Impact of COVID-19 on consumer business in India

Deloitte PoV

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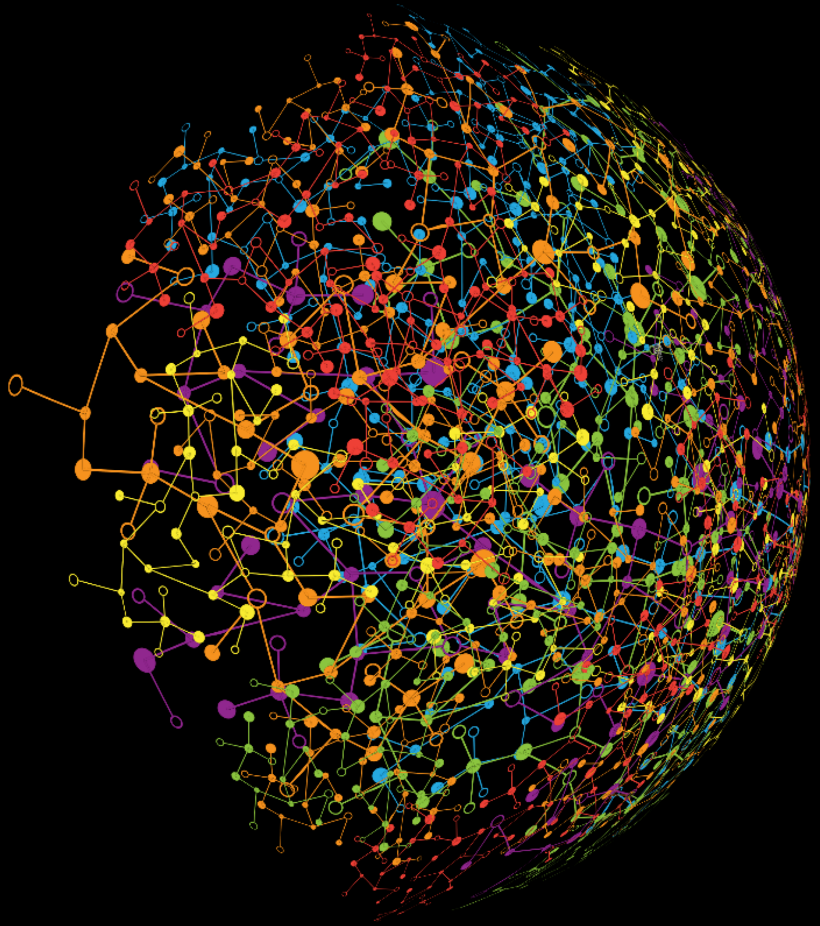
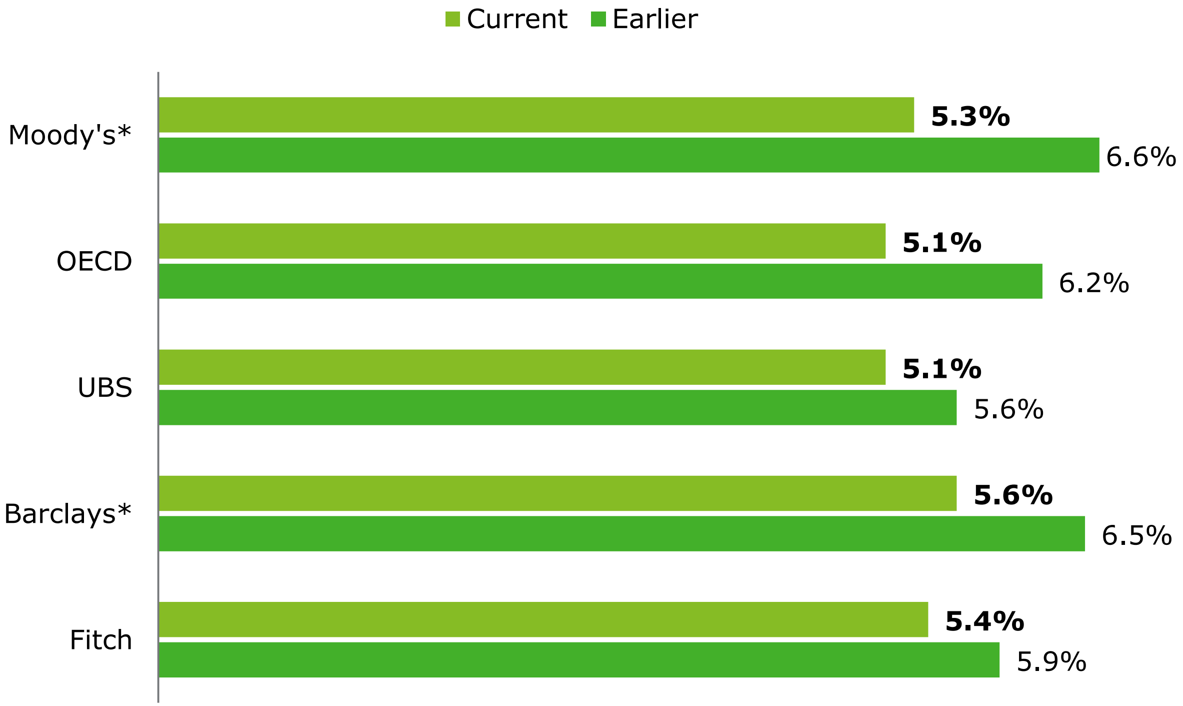
30 March 2020



The pandemic has set foot in India and is expected to lead the **country towards a major slowdown**

