HS 405

Issues in International Trade and Finance

Assignment/Report

Economic Impact of Covid-19 (World Trade & Banking Sector)

Author :
Ajit Singh

Roll no:
1801010

Instructor:
Dr.Kaveri Deb

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1 Introduction and Impact of COVID-19 on World Trade

The COVID-19 Pandemic:

A novel strain of coronavirus — SARS-CoV-2 — was first detected in December 2019 in Wuhan, a city in China's Hubei province with a population of 11 million, after an outbreak of pneumonia without an obvious cause. The virus has now spread to over 200 countries and territories across the globe, and was characterised as a pandemic by the World Health Organization (WHO) on 11 March 2020

As of 8 November 2020, there were around 50 million laboratory-confirmed cases of COVID 2019 infection globally, with around 1.25 million reported deaths.
Increasing numbers of confirmed diagnoses, including in healthcare professionals, indicated that person-to-person spread of SARS-CoV-2 occurred.
As this coronavirus affects the respiratory tract, common presenting symptoms include fever and dry cough, with some patients presenting with respiratory symptoms (e.g. sore throat, nasal congestion, headache, etc.) or even struggling for breath.
In severe cases, the coronavirus can cause pneumonia, severe acute respiratory syndrome, kidney failure and death.

How did COVID-19 impact the general Economy:

The COVID-19 pandemic spread with alarming speed, infecting millions and bringing economic activity to a near-standstill as countries imposed tight restrictions on movement to halt the spread of the virus. Due to the enforced lockdowns by the nations, economic activities came to a sudden halt as people were advised to stay at home and not venture out unless it was for necessary travel or work. This lead to several immediate problems like supply shortages, complete standstill of certain industries like tourism, air travel, oil consumption, Physical Education Centres, etc. which led to heavy losses and even closure of many firms. Unemployment increased and a general income contraction among people was observed. Recession trends were observed across major nations like the USA and the EU. However, this was just scratching the surface. The pandemic brought along possibilities of major future problematic outcomes such as:

- **Should COVID-19 outbreaks persist, should restrictions on movement be extended or reintroduced, or should disruptions to economic activity be prolonged, the recession could be deeper. Businesses might find it hard to service debt, heightened risk aversion could lead to climbing borrowing costs, and bankruptcies and defaults could result in financial crises in many countries. Under this downside scenario, global growth could shrink by almost 8% in 2020**

- **Many emerging and developing economies were already experiencing weaker growth before this crisis; the shock of COVID-19 now makes the challenges these economies face even harder.**

Impact on World Trade: From Supply Chain Point Of View:

An important priority during a pandemic of this scale is to keep the key supply chains for essential goods for the crisis – including medical supplies, food products and ICT goods and services – open and functioning. However, a number of challenges were faced to keep these supply chains going related to the business of trade. For example:

- **Cancellation of passenger flights linked to travel bans limited the availability of air cargo while urgent shipping of essential goods increased demand, resulting in increases in the price of air cargo. Delivery times also increased. This matters for some time-sensitive medical supplies, but also for some high value food trade.**

- **At the time the virus struck, large numbers of shipping containers were in Chinese ports, and restrictions on their movement led to a shortage that has seen the price of containers**

