Asian Journal of Economics and Finance. **2020**, 2, 4 : 443-451

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Economic Impacts of the COVID-19 Pandemic in South Asian Countries: Prospects and Policy Implications

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Received: 30 August 2020; Revised: 29 September 2020;
Accepted 10 October 2020; Publication: 15 October 2020

Abstract: The paper intends to review the relevant literature, analyze short-term and long-term impacts of COVID-19, evaluate the economic impacts of the pandemic and its prospects in South Asian countries and draw policy implications for growth recovery in South Asian economies. COVID-19 induced economic slowdown in 2020 lowers potential growth for next four to five years due to reduced investment, credit restrictions and low adoption of new technologies. Regional growth in South Asia is estimated to decline by 2.7% in 2020 due to pandemic induced restrictions in consumption and services and private investment. In India, growth slowed to 4.2% in 2019-2020 and estimated to decline by 3.2% in 2020-2021 due to stringent restrictions to contain the pandemic spread, despite fiscal stimulus and monetary easing. Bangladesh and Nepal are expected to experience substantial decline in growth at 1.6% and 1.8% due to pandemic-induced disruptions, fall in exports and remittances. Sharp decline in oil prices could provide cushion to fiscal and current account balances in South Asian economies, particularly India and Pakistan, which may offset decline in remittance inflows in 2020. In 2021, GDP growth is estimated to recover to 2.8% due to resumption in services and manufacturing in the region, however, slow revival of tourism will affect the pace of economic recovery. Targeted policies are needed to complement the fiscal stimulus and monetary easing at the national level. The worst affected households, informal sector, and businesses should be provided the additional targeted social protection, direct social transfers and fiscal support respectively in post-crisis era for economic resilience and recovery. Robust policy measures will be needed for speedier economic recovery once the pandemic abates and containment measures removed through strong initiatives at the national level and multilateral cooperation.

Keywords: Economic impacts, COVID-19 pandemic, South Asian countries, policy implications

I. Introduction

World Health Organization (WHO) has declared COVID-19 a global pandemic. Globally, millions of people suffered from the pandemic, which is still spreading rapidly. Reported cases of the pandemic infected people may be far smaller lower than actually infected persons (Hortacsu, Liu, and Schwieg 2020). The past pandemics like SARS-Cov (Severe Acute Respiratory Syndrome, or SARS) in 2002-03, MERS-Cov (Middle East Respiratory Syndrome, or MERS) in 2012 were less transmittable with lower fatality (Wilder-Smith, Chiew, and

Lee 2020) compared to COVID-19 with fatality rate ranges from 0.3% to 3.4% due to uncertainties, testing deficits and asymptomatic cases, however, significantly lower than the Spanish flu fatality rate estimated at 3.5% to 20% during 1918-19 (Spreeuwenberg et al. 2018). Globally, social distancing, restrictions on mobility and economic activities, lockdowns, closure of business, educational and religious institutions, and voluntary actions have been initiated to contain the pandemic spread to slower the infection rate and delay the peak (Ferguson et al. 2020). Extraordinary measures to stem the pandemic spread have led to severe disruptions in economic activities and global slowdown. South Asian countries have experienced rapid decline in trade, capital outflows, fall in oil demand, significant disruption in small and medium enterprises (SMEs), huge unemployment, slower domestic demand and reduced consumption. Against this background, the paper intends to review the relevant literature, analyze short-term and long-term impacts of COVID-19, evaluate the economic impacts of the pandemic and its prospects in South Asian countries and draw policy implications for growth recovery in South Asian economies.

II. Review of Literature

COVID-19 fatalities are increasing and likely to surge (Atkeson 2020), which strong impacts on output in the short-term and likely to impact gross domestic product (GDP), trade, supply chains, demand pattern, capital flows, employment and socio-economic conditions negatively. COVID-19 pandemic disrupts economic activities (Baker et al. 2020a), causes capital outflows and affects financial markets (Ma et al. 2020). Infectious disease outbreaks affects the elderly more, and reduces quality of health care systems, and lowers access to water and sanitation services (Farzanegan et al. 2020). Global value chains (GVCs) disruption increases economic cost of the pandemic via decline in manufacturing and exports (Baldwin and Tomiura 2020).