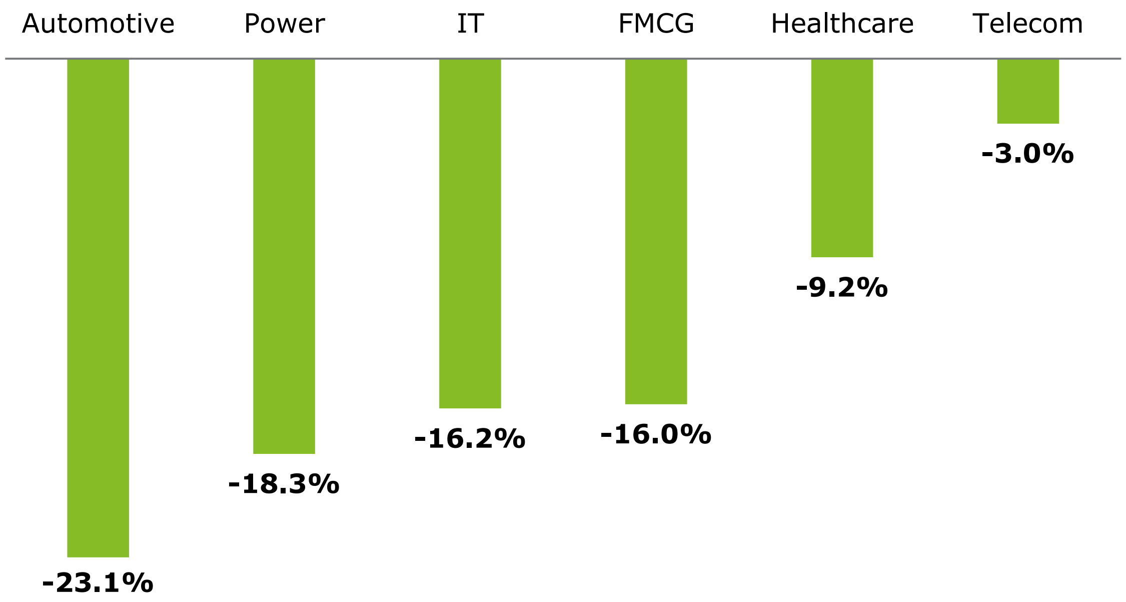
Major financial institutions have lowered growth estimates for India by 0.5–1.5 percent

FY21 growth projections for India



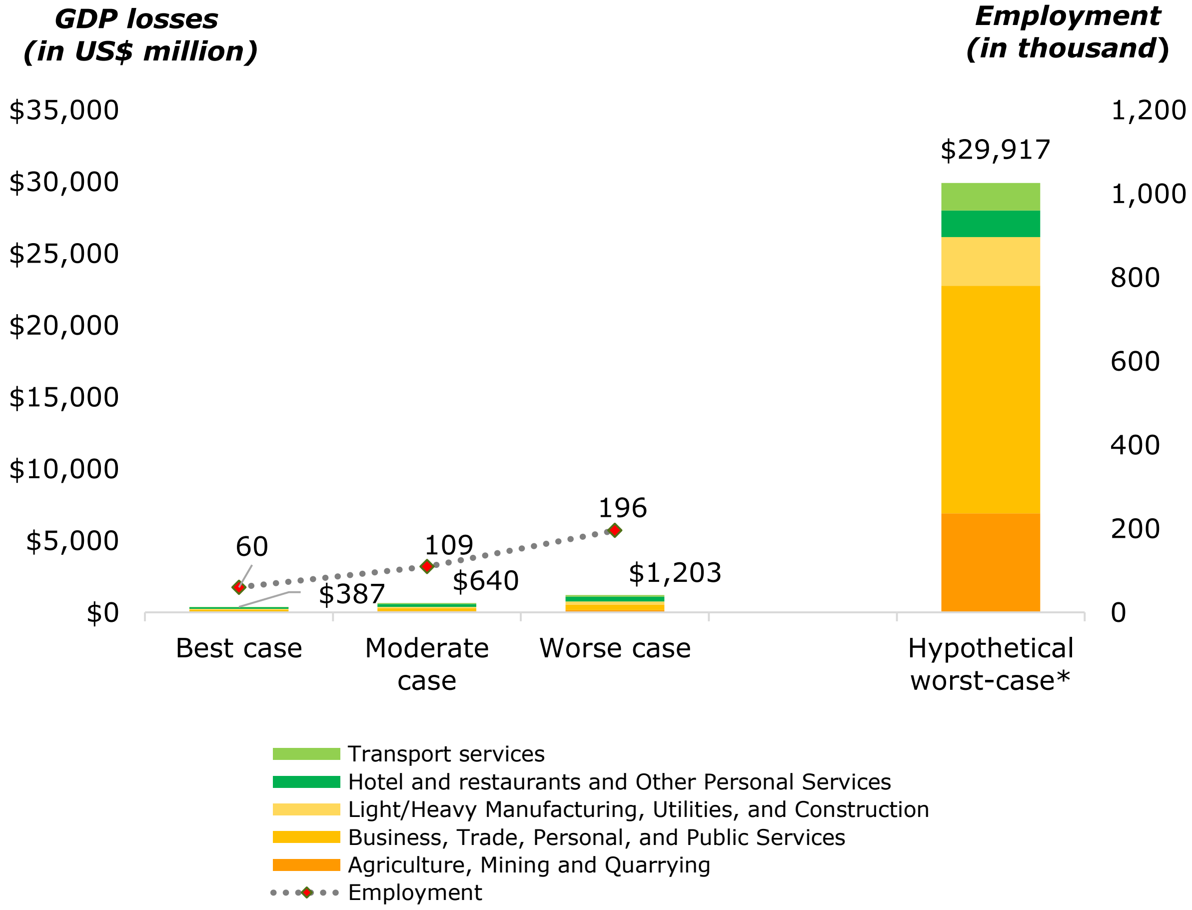
This is likely to put a downward pressure on ~~the~~ markets and industries

Impact on markets



Note*: FY20 projections
Source: MoSPI, Commerce Ministry, "Indian economy braces for coronavirus-induced shock as curbs set to pull down growth", Mint, 15 March 2020

The Asian Development Bank (ADB) presents the following **four scenarios** of COVID-19's **impact on Indian economy and employment**



