so that they can earn a reasonable income to sustain life and finance their basic minimum needs. In sharp contrast, however, the Covid-19 pandemic created a strange situation wherein the protection of lives came in conflict with the protection of livelihoods. To put it differently, the pandemic led to a "Trade-off" between lives and livelihoods whereby with a view to protecting the lives of labourers, it became inevitable to compromise on their employment and sources of livelihood at least in the short-term.

To be specific, arresting the spread of the deadly Covid-19 virus called for immediately restricting social contact through the imposition of a country-wide lockdown, but doing so amounted to depriving a large segment of working population such as casual labour and daily-wagers of their source of livelihood at least for the time being. Confronted with such an unprecedented situation, the planners and policy-makers realised that the loss of employment was a "temporary" phenomenon whereas any possible loss of life was in sharp contrast "permanent" in nature. For, any loss of a source of livelihood encountered during the short-term can be easily "reversed" over the long-term while any loss of precious life was evidently "irreversible".

Thus, after thorough deliberation, the policy-makers accorded precedence to lives over livelihoods. Such a policy stance was well in line with the basic principles of economic theory following from optimisation in the face of binding constraints which suggest that in a situation wherein loss is inevitable, rationality dictates that loss minimisation is equivalent to profit-maximising behaviour. For example, despite incurring losses under perfect competition, a rational firm continues to operate so long as the variable costs are covered since fixed costs are in any case "sunk costs" that cannot be recovered in the short-term even if the firm stops production and closes down. Thus, as long as the price or average revenue is in a position to cover average variable cost, it is still profitable to carry on with production since it minimises on the losses. It is only when the total revenue can no longer cover even the total variable cost that the perfectly competitive firm decides to close down or shut down.

In an exactly analogous manner, when the planners and policy-makers confronted with a pandemic situation realised that it was no longer possible to avoid a loss, they tried to minimise the extent of total loss by choosing the lesser of the two evils under consideration *viz.*, the loss of livelihoods in the short-term. For, it was worth tolerating the pain of loss of employment in the short-term in order to derive the long-term gain resulting from the protection and preservation of precious lives. With a view to mitigating the hardship faced by poor workers having lost their source of livelihood on account of the lockdown, they were provided with State support in the form of direct benefit schemes like cash transfers, free distribution of food grains and the like. Thus, it follows that whenever policy makers face a dilemma of choosing between lives and livelihoods, prudence in public policy making dictates that they must always go in for the protection and preservation of lives as the first and foremost priority area since in a situation wherein loss is unavoidable, it is loss-minimisation that is tantamount to profit-maximisation.

1.4 POLICY IMPERATIVES: DEMAND VERSUS SUPPLY-SIDE MANAGEMENT

The Covid-19 pandemic, and the subsequent lockdown undertaken to contain it, tended to affect both the supply as well as demand conditions in the economy adversely. In this context, the Reserve Bank of India (2021b) in its Annual Report 2020-21 has very aptly observed that the pandemic produced the fusion of an aggregate demand shock which was broad-based and a supply-shock that was lockdown-induced.

That the supply of commodities gets curtailed under such constrained situations is quite obvious. For, when the industrial and manufacturing units are temporarily shut down and stringent restrictions are imposed even on the movement of economic agents during a lockdown, the supply position cannot evidently remain normal.

Likewise, even if agricultural production was not as hard hit as industrial production during the country-wide lockdown, the supply of agricultural products was nevertheless hampered by the disruption of transportation services on account of unavailability of requisite manpower.

When it comes to demand conditions in the economy, they too are adversely affected by a lockdown imposed to restrict and control the spread of the pandemic. For, the effective demand in an economy is governed by the "purchasing power" of economic agents along with their "propensity to consume", both of which are adversely affected by the lockdown. Evidently, when a significant proportion of workers and manual labour loses its employment during lockdown, their income and hence their purchasing power goes down thereby affecting the aggregate demand in the economy adversely. Further, in the face of uncertainties posed by lockdown conditions, economic agents typically experience a rise in their "propensity to save" so as to meet exigencies in the immediate future. This in turn lowers their propensity to consume as a result of which, the aggregate demand in the economy is further reduced. In this context, it is worth noting that such a decline in the propensity to consume is more pronounced in the case of "discretionary consumption" *i.e.*, the consumption of non-essential commodities.