Fiscal stimulus and monetary measures lower the negative economic impacts of the pandemic, however, fiscal multipliers depend on debt levels and external financing needs and robust social security system (Loayza and Pennings 2020), while effectiveness of monetary measures depend on strong formal sector and high financial inclusion. COVID-19 generates severe economic impacts compared to past pandemics. Initial estimates show smaller economic losses, while subsequent estimates reflect higher economic costs of the pandemic due to its persistence and severity (ADB 2020; OECD 2020a). Without stringent controls, short-term estimates of output losses stood at 2% to 6% of GDP in developing countries and 2% to 8% in developed economies (McKibbin and Fernando 2020), while economic losses stood at 2.5% to 4% in developing countries and 1.8% to 3.8% of GDP in developed economies (Maliszewska et al. 2020) due to decline in employment, consumption, trade, travel and tourism. With restrictions on economic activities, estimates suggest

decline in output by 25% in developed economies (OECD 2020b) and extended containment generates additional economic losses (IMF 2020).

COVID-19 induced economic slowdown in 2020 lowers potential growth for next four to five years due to reduced investment, credit restrictions and low adoption of new technologies. Severe vulnerabilities of debt and insolvency risk increase the likelihood of a financial crisis (Kose et al. 2020). Learning disruptions due to closure of educational institutions to reduce the pandemic spread adversely affects the disadvantaged students (World Bank 2020a) and hamper human capital accumulation and earnings potential in low-income families with less learning support at home (Van Lancker and Parolin 2020). COVID-19 severely affects the poor and vulnerable sections the most due to decline in income, high risk of infection, fatality and lower availability of essentials (World Bank 2020a) and recent success in poverty reduction and inequality is expected to be lost (Sumner et al. 2020). In brief, GVCs disruptions, fragile trade and shortages of essential goods may force the governments and firms to reassess the benefits of low-cost off-shoring of manufacturing by using capital-intensive import-substitution. Economic impact of the pandemic is likely to persist longer even after it dissipates and could change production structure more compared to past recessions. Restrictions and adjustments in consumer behaviour to reduce the pandemic risk such remote working and avoidance of crowds are also likely to persist and it may take years to recoup the economic losses.

III. Short-term effects of COVID-19

IMF (2020) estimates labour supply to decline by 5% to 8% globally, financial market disruption and credit tightening, sharp fall in commodity and oil prices, and peak GDP loss by 7.7% to 10% in developed economies and 5.4% to 8% in developing economies. Maliszewska et al. (2020) and World Bank (2020c) found labour input to decline by 3% in 2020 due to COVID-19 linked illness and mortality, trade costs to surge by 25%, and peak GDP loss by 1.8% to 3.8% in developed countries compared to 2.5% to 4% in developing countries. McKibbin and Fernando (2020) reveals the pandemic induced illness and mortality to cause decline in labour supply by 0.4% to 4.6%, fall in consumption by 0.8% to 4.5% including tourism and trade reductions, financial market disruption, increase in costs of doing business by 25% to 50%, and peak GDP loss by 2% to 8% in developed economies and 1.6% to 6% in developing economies. Baker et al. (2020b) estimates peak GDP loss of 3% to 20% in the United States, while Banco de España (2020) reveals reduced domestic demand and peak GDP loss of 8.5% to 14.1% in Spain. Breisinger et al. (2020) estimates zero internal tourism, 10% to 15% reduction in remittance and Suez Canal revenue, and peak GDP loss by 2.1% to 4.8% in Egypt in 2020.