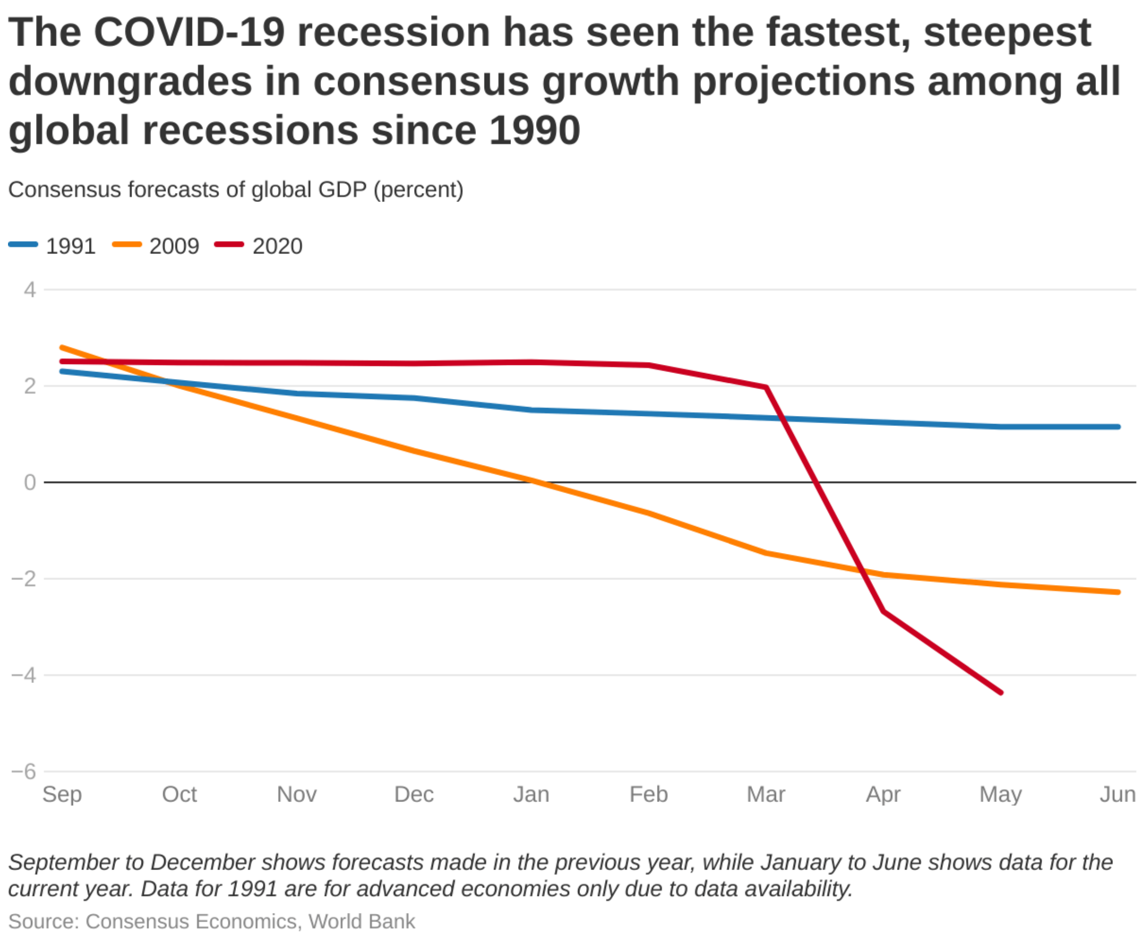

Figure 1: Growth projections during recessions since 1990 (1991, 2009 and the one due to COVID-19

rise (in some cases considerably), with flow-on effects for the price of cargo, including food products.

- **Lockdowns did and are also impacting the availability of labour to unload ships at ports (notably in countries where this is less automated) or raised costs due to increased protective measures for workers.**

- **Limits on mobility of people and lockdowns are affecting a variety of trade processes, from physical inspections of goods, to testing and certification, to changing how anti-dumping investigations are conducted.**

All of these are adding to the time and costs of international trade on products that matter in the moment, such as medical, food and agricultural supplies.

Keeping the trade in essential medical supplies flowing means removing barriers such as tariffs on medical goods essential for combatting COVID-19 (e.g. several countries maintain tariffs of up to 10% on COVID test kits) as a number of countries have already done. It means expediting certification procedures to allow new products to be traded as soon as possible and ensuring that technical requirements are science-based and do not unnecessarily restrict trade. Finally, it means enhanced trade facilitation to keep goods moving as quickly as possible – including identifying key actions needed to ensure smooth customs procedures with limited human intervention.

2 Impact of COVID-19 on the banking sector

Impact of COVID-19 on the general Banking Sector:

COVID-19 has generated significant instability and high volatility in global capital markets. While the full impact is yet to be determined, it's expected that the adverse impact are likely to continue from the virus' knock-on effects.

