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COVID 19

ECONOMY & ACCOUNTING

CHAPTER 1

IMPACT ON INDIAN BUSINESS

The COVID-19 pandemic has effectively brought normal life to a halt in India. The importance of social distancing and a lockdown in curbing the spread of the virus cannot be stressed enough, but these measures also have huge repercussions on livelihoods and the economy at large. The Indian economy has been experiencing significant slowdown over the past few quarters. In the third quarter of the current fiscal, the economy grew at a six-year low rate of 4.7%. The outbreak has presented fresh challenges for the economy now, causing severe disruptive impact on both demand and supply side elements which has the potential to derail India's growth story

Demand Side Impact - Tourism, Hospitality and Aviation are among the worst affected sectors that are facing the maximum brunt of the present crisis. Closing of cinema theatres and declining footfall in shopping complexes has affected the retail sector by impacting consumption of both essential and discretionary items. Consumption is also getting impacted due to job losses and decline in income levels of people particularly the daily wage earners due to slowing activity in several sectors including retail, construction, entertainment, etc. With widespread fear and panic now increasing among people, overall confidence level of consumers has dropped significantly, leading to postponement of their purchasing decisions. Travel restrictions have severely impacted the transport sector. Hotels are seeing large scale cancellations not only from leisure travelers but even business travelers as conferences, seminars and workshops are getting cancelled on a large scale.

Supply Side Impact - On the supply side, shutdown of factories and the resulting delay in supply of goods from China has affected many Indian manufacturing sectors which source their intermediate and final product requirements from China. Some sectors like automobiles,

pharmaceuticals, electronics, chemical products etc. are facing an imminent raw material and component shortage. This is hampering business sentiment and affecting investment and production schedules of companies. Besides having a negative impact on imports of important raw materials, the slowdown in manufacturing activity in China and other markets of Asia, Europe and the US is impacting India's exports to these countries as well. Production has come to almost a standstill, as Government had imposed lockdowns to help break the chain of the corona virus outbreak. Since these measures will remain in place at least until the end of 3rd week of April, companies are sure to lose a significant part of the output for the March & April months. Even an improvement in the Covid-19 situation wouldn't bring much respite to the industry in April as it would take a while for consumer confidence to become normal. There will be a period when companies won't be generating revenue and there will be some level of fixed expense that is incurred and that will drain the P&L for everyone. Nobody is spared.

Impact on Financial Market - Greater uncertainty about the future course and repercussion of Covid-19 has also made the financial market extremely volatile, leading to huge crashes and wealth erosion, which in turn is impacting consumption levels. One of the major slides in the domestic equity markets was seen on March 12, when following the trend of the global equity markets, both the BSE Sensex and NSE Nifty crashed by more than 8% in a single day. The BSE Sensex dropped over 2,919 points – its biggest one-day fall in absolute terms while the NSE Nifty dropped by 868 points. An estimated Rs 10 lakh crore of market cap was reportedly wiped off due to this single day fall. The fall has continued till date as investors resorted to relentless selling amid rising cases of coronavirus. On March 19, Indian equity markets again plunged to new low. Sensex closed 581 points lower at 28,288 and Nifty fell 205 points to end at 8,263. With equity markets likely to remain volatile in future as well, further wealth erosion of investors is expected.

CHAPTER 2

MAJOR INDUSTRIES IMPACTED

Almost all the sectors have been hugely impacted by this outbreak of COVID 19. However, there are certain set of industries who have been exponentially impacted and such impact will remain for long on their balance sheets, those have been listed as under:

Aviation – This industry in India had already been in losses all throughout majorly due to high cost and extremely high level of competition in India. India has huge number of travelers, however this sector has failed to make profits. Besides, this outbreak of virus has made it worse for such sectors with a complete lockdown on their operations. Players in these sectors have already announced pay cuts to their ground staff and crew members considering that it will take a lot of time for them to revive.

Tourism and Hospitality – This industry is major source of earning for many states in India. It goes without saying that there will be reduction in the foreign travelers travelling to India for visiting these states until the entire world responds positively to the situation and the economy neutralizes. Till the time this situation is stabilized, this industry is going to suffer a huge hit.

Capital Markets, Financial Services & Fintech – This can be clearly visualized looking at the markets across the globe. The volatility as mentioned above is tremendous. The capital markets in India has drastically fallen. This has a chain impact on the financials services thereby leaving its impact on the fintech area also.

Ecommerce – This was the first industry besides the tourism industry which started responded negatively on outbreak of the virus. People have become health conscious and stopped accepting any supplies which came through multiple logistics. Also the tech based e-

commerce websites offering services have seen their downsides as their end consumer business have been having an impact due to COVID 19.

Education – As we could all see the schools and colleges are shut and they would be the last sector which is expected to obtain normalcy due to hygiene and until a vaccine for this deadly virus is invented. Having said that, this sector has now started taking online classes but it is to be seen how this sector responds to such approach.

