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COVID-19: THE ECONOMIC OUTLOOK, IMPACT, AUTHORITIES AND LONG TERM STRATEGIES OF NEPAL

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Abstract:

The paper introduces a coronavirus pandemic impact on the economy from a variety of dimensions such as economic outlook, growth shock, recession curve analysis, the role of regulators and proposed long term strategies. This paper also analyzes the impact of the coronavirus pandemic on the growth of the economy. The study observed about the consequences of the pandemic with the help of three shaped of curve called U, L and V. Also, this study used the secondary published data from International financial institutions such as World Bank and Asian Development Bank as to describe the current growth and also predict the pre-COVID economic growth of Nepal.

Keywords:

Economic Shock, Regulators, Recession, Governance, Role of the State

JEL Classification: E66

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1. Economic Outlook

The coronavirus pandemic is the most significant negative shock since the global financial crisis and is causing severe damage to global activity .Early estimates predicted that, should the virus become a global pandemic, most major economies will lose at least 2.4 percent of the value their gross domestic product (GDP) over 2020, leading economists to already reduce their 2020 forecasts of global economic growth down from around 3.0 percent to 2.4 percent. To put this number in perspective, global GDP was estimated at around 86.6 trillion U.S. dollars in 2019 – meaning that just a 0.4 percent drop in economic growth amounts to almost 3.5 trillion U.S. dollars in lost economic output. However, these predictions were made before COVID-19 becoming a global pandemic, and before the implementation of widespread restrictions on social contact to stop the spread of the virus.

Nepal's economy grew to an estimated 7.1% in FY2019. GDP growth will likely moderate to 5.3% in FY2020 largely owing to the global outbreak of COVID-19 pandemic. The economy may rebound to 6.4% in FY2021 with the resurgence of economic activities post-COVID. Inflation rose to 4.6% in FY2019 and will inch up to 6.0% in FY2020 and stay moderate at 5.5% in FY2021. Hence, the evolution of the global pandemic—and thus the outlook for the global and regional economy—is highly uncertain. Growth could turn out lower, and the recovery slower, than we are currently forecasting. For this reason, strong and coordinated efforts are needed to contain the COVID-19 pandemic and minimize its economic impact, especially on the most vulnerable. (ADB, 2020 April Report)

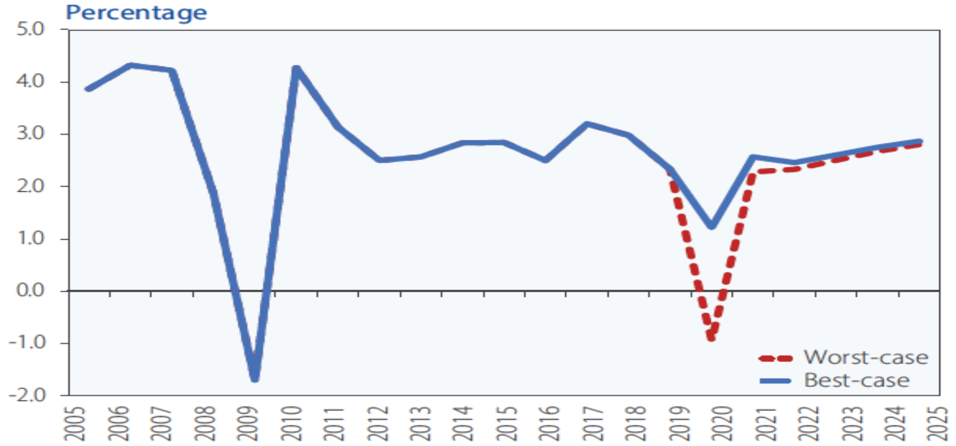
While there is no way to tell exactly what the economic damage from the global COVID-19 novel coronavirus pandemic will be, there is widespread agreement among economists that it will have severe negative impacts on the global economy.

2 .Growth shock - Global Growth vs Nepal Growth

A raging pandemic unleashed by a highly contagious COVID-19 virus has triggered unprecedented restrictions not only on the movement of people but also on a range of economic activities, and the declaration of national emergencies in the worldwide. Growing demand for urgent healthcare and rising death tolls are straining national healthcare systems. The pandemic is disrupting global supply chains and international trade. With nearly 100 countries closing national borders during the past month, the movement of people and tourism flows have come to a screeching halt. Millions of workers in these countries are facing the bleak prospect of losing their jobs. Governments are considering and rolling out large stimulus packages to avert a sharp downturn of their economies which could potentially plunge the global economy into a deep recession.