Two of the areas that are likely to be most impacted by COVID-19 are:

- **Profitability and credit management:** The low interest rate scenario, along with the significant impact of the COVID-19, is reducing the core banking profitability in mature markets. Financial institutions are thus shifting towards commission-based income from the likes of payments and tech businesses.
  One of the immediate effects of the health emergency on the real global economy is the increased credit risk of corporate and retail clients of the banks. In order to continue financing the real economy and support its recovery, banks are called to distinguish between purely temporary phenomena and longer lasting impacts which would require actions of management.

- **Customer relationship (A Positive opportunity for digitization):** Although COVID-19 may lead to a crisis in the real economy, the impact on the banking system and on the bank -customer relationship can also be defined as a 'positive discontinuity' for the purpose of digitization of the sector and the ability to offer an excellent customer experience via various new age ICT tools and cutting edge technologies.
  Banks, even the most territorial and branch-centric ones, are forced to encourage the use of channels that have never been their strategic priority. This is a positive move in the longer run. COVID-19 aftermath could make them even more inclined to accelerate the digital transformation path through partnerships and collaborations within the fintech community.

High volatility in stock markets depressed banks' valuation
COVID-19 has generated significant instability and high volatility in global

capital markets. The financial sector has been one of the most affected, with bank valuations dropping in all countries around the world. Banking stocks were severely impacted during COVID-19. In the period from 01 December 2019 to 30 April 2020 – most banks saw a price slump in mid-March.

Impact on the Indian Banking Sector:

The Indian economy wasn't in great shape even before the Covid-19 outbreak, which only made matters worse. Hit by economic slump due to Covid-19, the banking systems in emerging markets like India, Mexico, and South Africa will be slower to recover to 2019 levels and it will happen only beyond 2023, according to rating agency Standard and Poor's (S&P). A report released by RBI in September 2020 notes that the pandemic "has affected the best of companies" and businesses that were otherwise viable before the outbreak. Experts believe that banks may be more risk-averse to restructuring loans this time around, having already suffered big losses in previous restructuring efforts.

Covid-19's addition to an already stressed debt:

Nineteen sectors, which were not under stress before the pandemic but have been hit it, account for Rs 15.5 lakh crore of extra debt during aftermath of COVID-19 . Retail and wholesale trade are the worst affected with outstanding debt of Rs 5.4 lakh crore. The pandemic has also affected 11 sectors which were already under stress. These sectors have a debt of Rs 22.2 lakh crore. Non-banking financial companies (NBFCs) have the highest , Rs 7.98 lakh crore, among these sectors.

Opportunities ahead and tackling the aftermath of COVID:

A lot has been done already. Banks in India have focused on maintaining critical staff at branches and have temporarily redeployed staff to manage online or phone enquiries from customers. They've also deployed mobile ATMs and implemented doorstep banking for senior citizens and other customers that need additional attention. Several financial firms have started to implement video collaboration tools, new chat and messaging software and other fintech innovations to continue live interactions with customers who have been cop-