Entertainment and Sports – The cinema houses and stadiums have all gone silent and these are the main zones where the crowd gathering is huge. Entertainment industry is one of the largest industry in India. It has also be seen that there has been an impact on the sports as the IPL which was going to be commenced in march was earlier postponed until April and this may further be extended if the situations done neutralize. These industries have a predetermined contracts, it will be interesting to see how these industries respond to the force majeure clause in their contract considering the impact of COVID 19.

Automobiles – We had seen that the automobile industry was already running through its bad phase in India considering the slowdown in its sales and services. In the midst of this when such outbreak has incurred effecting huge chunk of businesses, automobile being a luxury consumable for most of them, would be a last preference for the consumers and many would consider postponing their plan of buying one leaving a big impact on this sector.

Real Estate – This sector was running in its bad phase in most of the states in India with the developers having huge inventory and less buyers in the market to outright purchase considering that the annual yield from the investment in real estate had stagnated in the past. This has further worsen the situation of the developer as the projects which were being developed have now been stand still. This sector has its major working capital applied in the project and not completing the same on time spoils the entire cycle leaving the project unprofitable.

CHAPTER 3

IMPACT ON FINANCIAL REPORTING

While we are empathetic to the global concerns of health and safety of people, there is also a need to advise the preparers of financial statements to ensure that the potential impact of COVID-19 is suitably considered in preparing and reporting their financial statements for the year ended March 31, 2020. Specific requirements of a few accounting standards that may need special attention are indicated in this Accounting Advisory. It may be noted that we are only drawing the attention of preparers to some of the important requirements of Indian Accounting Standards (Ind AS) and Accounting Standards (AS), and this is not meant to be exhaustive and may differ based on specific facts, circumstances and business of respective preparers.

Inventory Measurement (Ind AS 2 and AS 2) - In accordance with Ind AS 2, Inventories, and AS 2, Valuation of Inventories, it might be necessary to write down inventories to net realisable value due to reduced movement in inventory, decline in selling prices, or inventory obsolescence due to lower than expected sales.

Impairment of Non-Financial Assets (Ind AS 36 and AS 28) - Due to COVID 19, there might be temporary ceasing of operations or an immediate decline in demand or prices resulting in lowering of revenues and profitability and reduced economic activity. These are the factors that the management may consider as the indicators that may require impairment testing for the purpose of Ind AS 36 and AS 28.

Financial Instruments (Ind AS 109 & 107) - Management needs to incorporate effect of **Expected Credit Loss** (ECL) while preparing Financial Statements, it might possible default by the borrower may have increased significantly due to reduced economic activity. Entities

may also need to consider the impact of any Prudential Regulatory actions to sustain the economy such as loan repayment holidays, reduction in interest rates etc. In respect of Ind AS 107, Financial Instruments Disclosures, entities may need to disclose the impact of COVID-19 on various credit related aspects such as methods, assumptions and information used in estimating ECL, policies and procedures for valuing collaterals etc.

Leases (Ind AS 116) - Due to Covid-19, there may be changes in terms of lease, such terms shall be considered while accounting for leases. Variable lease payment may be significantly impacted. Entities will need to determine whether as a result of COVID -19, any lease arrangement has become onerous.

Under AS 19 discount rate used to determine present value of minimum lease payments of new leases may need to incorporate any risk associated with COVID-19.

Revenue (Ind AS 115 and AS 9) - Due to COVID-19, there could be likely increase in sales returns, decrease in volume discounts, higher price discounts etc. Under Ind AS 115, these factors need to be considered in estimating the amount of revenue to recognised.

Entities to whom AS is applicable, may have postponed recognition of revenue due to significant uncertainty of collection in view of the impact of COVID-19.

Provisions, Contingent Liabilities and Contingent Assets (Ind AS 37 and As 29) - As a result of COVID -19, some contracts may become onerous for reasons such as increase in cost of material/labour, etc. Management should consider whether any of its contracts have become onerous. Due to COVID-19, there is a need for exercising judgement in making provisions for losses and claims. A provision may be accounted for only to the extent that there is a present obligation for which the outflow of economic benefits is probable and can be reliably estimated.

Going Concern Assessment - Management of the entity should assess the impact of COVID-19 and the measures taken on its ability to continue as a going concern. The impact of COVID- 19 after the balance sheet date should also be considered in assessing whether going concern assumption is appropriate or not. Events occurring after the balance sheet date may indicate that the enterprise ceases be a going concern. It may be necessary for the management to evaluate whether it is proper to use the fundamental accounting assumption of going concern in the preparation of the financial statements.

Income Taxes (Ind AS 12 & AS 22) - COVID-19 could affect future profits and/or may also reduce the amount of deferred tax liabilities and/or create additional deductible temporary differences due to various factors. Entities with deferred tax assets should reassess forecasted profits and the recoverability of deferred tax assets in accordance with Ind AS 12, Income Taxes, considering the additional uncertainty arising from the COVID-19 and the steps being taken by the management to control it.