In the worst-case scenario, the world economy could contract by 0.9 percent in 2020 (Figure 1). The coronavirus outbreak has dealt a massive blow to global activity, and the associated costs and spillovers will significantly erode the global outlook. The pandemic also compounds other downside risks, such as further disruptions to trade relations, spillovers from sharp downturns in major economies, and disorderly commodity and financial market developments. Against this backdrop, many economies are not adequately prepared to confront the negative shocks related to the materialization of these risks

Figure 1
World growth outlook for 2020 in the best- and worst-case scenarios, as of late March 2020



Source: UN DESA.

Whereas the economic growth of Nepal in FY2020 is anticipated to contract from pre-COVID estimate of 6.3% to 5.3% as shown in the following figure 2. However, growth could further contract if the lower remittances, trade and tourism, and broader disruptions caused by the COVID-19 outbreak. Economic growth during FY21 is also likely to remain subdued due to the lingering effects of the pandemic with some recovery expected in FY22. Therefore, the urgent and bold policy measures are needed, not only to contain the pandemic and save lives but also to protect the most vulnerable in our societies from economic ruin and to sustain economic growth and financial stability.

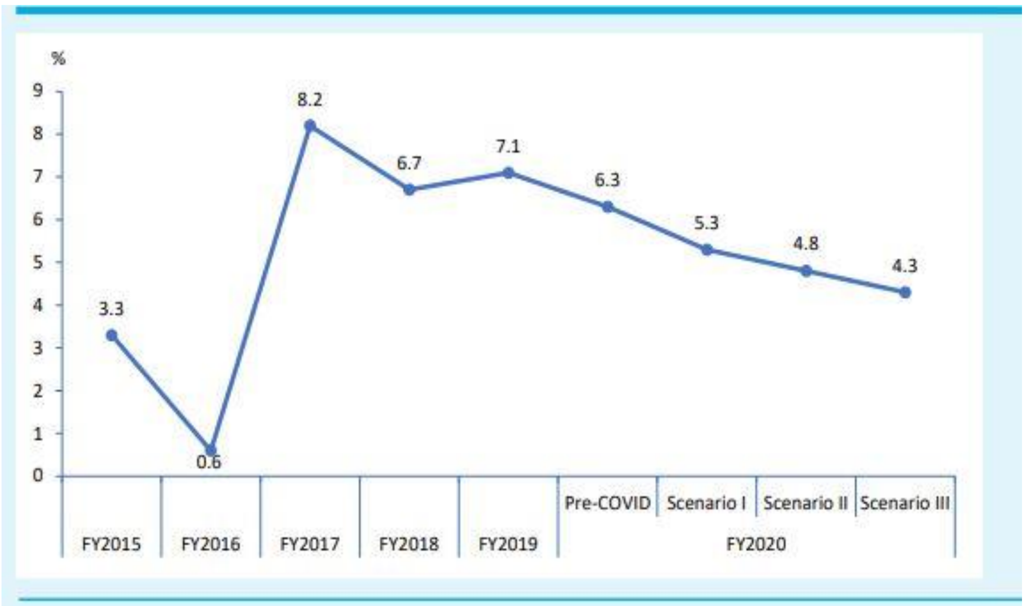


Figure 2: GDP growth rate at Market Price (%) Source: ADB, April Report

3. Economic Consequences

The impact of the coronavirus pandemic on growth in the economy will depend on how the outbreak evolves. If the outbreak is largely contained by the second half of the year and measures to stop the spread of the virus—including quarantines, travel restrictions, and international border closures—are lifted, economic activity could resume, supply chains could recover, and financial markets and commodity prices could stabilize. The following are the major economic consequences towards the Nepalese economy.