In view of this, the policy-makers found it pointless to try to boost discretionary consumption through fiscal incentives so long as lockdown was imposed and its associated 'restrictions' and 'uncertainties' were still prevailing as they tend to raise the propensity to save thereby dampening the propensity to consume. After all, there is no point in pressing the accelerator in a vehicle till its hand-brake is released, otherwise it would only end up in the wastage of petrol or other precious fuel. It was only when the lockdown was eventually relaxed in a phased manner that the Government raised its fiscal spending in India with a view to boosting discretionary consumption in the economy. Till then, the entire focus of fiscal policy was on financing the provision of essential items to economically weaker, vulnerable and downtrodden sections of the society through direct benefit transfers and food subsidy programmes. And when the phase of unlocking the economy started, such a favourable fiscal policy was supplemented by an expansionary monetary and credit policy, covering in its ambit measures to ensure sufficient liquidity and purchasing power in the economy like emergency credit guarantee scheme and temporary moratoria granted to debtors as an immediate relief to debtors. This is how the demand-side management of the economy was effectively carried out by planners and policy-makers during the Covid-19 pandemic.

As far as the supply-side management of the Indian economy during the pandemic is concerned, the essential aim of policy-makers in India was to minimise the supply-side disruptions over the medium to long-term. Towards this end, policy rates were lowered as quite a few firms were suffering financial distress, and sturdy credit growth was ensured for Micro, Small and Medium Enterprises *i.e.*, MSMEs. With reference to a pandemic situation, the International Monetary Fund (2021) too has supported the view that fiscal policy shall provide loans to businesses as also targeted transfers and direct payments to affected households in a "calibrated manner" in accordance with the stage of the pandemic.

Thus, an important insight for public policy making derived from the experience with Covid-19 pandemic is one of "gradualism" *i.e.*, following a step-by-step approach of gradually adapting to the emerging economic environment rather than abruptly and arbitrarily jumping over to a policy stance. Till the lockdown restrictions were continuing, it was in the best interest of the economy to exclusively focus on the provision of necessities to the masses, especially the poorer and economically worse-off sections of the society who had recently lost their source of livelihood owing to the lockdown. But as soon as the lockdown was relaxed, it was found prudent to provide a fiscal stimulus to step up "discretionary consumption" on non-essential items as well. In this way, the most optimal growth path for an economy can simply be chalked out on the basis of the principle of "gradualism".

1.5 FINANCING OF SCHEMES FOR COMBATING COVID-19: THE ISSUE OF RESOURCE MOBILISATION

Evidently, the effective demand-side as also supply-side management of the economy particularly in the face of a crisis situation created by a pandemic like Covid-19 calls for providing a huge quantum of financial resources. For instance, any kind of expansionary monetary and fiscal policy invariably imposes a burden on the public exchequer. After all, ensuring sufficient liquidity and purchasing power in the economy, emergency credit guarantee schemes, temporary moratoria granted to debtors and boosting aggregate demand through fiscal incentives entail enormous costs to the government and the monetary authority.

It is worth noting that the Government of India is already under tremendous fiscal stress as protection of lives in the face of the sudden outbreak of Covid-19 pandemic necessitated remarkably stepping up expenditures on health infrastructure and facilities. Likewise, offering minimum consumption support to the masses especially to the economically weaker sections through food subsidy programmes and direct benefit transfers imposed a heavy financial burden on the already precarious fiscal position of the government.

In view of this, a pertinent question arises as to how the various schemes and programmes announced by the government to combat Covid-19 pandemic are going to be financed in the case of Indian economy. That is to say, the issue at hand is how to mobilise huge financial resources for supporting the officially sponsored programmes to effectively tackle the pandemic in India.

Under normal conditions, government typically relies on direct and indirect taxes to finance its public expenditures. But this channel cannot be relied upon under pandemic conditions since due to the contraction of economic activity, profits and income levels have been adversely affected and thus there is hardly any scope for raising tax revenues through direct taxes. As far as the imposition of indirect taxes with a view to raising tax revenues is concerned, that too is not advisable as it would put unnecessary burden on economic agents passing through hardship and could quite conceivably curtail aggregate demand further thereby aggravating problems on the economic front.