Sector (impact as a percentage share within the sector)		Agriculture, mining, and quarrying	Business, trade, personal, and public services	Light/heavy manufacturing, utilities, and construction
Best case	GDP	-0.01	-0.01	-0.01
	Employment	-0.01	-0.01	-0.01
Moderate case	GDP	-0.02	-0.01	-0.02
	Employment	-0.01	-0.01	-0.01
Worse case	GDP	-0.04	-0.03	-0.03
	Employment	-0.02	-0.03	-0.02
Hypothetic worst case*	GDP	-1.62	-1.11	-0.57
	Employment	-1.7	-1.16	-0.62

Sector (impact as a percentage share within the sector)		Hotels, restaurants, and other personal services	Transport services	Total (Economy-wide)
Best case	GDP	-0.1	-0.03	**-0.01**
	Employment	-0.09	-0.01	**-0.01**
Moderate case	GDP	-0.18	-0.04	**-0.02**
	Employment	-0.17	-0.02	**-0.02**
Worse case	GDP	-0.31	-0.07	**-0.04**
	Employment	-0.29	-0.04	**-0.03**
Hypothetical worst case*	GDP	-1.64	-1.25	**-1.1**
	Employment	-1.64	-1.24	**-1.31**

Note*: The "Worst case" scenario is hypothetical, presenting the impact if a significant outbreak occurs in a country, and should NOT be interpreted as a judgment on the likelihood of an outbreak occurring there
Source: ADB, Deloitte analysis

The pandemic is likely to **impact the country's economy** through the following four vectors

Transmission routes

Supply disruptions

- Dependence on China for imports of raw and intermediate materials
- Higher input prices and reduced profitability, leading to decline in capacity building
- Supply-side disruptions may be temporary as China revives production units

Global and domestic demand

- Consumer spending to take a hit due to movement restrictions and fear of falling sick
- Reduced wealth effect due to falling share prices
- Hospitality and aviation sectors are impacted the most at a short span of time
- Low profitability and production disruptions impact business sentiments and investments
- Loss of employment, especially in the informal sector and for contractual workers, reduces consumer spending
- Demand in top few export destinations (China, the United States, and Europe) accounting for 40 percent of India's exports is severely hit

Stress on banking and financial sectors and parameters

Banks:

- Exposure to stressed industries and MSMEs
- Rising consumer loan default because of high unemployment and household leverage
- Stress on banks impact credit growth

Capital market and financial parameters

- The stock market has fallen 30 percent since pandemic started spreading in the West.
- A sharp depreciation of rupee against the dollar worsens trade deficit as exports contribution to GDP is low
- Rising bond yields make borrowing more expensive, thereby reducing bank margins.

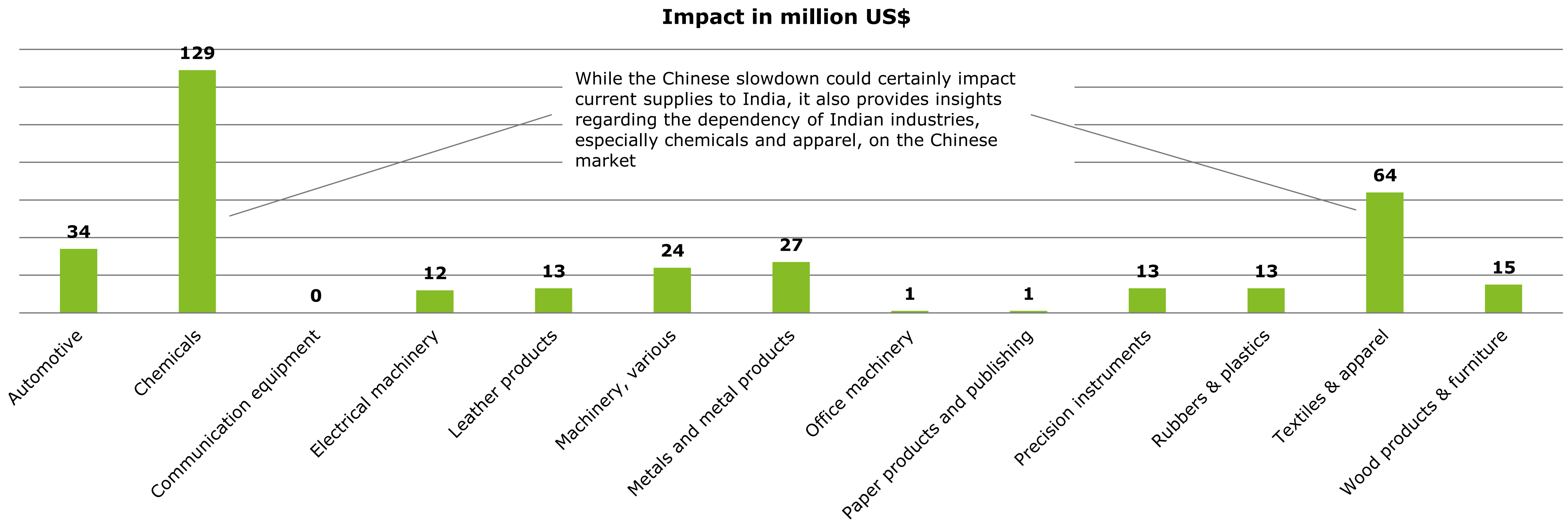
Falling oil prices

- Oil prices have fallen sharply. Brent crude oil fell from US$68.5 per barrel on 3 January to US$28.2 per barrel on 20 March.
- Lower oil prices could be a boon for India's twin deficit (the fiscal and current account)
- Gives policymakers some headroom to act.
- The rupee depreciation may partially offset the gains. Rupee has depreciated from INR 71.7 per US$ on 3 January to INR 75 per US$ on 20 March

Note*: Influence on business cycle - Inventory, Raw materials, Finished goods, New order, Export/ Import and Employment – and impact on inflation, needs to be monitored.
Source: CMIE; Deloitte analysis

China’s slowdown is expected to significantly **impact various industries** in India

A 2 percent reduction in Chinese exports of intermediate inputs may lead to a significant impact on Indian industries



Total impact of a 2 percent slowdown in Chinese production is estimated to be close to US$350 million for Indian industries