- COVID-19 pandemic will hard hit Nepal’s tourism industry. With the outbreak of disease, tourist arrivals dipped by 2.0% y/y in January 2020 and 1.0% y/y in February 2020. Hotels and restaurant have been shut temporarily. Overall, travel receipts which supply about 2.0 to 3.0% of GDP will decline this fiscal year. Remittance income will be severely affected due to COVID-19 pandemic.
- The income fell by 0.2% y/y in mid-February 2020 after rising by 16.0% in the year earlier period. Remittance income, about $ 8 billion per fiscal year, or 26% of GDP, is one of the major sources of foreign earnings. A sharp decline of remittance will undermine Nepal’s external stability. (ADB, 2020 April Report)
- International trade will be adversely affected with the temporary closure of borders. Only essential goods such as food and medicine are being imported. Commodity prices particularly of food and beverages has risen on account of supply chain disruptions.
- Decreased remittance income compounded by a fall in tourism receipts will weaken domestic demand. Domestic spending particularly on travel and recreation will plunge this fiscal year because of COVID-19 pandemic. Again, the extent of weakening will rest on the persistence of this disease. The decline could be more if there is a wide and prolonged outbreak of the COVID-19 pandemic.
- Foreign earnings will be hard-hit. Domestic production will be badly affected. Hundreds of thousands of people living on daily wages may be pushed to further poverty due to prolonged shutdown of the economy. Remittance income will substantially fall as out-migration will be totally discontinued.
- The tightening of credit conditions could force firms to deleverage rapidly, exacerbating a downturn. Banks may be forced to reduce lending, adding to downward pressures in the credit market. As corporate and consumer loan defaults rise, this would also result in a deterioration in bank balance sheets, further constraining banks’ ability to extend credit, and increasing the fragility of domestic banking systems.
- The adverse effects of prolonged restrictions on economic activities in developed economies will soon spill over to developing countries via trade and investment channels. Least developing countries with highly concentrated trade exposures to the world economy are particularly vulnerable to growth downturns. All commodity dependent economies—have similarly high levels of external debt.
- Growing debt distress—and likelihood of a debt crisis—could force many governments to sharply curtail public expenditure at a time when they need to ramp up spending to contain the pandemic and support consumption and investment.

4. Economic Shock: 3 scenarios

4.1 Shape of Curve

The two most important questions you will hear during any recession are “When will it end?” and “How quickly will we recover?” The answers to both of these questions can be found by analyzing the shape of the recession.

Recessions come in many shapes and sizes. However, economists tend to refer to the following three shapes the most:

– V-shaped recession

– U-shaped recession

– L-shaped recession

- V-Shaped Recessions

V-shaped recessions are recessions that begin with a steep fall but then quickly find a bottom, turn back around and move immediately higher. A V-shaped recession is a best-case scenario. The recession of 1990 to 1991 and the recession of 2001—both of which only lasted eight months—are considered to be V-shaped recessions.

- U-Shaped Recessions

U-shaped recessions are recessions that begin with a slightly slower decline but then remain at the bottom for an extended period of time before turning around and moving higher again. The recession from 1971 through 1978—when both unemployment and inflation were high for years—is considered a U-shaped recession.