Economic effects of restrictions due to the pandemic are likely to be substantial in developed countries (OECD 2020a) compared to developing

countries (IMF 2020). However, external shocks create economic policy uncertainties, increase financial market volatility and restrict investment in developing economies (Huidrom et al. 2020) and extremely poor population unable to comply with the poorly designed pandemic restrictions (Chang and Velasco 2020) due to difficulties in adhering social distancing in crowded localities and informal work condition, thereby affecting more women and small farmers. Industrial metals prices fall by 24%, while agricultural commodity price declines in first quarter of 2020 (World Bank 2020c), however, export bans and excess buying result in localized spikes in food price despite ample global supply (Voegele 2020). Food insecurity increases due to breakdowns in local agricultural supply chains and restricted trade in developing countries and increase hunger twice in 2020 (WFP 2020).

IV. Long-term effects of Covid-19

Global economy experienced slower growth prior to the pandemic due to global recession of 2009 and likely to slow down growth potential in developing economies in near future (Kilic et al. 2020). Long-term economic effects are likely to be substantial due to wide-ranging uncertainties in supply chains and working conditions, employment and income prospects, consumer spending and business investment (McKibbin and Fernando 2020). Low capacity utilization is likely to discourage investment, loss of human capital, reduce job-search, and labour productivity. COVID-19 is likely to adversely affect long-term growth prospects in developing countries due to GVCs disruption and trade shocks (Didier et al. 2020) accompanied by financial crises.

V. Economic impacts of COVID-19 in South Asia

In South Asian countries pandemic restrictions heavily impact short-term economic activities including manufacturing, exports, and consumption. Industrial and services activities declined sharply with collapse in domestic and global demand. For instance, auto-manufacturing in India and Pakistan, and garment production in Bangladesh have been adversely affected due to sharp decline in demand. Business confidence and private consumption have been severely hindered in Bangladesh, India, Nepal, and Pakistan. Closure of SMEs has caused huge decline in employment and private investment. Tourism declined sharply in Bhutan, Nepal, which affects more than two-thirds of GDP in these countries. Fiscal stimulus and monetary measures cover health expenditure, social transfers and protection, credit support to SMEs and food security. Growth of GDP, consumption, investment, exports and exports in South Asia is given in table 1.

Prior to the pandemic, financial markets and capital flows were rattled due to the global crisis and deteriorated more in large economies of the region. Real GDP growth at market prices in South Asian countries is given in table 2. Regional growth is estimated to decline by 2.7% in 2020 due to pandemic

induced restrictions in consumption and services and private investment (see table 1). In India, growth slowed to 4.2% in 2019-2020 and estimated to decline by 3.2% in 2020-2021 due to stringent restrictions to contain the pandemic spread, despite fiscal stimulus and monetary easing. Pakistan and Afghanistan are likely to experience economic slowdown with output contractions by 2.6% and 5.5% respectively in 2020 and 2021, while Bangladesh and Nepal are expected to experience substantial decline in growth at 1.6% and 1.8% due to pandemic-induced disruptions, fall in exports and remittances. In Sri Lanka, output is likely to decline by 3.2% due to supply chain disruptions and sharp decline in tourism, while Maldives is expected to experience a huge decline in GDP by 13% in 2020 due to decline in tourism. Sharp decline in oil prices could provide cushion to fiscal and current account balances in South Asian economies, particularly India and Pakistan, which may offset decline in remittance inflows in 2020. In 2021, GDP growth is estimated to recover to 2.8% due to resumption in services and manufacturing in the region, however, slow revival of tourism will affect the pace of economic recovery.

Table 1: Growth of GDP, consumption, investment, exports and exports in South Asia (%)

Items	*2017*	*2018*	*2019*	*2020[1]*	*2021[1]*	*2020[2]*	*2021[2]*
South Asia's GDP	6.5	6.5	4.7	-2.7	2.8	-8.2	-3.1
GDP per capita (US$)	5.2	5.2	3.5	-3.8	1.7	-8.1	-3.1
Private consumption	6.4	7.2	4.5	-2.6	3.3	-8.4	-3.0
Public consumption	12.1	8.7	10.8	8.4	6.3	0.6	-1.3
Fixed investment	5.8	11.2	-0.1	-8.2	1.2	-14.6	-5.3
Exports, GNFS	4.8	10.2	0.3	-12.5	4.1	-17.7	-1.8
Imports, GNFS	14.1	13.2	-5.8	-13.6	2.6	-18.4	-3.5
Net exports, contribution to growth	-2.6	-1.6	1.8	1.1	0.1	1.4	0.6

Source: World Bank (2020d)

Note: Data for 2019 are estimates and 2020 and 2021 are forecasts, while [1] refers to projections made in January 2020 and [2] refers to projections made in June 2020 and shows percentage point differences from January 2020 projections. GNFS stood for goods and non-factor services.