Source: ADB; UNCTAD

Possible **consequences** of this event on India's outlook

The following three scenarios, using the Oxford's global economic model, provide a probabilistic economic outlook

Scenario 1: Optimistic scenario with a V-shaped recovery
The contagion is controlled efficiently by June 2020 through effective government interventions. The economy starts recovering from Q2 FY21 and achieves rapid economic growth thereafter

Scenario 2: Somewhat optimistic with severe impact and a U-shaped recovery
Supply-chain problem multiplies and global demand declines sharply. In India, there is limited success in controlling the spread. The economy resumes back to life and witnesses normalcy from Q4 FY 2021

Scenario 3: Pessimistic scenario with a new low level of normal
In India, the disease spreads rapidly leading to a steep decline in demand and cuts in production. The situation eases in Q1 FY22 after which, the economy revives, but modestly. Over the next two years, the economy grows by 1.5–2 percent lower than it would have grown otherwise, with unequal recovery across sectors

Source: Deloitte analysis`

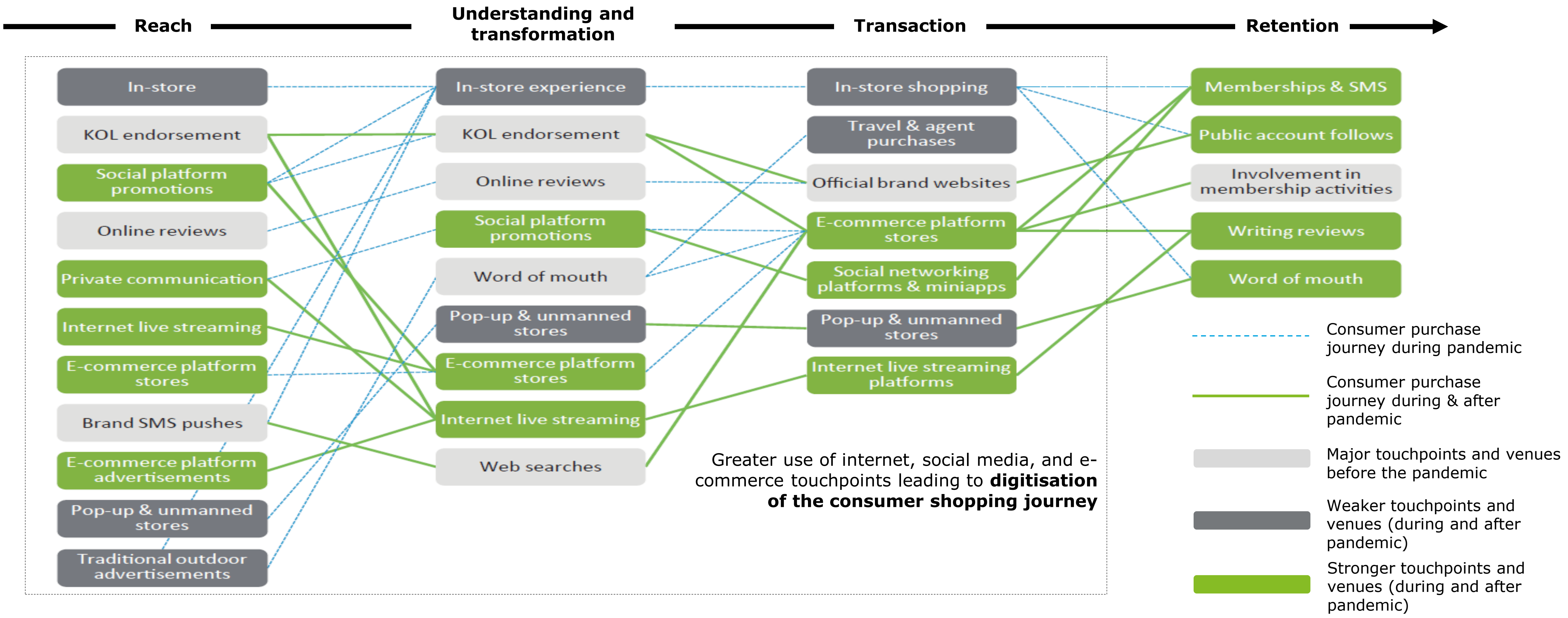
Scenario 1: The optimistic scenario (temporary impact of COVID-19 and a V-shaped recovery)				
Quarters	**Q4 FY20**	**Q1 FY21**	**Q2 FY21**	**Q3FY21 ..... Q4 FY22**
GDP growth	4.0%–4.2%	2.5%–2.8%	4.1%–4.3%	5.5%–6.8%
Inflation	Moderate	Low	Low	Rises but moderates around target rate

Scenario 2: Somewhat optimistic scenario – A severe and extended impact of COVID-19 with a U-shaped recovery				
Quarters	**Q4 FY20**	**Q1 – Q3 FY21**	**Q4 FY21**	**Q1FY22 ..... Q4 FY23**
GDP growth	4.0%–4.2%	2.2%–3.0%	4.2%–4.4%	5.5%–7.5%
Inflation	Moderate	Low	Moderate	Rises above 4%, moderates by Q4 FY21

Scenario 3: The pessimistic scenario (prolonged severe downturn leading to a new low level of normal)				
Quarters	**Q4 FY20**	**Q1 – Q4 FY21**	**Q1 – Q4 FY22**	**Q1FY23 ..... Q4 FY23**
GDP growth	4.0%–4.2%	2.2%–3.5%	4.4%–4.5%	5.0%–6.0%
Inflation	Moderate	Moderate	Moderate	Moderate

Note 1: The color of the tables indicates the phases of the slowdown and revival. Red is a sharp decline in growth, while green is recovery.
Note 2: In scenario 2, inflation picks up in H2 FY21 as demand revives faster than supply. Inflation is expected to increase above the target range (4 percent) for a short period of time in FY21 because of economic overheating. In this scenario, inflation remains around 3-4 percent during this period, despite weak demand because of a sharper fall in production.