- L-Shaped Recessions

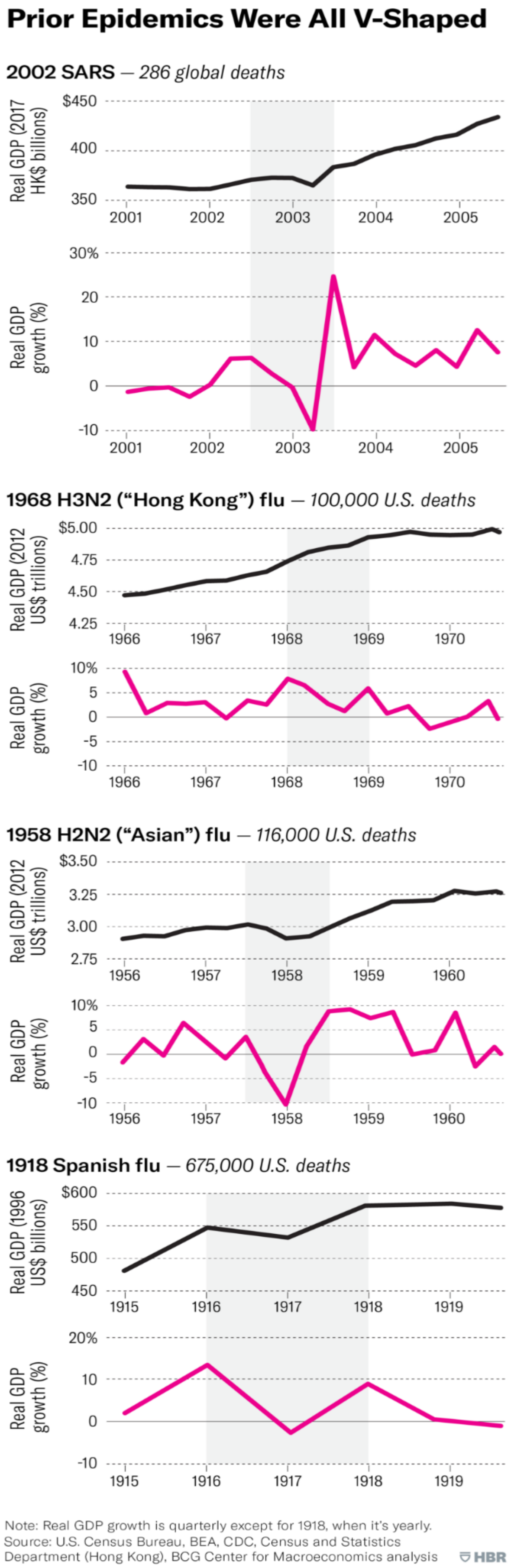
L-shaped recessions are recessions that fall quickly and fail to recover. An L-shaped recession is a worst-case scenario because they offer no hope of recovery. The Japanese recession that began in the early 1990s is considered an L-shaped recession

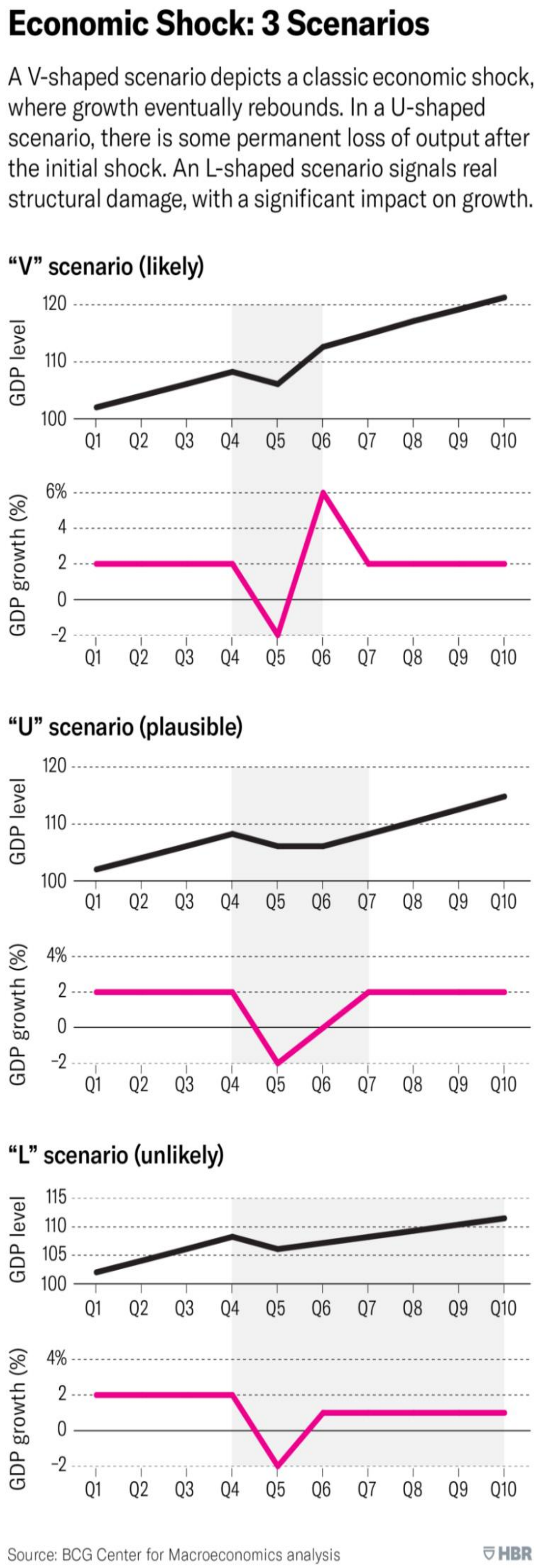
All there curve are also present in following figure as "V" scenario, "U" scenario and L "scenario" as likely , plausible unlikely condition respectively.