Table 2: Real GDP growth at market prices in South Asian countries (%)

Country	*2017*	*2018*	*2019*	*2020[1]*	*2021[1]*	*2020[2]*	*2021[2]*
Afghanistan	2.7	1.8	2.9	-5.5	1.0	-8.5	-2,5
Bangladesh	7.3	7.9	8.2	1.6	1.0	-5.6	-6.3
Bhutan	6.3	3.8	3.9	1.5	1.8	-4.1	-5.8
India	8.3	7.0	6.1	4.2	-3.2	-0.8	-9.0
Maldives	6.8	6.9	5.2	-13.0	8.5	18.5	2.9
Nepal	8.2	6.7	7.0	1.8	2.1	-4.6	-4.4
Pakistan	5.2	5.5	1.9	-2.6	-0.2	-5.0	-3.2
Sri Lanka	3.6	3.3	2.3	-3.2	0.0	-6.5	-3.7

Source: World Bank (2020d)

Note: Data for Afghanistan, Maldives and Sri Lanka refer to calendar year and for other countries based on fiscal year and data for Pakistan are calculated at factor cost. Data for 2019 are estimates and 2020 and 2021 are forecasts, while [1] refers to projections made in January 2020 and [2] refers to projections made in June 2020 and shows percentage point differences from January 2020 projections COVID-19 induced restrictions could affect the regional economy the most due to huge population, large informal sectors, high poverty and inequality, and less developed health infrastructure with large potential to increase poverty and food shortages in vulnerable economies (UN 2020). Persistent disruptions in global financial markets, surge in non-performing assets, inefficiencies, information asymmetry and high levels of debt are likely to adversely impact financial sustainability and thus reduce capital flows and investment across the region and limit the effect of fiscal stimulus. Despite limited integration into GVCs, inadequate intermediate inputs are likely to impact pharmaceutical and textile sector in Bangladesh and automotive industry in India.

VI. Policy Implications

Sufficient resources should be allocated to improve health care systems to cope the increasing demand of health care services. Trade restrictions on medical and health products should be removed to support the vulnerable regional economies. Targeted policies are needed to complement the fiscal stimulus and monetary easing at the national level. Economies with vulnerable populations need external support to contain the crisis costs, for which robust multilateral cooperation is essential. The worst affected households, informal sector, and businesses should be provided the additional targeted social protection, direct social transfers and fiscal support respectively in post-crisis era for economic resilience and recovery. There is need to temporarily waive the tax and rental payments for the most affected households and businesses. Laid-off workers should be given sufficient unemployment insurance and SMEs should be given reasonable wage subsidies. SME creditors should be permitted to temporarily defer the loan and interest payments with no penalty.

Taming the COVID-19 needs robust multilateral cooperation for development of vaccine to counter the pandemic, avoid trade restrictions for medical and essential supplies, and provision of grants and emergency funds to financially fragile economies with limited health care system. Robust policy measures will be needed for speedier economic recovery once the pandemic abates and containment measures removed through strong initiatives at the national level and multilateral cooperation. Removing of containment measures is likely to be steady, however, voluntary social distancing is likely to persist. SMEs should slowly resume economic activities after relaxation in restrictions, but uncertainties in demand and supply need to tackle patiently. Fiscal stimulus and monetary easing need coordinated actions from all

stakeholders to increase demand during recovery. Hiring subsidies should be extended to motivate SMEs to reemploy the workers. Inflation expectations should be modest to tackle supply chain disruptions and persistently weak demand.

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