Changes in consumer shopping journey **before, during, and after** the pandemic: an illustrative



Source: "Future Consumer" Series: Omni channel Transformation Begins by Grasping the Key to Consumer Mentalities, Deloitte; KOL – Key Opinion Leader

Segmental impact: **outlook** of select segments within consumer markets

Food and beverage:

- Development of the **frozen** and **instant food** industry chain is likely to be promoted to ensure supplies during the pandemic
- The lockdown situation has led to consumers **stocking essential products** at home leading to **greater demand** initially. Further, **quick recovery for F&B products is expected** after this situation concludes
- Consumers' close attention to hygiene and their **awareness to improve immunity** is expected to surge, prompting escalating consumer demand that can only be met with upgraded materials, techniques, and equipment

Quick recovery

Apparel and footwear:

- **Inventory and distribution challenges** amid the lockdown would imply that most enterprises' survival is likely to be determined by **two quarters of destocking and withdrawal of funds**, prompting reshuffles and integration
- Use of on-site workplaces, party venues, gyms, and other **places of gathering is expected to remain limited**, leaving companies with a demand only for indoor products
- Some brands might need to **temporarily shut down** or even close stores, providing an **opportunity for business restructuring and store network reorganisation**

Beauty:

- Fewer makeup scenarios are expected to give rise to new areas of demand, including "**home makeup,**" "**mask makeup,**" and "**contrast makeup,**" influencing the pattern of beauty products
- Amid the downturn for offline beauty stores, **demand for in-home skincare is expected to increase**
- Supported by increasing use of virtual technologies, **online shopping is likely to gradually replace offline shopping**, making **decentralisation imperative** for the industry

Lower trade

Retail:

- Non-contact demand during the pandemic is expected to **boost sales at smaller stores that can host** smaller crowds at a time. However, **supermarket chains have ensured supply of products** at regular prices
- Due to the pandemic's impact on consumer behavior and habits, "**online-sales**" are expected to witness a **significant surge,** even after the industry recovers
- The establishment of **online platforms** is expected to become indispensable for offline stores, and **online–offline service integration is expected to increase**

Changing behavior

Impact on liquidity

Low	Medium	Severe
• Pharmaceuticals • Power	• Gems and jewelry • Textiles • Automobiles and components • Consumer durables and electronics	• Airlines • Hotels, malls, and multiplexes • Poultry • Retailers and restaurants

Source: "Situational Thinking + Phased Preparation + Motivated Rally" How consumer products & retail enterprises can win the battle against COVID-19, Deloitte

Segmental impact: **automotive**

Dependency on China

- The Auto sector has a **moderate dependency** on China for imports with overall 18% of automobile component imports and ~30% of tyre imports
- Wuhan is a large Auto hub with not only OEMs but a large number of part manufacturers supplying parts to many tier 1 manufacturers and OEMs in India – many players started to feel the impact of COVID-19 in India in Jan itself with parts not reaching on time
- The **import dependency is higher in the two-wheelers segment** as more than four-fifths of the imported components in two wheelers are from China. Hence, this segment is likely to be impacted more
- **Chinese import ranges around 20 to 25 percent of the total imports**, in other segments including buses, passenger vehicles and commercial vehicles and demand has been highly sluggish

Alternatives for India

- The sector has **inventories sufficient for short-term support**, but lack of single, critical components can hurt OEMs
- Local **Indian auto-component manufacturers are unlikely to immediately capitalise on the void created by China,** as it takes time for OEMs to recalibrate their supply chain
- In a scenario of disruption in the supply of key components, the industry could look at **sourcing them either locally or from other countries** such as Germany, South Korea, Japan, and Thailand (currently accounting for around one-third of the total imports)
- However, the **change in procurement channels could be costlier and the supply could be insufficient** to meet the demand

With the rapid spread of the COVID-19 outbreak across the world, **global auto industry and consumption is likely to be impacted significantly**. This is likely to also pose challenges to export-oriented ancillary component manufacturers. This **coupled with the previous slowdown observed in the sector** in India, is expected to be a **double whammy** for the sector.

Source: Media articles, Deloitte analysis

Segmental impact: **consumer products and retail**

Fast moving consumer goods (FMCG)

- In the **immediate aftermath** of announcing the lockdown, the **demand and consumption of FMCG and household products increased massively** owing to panic buying by consumers and companies had to increase production
- Products such as food, groceries, and staples, health and hygiene products including soaps, detergents, hand washes and sanitizers, etc. witnessed massive uptick in demand
- However, with the implementation of the lockdown and **companies facing disruptions across manufacturing and supply chain**, there is a **considerable slowdown in growth** of these products
- The disruptions in supply chain and logistics is leading to **drying up of inventory levels at retailers** which may significantly impact the supply of products to consumers

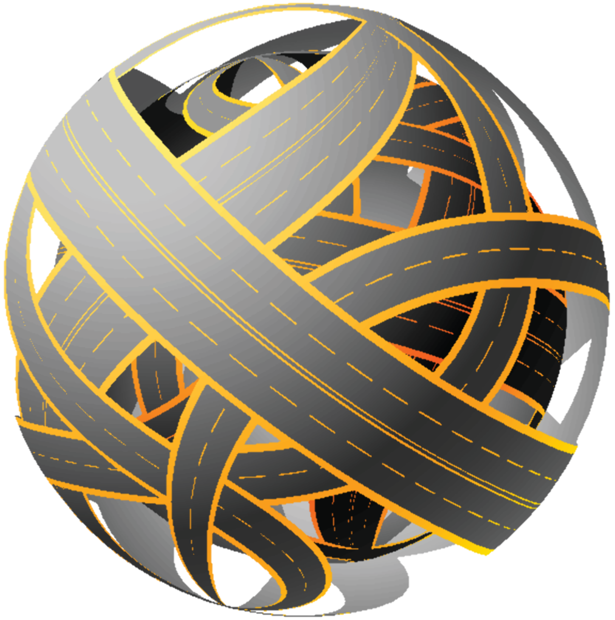
Consumer durables and electronics

- The COVID impact is expected to be felt acutely in the consumer durable sector as it has a **high dependency on China** for imports
- India **imports almost half of its completely built units of consumer durables** from China. In addition, India also **imports** a **bulk of** its **consumer durables components** from China
- Players may have already **stocked inventory**, so the impact is likely to be felt only towards the end of Q4 FY20
- **Product prices could see an increase soon.** The situation is extremely unpredictable with respect to this sector and is expected to take close to a year to show any signs of growth

The high probability of the virus spreading in India could result in a **massive impact on the consumer products and retail sectors.** The consumers are likely to **curtail their discretionary spending** which would significantly impact the sector's growth further. However, if the supply and logistics disruptions are minimized, a quick recovery in categories such as food and beverage and FMCG products can be expected post the situation concludes.