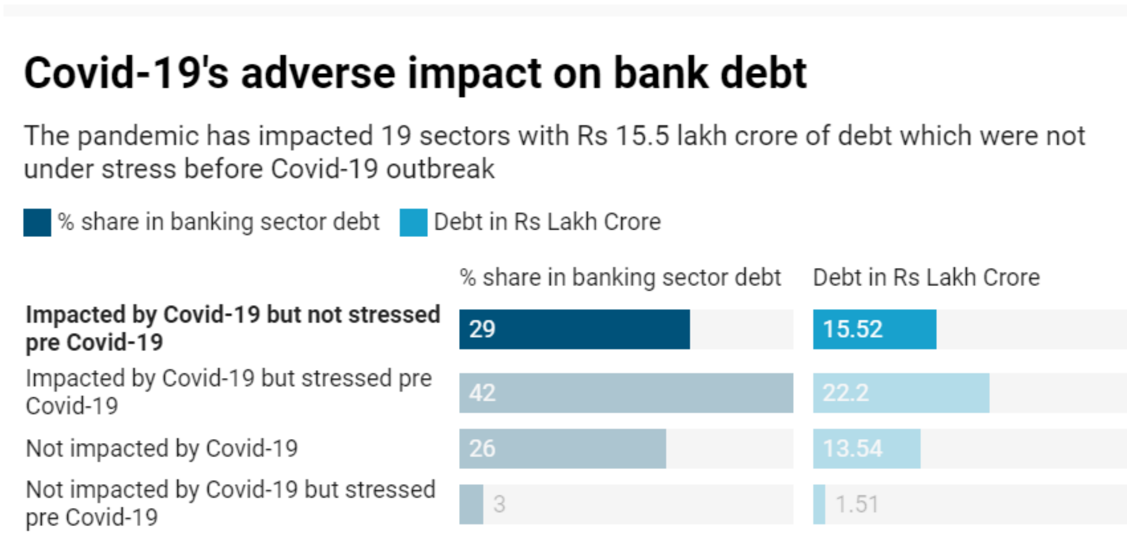

Figure 2: Addition to Bank debts due to COVID-19

ing with social distancing norms, with some already making use of common consumer apps to that end.
Most banks have addressed the immediate challenges of COVID-19, related to protecting staff and providing much needed services to customers. They now have the chance to be active participants to help mitigate this crisis, and there are four key areas they are and can improve their focus on to help navigate the current situation:

- **Customer Service and Advice:** As discussed in the above section on Customer relationship (A Positive opportunity for digitization)

- **Credit Management:** Even with the Indian government's stimulus packages and Reserve Bank of India's (RBI) liquidity measures, banks are expecting an increase in loan defaults as borrowers across customer groups struggle to make payments in the face of an economic crisis resulting from lost business and jobs. Banks are preparing for losses and are building capacity to deal with an increase in late payment of loans. As consumer demand picks up, albeit gradually, post lock-down, banks will need to repurpose their go-to-market and customer acquisition model, keeping in mind changing consumer behavior post COVID-19.

- **Revenue Compression:** Revenue from retail and commercial banking is falling sharply, as underlying consumption and transactions have seen an exponential dip. While central banks around the world slash interest rates, banks are reducing yields to generate business, thus significantly reducing net interest margins. Income from payments and other fee-based services are hit by a general decline in economic activity. With measures like moratorium periods provided on loans, banks' cashflow have also taken a hit. It is expected that an overall drop of up to 10% will happen in banks' payments revenues, which means a USD 150 billion top-line decline for the industry globally, as demand in sectors like retail and entertainment falls sharply or moves to online channels, while activity in areas such as tourism and travel evaporates.

  There is little that banks can to do to stop the overall drop in revenue, but they can focus on making payments safer by increasing limits on contactless payment channels and educating consumers on digital wallets. Banks can also focus on cashback and loyalty rewards to encourage spending in sectors that need it the most.

- **Operating Model Adjustments, Cost Elasticity and Innovation:** Over the next few quarters, the banking sector will face a misalignment between short-term costs and revenues due to the economic impact of COVID-19. Banks would need to review and prioritize current projects to ensure allocation of resources to the most pressing needs. Banks will also focus on investing in areas that will outlive the current pandemic, including projects and initiatives that maintain or improve the customer experience such as a paperless utility, end-to-end digital advisory and lending capabilities, increased fraud and cybersecurity analysis and detection, etc. These new digital tools will make banks more efficient and resilient to future changes. Banks that haven't focused on remote working and virtual collaboration in the past are now planning to explore establishing elastic operations. This will insure banks against such unprecedented lockdowns and perhaps better manage cost overheads.

Summary:

COVID-19 will have long-lasting impact on many industries including banks. According to CXO today publication India, Post crisis, digital maturity and COVID-19 resiliency will determine strategy of banking players with three segments emerging: banks that are already future-ready with truly digital banking capabilities and cost elasticity, banks that are lacking in the digital sector and that need to evolve and renew due to sub-par COVID-19 resiliency, and lastly banks that will struggle to survive as a result of being digital laggards with sub-par financial and operational resiliency.

COVID-19 will change our behaviors as customers, citizens and employees in India and around the world. As people become more focused on their well-being, businesses will also need to understand how they can be part of a new health ecosystem that is likely to dominate customer thinking going forward. The idea that "every business is a health business" is already emerging in many corners of financial services, and that is perhaps one of the few positive lasting impacts to result from COVID-19, according to many experts. (Referenced)

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