Other standards such as Property plant & equipment, borrowing cost and Presentation of Financial Statements should be assess in detail by the management of entities.

CHAPTER 4

IMPACT ON AUDIT OF FINANCIAL STATEMENT

Given there are increasing restrictions on travel, meetings and access to client locations, auditors would be facing practical difficulties in carrying out audits. These underlying situations, however, must not undermine the delivery of high-quality audits. Audits should continue to be planned and performed in compliance with the auditing standards. To enable the auditors to perform audits, they may be required to use alternate audit procedures which will have to be performed in order to obtain sufficient and appropriate audit evidence.

Auditors must carefully evaluate unique circumstances prevailing in their audits and assess risk accordingly when applying the concepts in this Advisory in their audits.

Areas which require special attention of auditors in current scenario are cited below along with reference to Standard of Auditing (SA)

- Planning and Performing an Audit (SA 315, Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and its Environment & SA 320, Materiality in Planning and Performing an Audit).
- Assessing Financial Impact and their Reasonable Estimation (SA 540, Auditing & Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures).
- Valuation of Inventory on a date other than date of financial statements i.e. 31st March 2020 (SA 501, Audit Evidence - Specific Considerations for Selected Items).
- Audit of Consolidated Financial Statements where Components/component auditors are located in severely affected places (SA 600 Using the Work of Another Auditor).

- Subsequent Events or Events after Reporting date (SA 560, Subsequent Events).
- Going Concern [SA 570(Revised)].
- Evaluation of Work of Management's Expert (SA 500, Audit Evidence).
- Written Representation from Management (SA 580 Written Representation).
- Auditor's Opinion, [SA 700(Revised)], Forming an Opinion and Reporting on Financial Statements, SA 705(Revised), Modifications to the Opinion in the Independent Auditor's Report, SA 706(Revised), Emphasis of Matter paragraph in the Independent Auditor's Report.
- Reporting of Key Audit Matter (SA 701 Communication Key Audit Matter in the Independent Auditor's Report)
- External Confirmations (SA 505, External Confirmations).
- Risk of Fraud (SA 240, The Auditor's Responsibilities Relating to Fraud in An Audit of Financial Statements).

CHAPTER 5

CONCLUSION

Although it is difficult to determine the exact impact the coronavirus will have on the world's economy; it is clear the impact will be substantial and pervasive. And it appears the worst is yet to come. Investors worldwide are closely watching the coronavirus's impact on world markets. The US stock market has shown substantial volatility, with the Dow Jones Industrial Average suffering its worst single-day losses since the 2008 financial crisis.

Even if the tide turns quickly and the virus's spread is curtailed, its impact will likely be long-lasting. Some entities with thin margins and weak balance sheets will have been driven out of business. Others may need to consider bankruptcy protection to address liquidity issues, or supply chain or vendor disruptions.

CHAPTER 6

THOUGHTS FROM INDIAS CEO'S

This pandemic situation of COVID 19 across the world has thought many lessons to the which would be helpful for developing the leadership skills of an individual. As one rightfully says, we should always take a learning from the bad times as the good times never teach us.

“It reminds us that we are all connected and the false borders we have put up give us no protection. It reiterates how important our health is and how we should not neglect it and, most importantly, it teaches us that our true work is not just our job, that’s just what we do.”

- Suneeta Reddy MD, Apollo Hospitals Enterprise

“First, if your culture is great, your biggest support in times of utter uncertainty will be employees —it’s a wonderful and very comforting feeling to have. The second is an intuition, actually a conviction, that in future, such black swan events will occur more frequently and that one must always have a business continuity plan in place that factors in perhaps zero revenue for up to 6-12 months in the worst case.”

- Patu Keswani Chairman, Lemon Tree Hotels

“Because of SARS, Singapore spent a lot of funds to beef up its health infrastructure, which has helped it cope now. For a company, having good reserves, a healthy balance sheet and not a very aggressive structure helps deal with difficult times. Be healthy, frugal and keep company as risk-free as possible — these are big lessons.”

- Ajay Bijli Chairman, PVR Ltd

“That the magic of the human race is us - people. Everyone wants to help each other and have everyone come out strong. Witness the myriad zoom webinars going on with so many stakeholders coming together on one platform to share best practices, hear out concerns and offer help. Sometimes it takes an unfortunate situation to bring out the mettle of human race. The Chinese word for "crisis" signifies both challenge as well as opportunity. Its a great time to hunker down and build new products and find new opportunities. Every downturn has seen a cycle of Innovation”

-Sanjay Nath, managing partner, Blume Ventures

ABOUT THE FIRM

We, at Wadhwa & Shah, always strive towards providing extra edge to our clients in their growth. Having a team of enthusiastic and young chartered accountants along with other professionals, we work together towards a common goal of client satisfaction.

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