Source: "Future Consumer" Series: Omni channel Transformation Begins by Grasping the Key to Consumer Mentalities, Deloitte; Media articles

Segmental impact: **tourism and hospitality**



Hotels and restaurants

- There has been a **massive decline in the restaurant and food service business**. The impact is growing exponentially as the country comes under a lockdown for 21 days – food delivery has become the major means of revenues in the food service business
- Similarly, the **hotels and linked businesses** (guest house, townhouses, banquet halls, etc.) **have been direely impacted** amid the lockdown.
  - Business stays, leisure stays, family holidays, get-togethers, social occasions, etc. are being completely curtailed and in such a scenario the hospitality sector is taking a hard hit
- **Layoffs seem inevitable** in the restaurant sector as cash flows have dried up almost completely. **Small and mid-size restaurants would be the worst affected** as they struggle to cover fixed costs.

Travel and tourism

- COVID 19 has resulted in **one of the severest downturns** for the travel and tourism sector in India. Coming on back of a sluggish economy and subdued growth over the past few years, the COVID 19 blow is widely expected to push the sector to the brink.
- The **aviation and tourism** sectors are direly impacted leading to a **near collapse of the sector**, majorly owing to the cancellation of inbound Visas and stringent restrictions on domestic or international travel
- With revenue streams drying up, **companies will be forced to restructure their workforce**. Reduced working hours, **work without pay, salary cuts and downsizing the workforce** are **expected to be the norm** over the next three months.

The Indian tourism and hospitality sector comprising of hotels, restaurants, tour and travel operators, wedding and conference planners, etc. **contribute more than US$250 billion or nearly one-tenth of the GDP.** In case the COVID situation prolongs, we may witness a complete halt in the sector's operations and it may take initial government support for revival post the situation concludes.

Source: Media articles, Deloitte analysis

Government interventions: **steps needed** to minimise impact on the consumer industry

Ensuring stock availability

- While the PM has assured normal distribution of products and services for the consumers, current circumstances of country lock-down, “janta curfew,” closure of public transportation and public places, etc. imply a challenging outlook for the sector
- The government must try to ensure that there is none to minimal disruption in the supply chain of consumer products, and their distribution follows normal course, else the panic may lead to mass shortage of essential products and commodities

Facilitating e-commerce

- One of the major steps for the government to ensure minimum disruption is to encourage and facilitate e-commerce
- There are various players in the consumer industry who have launched contact-less pickup and delivery models to ensure zero contact with consumers, and thus minimise the risk of contagion
- Such contact-less methods are apt in the current scenario and could also lead to greater employment in the logistics and distribution departments for e-com players and retailers

Incentivising and assisting logistics and delivery

- While the risks associated with COVID-19 are common for all citizens, the government can offset its impact in the consumer sector by incentivising logistics and delivery personnel, and increasing its delivery fleet
- Further, assisting such personnel by way of distribution of essential precautionary and protective healthcare products, and mandating timely disbursements of salaries could boost their morale

Boosting non-urban consumption

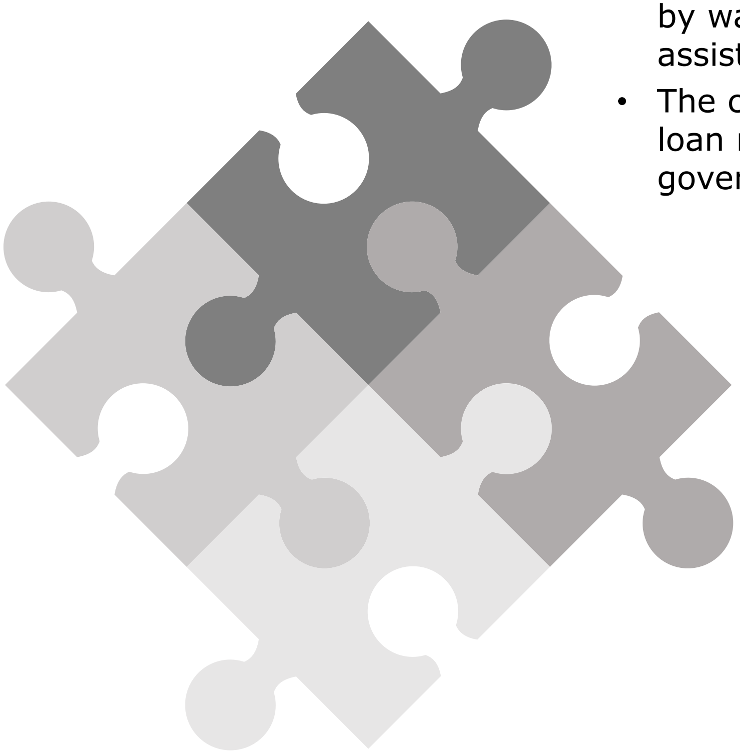
- To ensure that rural and non-urban citizens have adequate disposable income at hand, the government may resort to direct-benefit transfers and direct-account transfer of wages
- Already implemented by few state governments, this could allow immediate cash in hands of consumers, and they may not be constrained by non-availability of funds owing to delays or leakages
- At the same time, ensuring digital infrastructure in non-urban areas for consumers for ordering products online is also critical during such times