At the same time, under the abnormal circumstances created by the pandemic, we cannot rely too much on non-tax revenues as public sector units are also hard hit by the pandemic and cannot therefore be expected to generate huge surpluses. Similarly, disinvestment of Public Sector Units (PSUs) too does not appear to be a viable option for generating financial resources at the present juncture due to the adverse impact of Covid-19 on the general performance of PSUs along with a slackening of economic activity on account of the pandemic.

Under these circumstances, one plausible alternative for the monetary authority in India is to go in for deficit financing. This for instance can be accomplished by the printing of additional currency by the Reserve Bank of India (RBI) and giving it to the Government of India to finance its different schemes for effectively tacking the Covid-19 pandemic whether for boosting health infrastructure or to offer minimum consumption support to the masses and raising effective demand in the economy.

On closer examination, however, we find that such a policy alternative is more easily said than done. For, deficit financing is likely to lead to demand-pull inflation and is antithetical to the basic spirit of fiscal discipline as embodied in the Fiscal Responsibility and Budget Management (FRBM) Act of 2003. In the present monetary policy regime of "Flexible Inflation Targeting" wherein price stability has been accorded paramount importance, it becomes all the more desirable to keep the annual inflation rate within the tolerance band of 2 per cent to 6 per cent and thus deficit financing is undesirable due to its inflation generating potential.

Given the gravity of situation created by the Covid-19 pandemic and the severe resource constraint faced by the Government of India, however, some economists are nevertheless in favour of "deficit financing" as a viable alternative. For instance, Kumar (2020) is in favour of deficit financing as a means of generating resources to finance increasing government expenditures for mitigating the crisis created by the pandemic. In fact, given the demand-constrained situation created by the pandemic, he is optimistic that instead of being inflationary, a higher deficit will contribute towards maintaining some demand in the economy. The rationale underlying this optimism is that when the demand is drastically low in the economy, the infusion of additional liquidity through deficit financing is likely to bring demand to normal levels rather than leading to demand-pull inflation. In this context, Chakraborty and Thomas (2020) are of the view that innovative sources of financing the deficit such as money financing of fiscal programmes need to be explored.

Now it is for the monetary authority *i.e.*, the Reserve Bank of India in consultation with the Government of India to explore all such possibilities for financing the public expenditure on various schemes and programmes being undertaken to combat Covid-19. For instance, instead of outrightly printing money with a view of financing the deficit of the government, the monetary authority may decide to raise the borrowing of the government through the issue of Covid Bonds to the public. Evidently, which option is eventually exercised by the Government of India in consultation with the Reserve Bank of India will depend upon a number of considerations ranging from price stability to exchange rate stability and financial stability.

But one thing is very clear from the foregoing discussion that financing of various welfare schemes, policy programmes and public expenditure of the Government of India in the fight against Covid-19 pandemic is a really challenging task. To what extent the policy-makers in India are in a position to effectively meet this daunting challenge in the times to come will eventually govern our success in the battle against the pandemic.

1.6 CONCLUSION

Given the huge population base, high population density and grossly deficient health infrastructure in India, the emerging challenges of the Covid-19 pandemic are even more daunting in the case of Indian economy. Looking from an economist's perspective, the pandemic brought to the fore the urgent need for 'contingency planning' by building-up and maintaining sufficient reserve capacity and overcoming institutional rigidities and infrastructural bottlenecks. Further, the pandemic highlighted the significance of 'cautious optimism' and 'gradualism' in public policy making.

An important lesson that the unprecedented Covid-19 pandemic has taught is that during an economic crisis situation of such an enormous magnitude, demand-side management becomes as crucial as the supply-side management of the economy. Evidently, a huge quantum of resources is required under such circumstances so as to finance different schemes for boosting health infrastructure or to offer minimum consumption support to the masses and raising effective demand in the economy. The mobilisation of financial resources of such an enormous magnitude is a challenging task in an economy devastated by the pandemic, and how well the policy-makers in India are able to meet this challenge will govern the course of Indian economy in the coming future.

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