Offering unified solutions

- Large organised consumer companies, retailers and food service providers are likely to be amongst the most severely impacted lot owing to the closure of malls, restaurants, and people avoiding super and hypermarkets, etc.
- The government can encourage these players to unite with smaller retailers (kiranas) and e-commerce marketplaces and supply their stocks to ensure product availability
- This will not only ensure revenue generation and inventory circulation for the larger players, but will also lead to better availability of products for consumers

Source: Deloitte analysis

Government interventions: **regulatory measures taken** to offset impacts (to some extent) of COVID-19 in the consumer industry



1. Monetary stimulus

- Various state governments have announced relief packages for the population at the bottom of the pyramid by way of direct benefit transfers (DBT) to accounts of the population. Similarly, suitable nation-wide assistance will help in offsetting the impact of novel corona virus
- The central government has already announced some relief packages including working capital support, loan restructuring and credit terms alteration, stimulus to increase spending power of consumers, etc. State governments need to ensure proper execution of these relief packages through continuous monitoring

2. Cut in policy/fiscal rates

- The Reserve Bank of India cut its repo rate by 75 basis points (100 basis points = 1 percent). Subsequently various public and private sector banks are following suit which is facilitating greater liquidity in the market, both for companies and consumers
- This could lead to an increase in the spending power of consumers and establish more ways of investment for companies

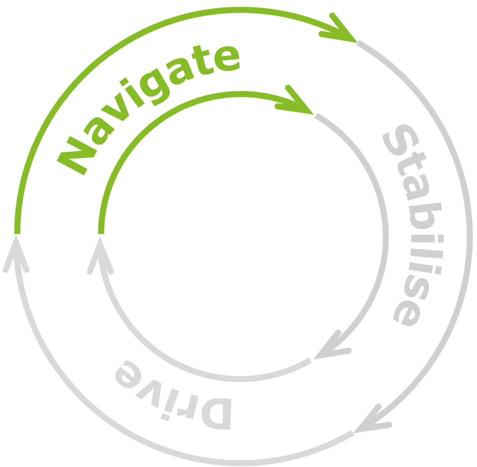
Additional measures needed to offset impact

- <u>Rationalisation of GST rates</u>
  - GST stimulus by way of rate concessions or reductions in tax rate of certain categories such as household goods of daily use, sanitation, and medical and healthcare products will help in boosting the demand of these products, and go a long way in reviving consumption growth

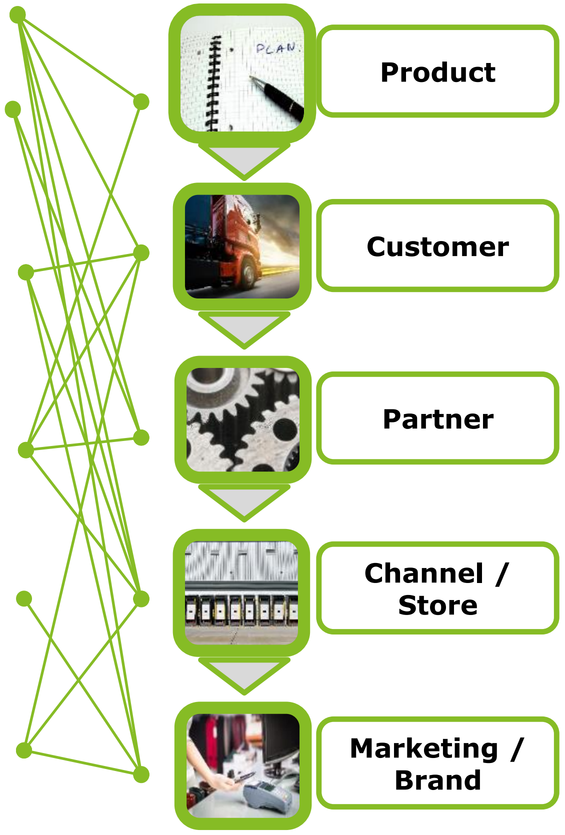
Source: Deloitte analysis

Consumer market response: **navigate uncertainties**

Continue with actions around managing continuity and mitigating risk



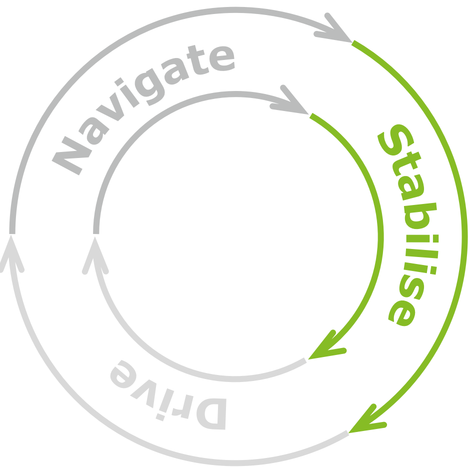
Focus on health and safety	• Prioritise **safety-enhancing products** with strong protective features
Cash-flow management	• Good management of cash flows to ensure that any business disruption does not affect employees or outsourced workers
Proactive communication with consumers	• **Engage with key customers** to support business continuity and reinforce loyalty • Be open and provide customers with **updates regarding service outings** and ways to deal with COVID queries, without prompting
Channel shift from offline to online	• There has been a geographical focus on less-affected rural areas • With the recent shutdowns in local transportation across the country, retailers have to **focus more of their efforts on e-commerce**
Strong social responsibility	• Maintain a positive presence with employees and build a "people-are-first" ethos; mass lay-offs can **damage the company's reputation** • Prepare and reinforce "COVID-friendly" policies such as flexible working for employees
Offering low touch point delivery	• Delivery executives engaging in **"contactless delivery"** provide employees and consumers peace of mind and ensures services are not hampered • An increased focus in cashless orders will **extend the pool** of available vendors



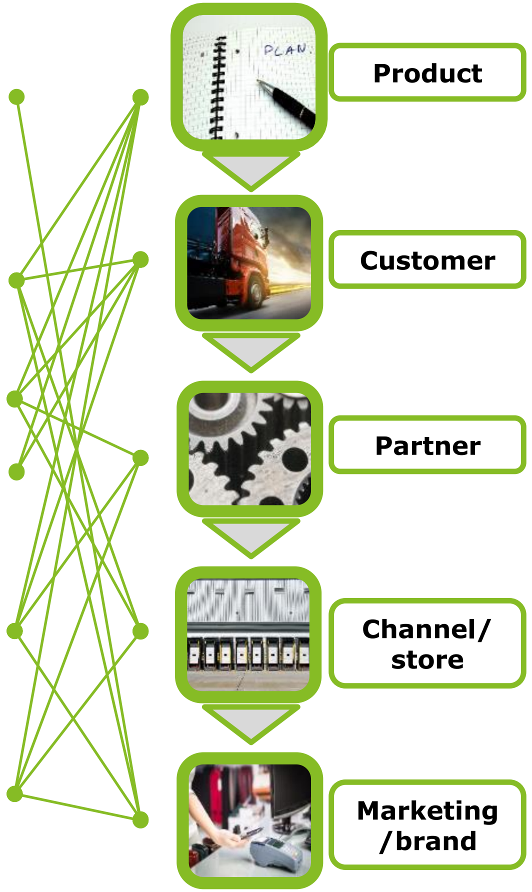
Source: Deloitte analysis

Consumer market response: **stabilise the chain**

Focus on ideation and actions to create the difference and emerge stronger



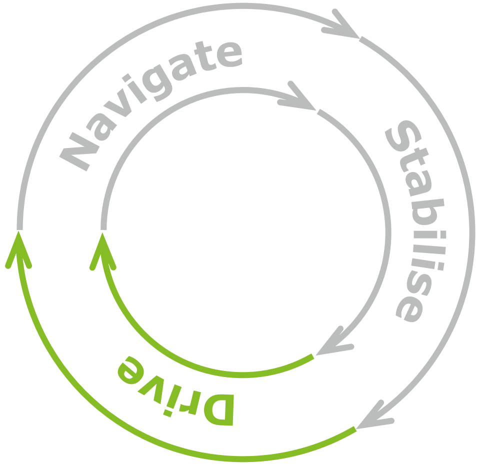
Catchment analysis important/direct to community	• As things slowly come back to normalcy, selective areas will be allowed to open. Hence, it becomes critical to identify stores with maximum return, and invest resources in those areas • Going directly to consumers and bringing high-demand products to them can **maximise conversion rates**
Sustaining online presence	• Spending time to nurture new consumers who have **shifted purchasing habits online** will be crucial in building a long-term customer base • Consumers are finding themselves **less hampered by familiarity** with single shopping channels
Social media marketing campaigns	• **Live-streamed marketing** has distinguished itself in promoting the latest cars, consumer electronics, health products, and even real estate
Provide mobile shops	• Consumers are looking to avoid crowds, provided these **alternate options** can ensure that goods are still being sold and customers are not missed
Predicting retaliatory purchases during business recovery phases	• As demands shifts focus back to urban, retailers need to be careful and ensure that they have the appropriate **allocation of resources** to not miss out on any opportunities • Careful planning will be needed to avoid stock issues after the epidemic as **some consumers splurge**
Stock management	• **Re-evaluate stocking strategy** in light of supply risk, supply and demand volatility, cash, and perishability • Shifting stocking focus towards **high-demand goods** and away from ancillary products can maximise revenues and boost sales



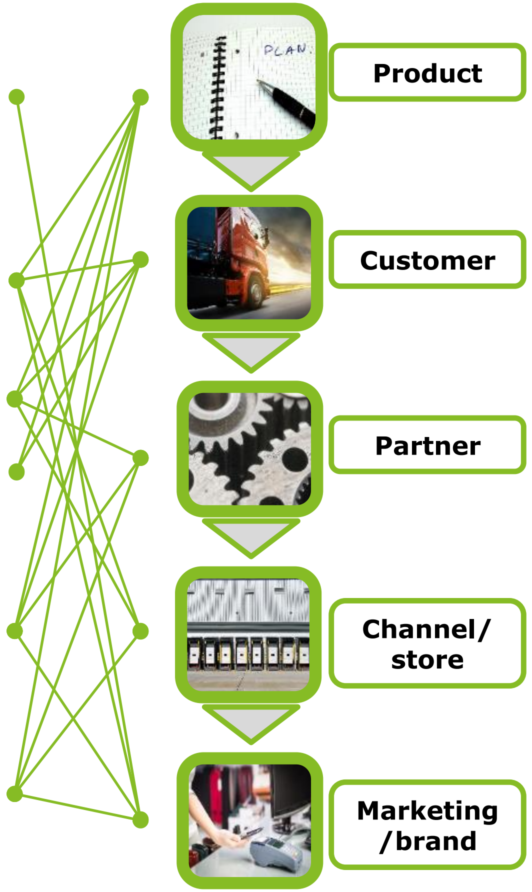
Source: Deloitte analysis

Consumer market response: **drive the future**

Enable actions to seize opportunities in the new normal



Omni-channel shifts	• Its important to retain new consumers who were on-boarded during any **extension of service**
Decentralised supply chain	• Growing a decentralised supply chain can provide **stability to operations** and **reduce external dependencies**
Value-for-money Purchases	• Even when things start going back to normalcy, several people will lose their purchasing power or be more conscious towards making purchases. Hence, customers will prefer brands that promise **value for money,** and meet customer expectations during dire conditions
Partner agility to accommodate changes	• **Work** closely **with identified tier suppliers** to obtain visibility, and understand flexibility and allocation logic • Being able to serve varied customer needs requires a partner that can shift supply quickly
Re-allocate resources to maintain the new urban–rural mix	• With the shift to rural retail, and with the newly associated customer base, retailers should focus on a **rebalance that strengthens** rather than weakens their position in the market
Social responsibility to remain key	• Having built a solid reputation, retailers should focus their supply chain to only work with partners who also stand by **similar principles**
Manufacturing hub	• On a positive note, Indian manufacturers have the opportunity to **establish themselves as manufacturing hubs** and leverage the void created in Chinese manufacturing



Source: Deloitte analysis

Thank you
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