4.2. Prediction of V-shaped recession

- If the virus spreads to most countries and efforts to contain the outbreak spill into the third quarter of 2020, financial market pressures continue, commodity prices remain weak, and domestic healthcare systems are strained, the growth impacts will be more severe. Either way, the region is bracing for a recession.
- Assuming that prior epidemics such as SARS, the 1968 H3N2 (“Hong Kong”) flu, 1958 H2N2 (“Asian”) flu, and 1918 Spanish flu all are V-shaped as describe in following figure 2.
    - A fairly sharp drop due to health shock, economic slowdown, corporate defaults, corporate bankruptcies, as well as layoffs.
    - A fairly speedy recovery may be expected using measures like support for health system, shield people and firms, reduce financial stress and plan for recovery by using true economic policy measures.
- Partial recovery in 2021 almost after a year which is based on the direction of curve as shown in following diagram.

- Hence, a V-shaped scenario depicts a covid economic shock where growth may be eventually rebounds.


Prior Epidemics Were All V-Shaped
2002 SARS — 286 global deaths
Real GDP (2017 HK$ billions)
$450
400
350
2001 2002 2003 2004 2005
Real GDP growth (%)
30%
20
10
0
-10
1968 H3N2 ("Hong Kong") flu — 100,000 U.S. deaths
Real GDP (2012 US$ trillions)
$5.00
4.75
4.50
4.25
1966 1967 1968 1969 1970
10%
5
0
-5
-10
1958 H2N2 ("Asian") flu — 116,000 U.S. deaths
Real GDP (2012 US$ trillions)
$3.50
3.25
3.00
2.75
1956 1957 1958 1959 1960
1918 Spanish flu — 675,000 U.S. deaths
Real GDP (1996 US$ billions)
$600
550
500
450
1915 1916 1917 1918 1919
20%
Note: Real GDP growth is quarterly except for 1918, when it's yearly.
Source: U.S. Census Bureau, BEA, CDC, Census and Statistics Department (Hong Kong), BCG Center for Macroeconomics analysis
HBR


Economic Shock: 3 Scenarios
A V-shaped scenario depicts a classic economic shock, where growth eventually rebounds. In a U-shaped scenario, there is some permanent loss of output after the initial shock. An L-shaped scenario signals real structural damage, with a significant impact on growth.
"V" scenario (likely)
GDP level
120
110
100
Q1 Q2 Q3 Q4 Q5 Q6 Q7 Q8 Q9 Q10
GDP growth (%)
6%
4
2
0
-2
"U" scenario (plausible)
4%
"L" scenario (unlikely)
115
105
Source: BCG Center for Macroeconomics analysis
HBR

5. Nepal's Five Regulators: Authorities and Working Areas

Regulators	Focus or Working area
Ministry of Finance	• Strengthened international cooperation for getting crisis fund by WB/IMF its building capacity for utilization. • Short Run: Direct wage or income support measures, tax deferrals, government-subsidized short-term work schemes and direct cash payments social protection programs can play a role in limiting the socio-economic effects. • 'Hysteresis' in fiscal policy.
Central Bank	• Quantitative easing • Peg interest rates at zero to support government borrowing by Central Bank • Slashing interest rates and injecting liquidity into the financial market. • Prompt response to coronavirus hard-hit sector by discounting in loan payment. • Stable the inflation rate using proper monetary measures. • Enhancing the liquidity into broader range in hard-hit sector of the economy. • Make a policy to provide easy loans to farmers and establish the agro-based industry to boost domestic demand.
Central Government	• Process for crisis Management: Plan, Supplies, Implication finding solution and monitoring. • Identification of the goods and services that should be prioritized in the current crisis. E.g. medicines, medical equipment, protective equipment, and testing kits, besides food and other goods related to basic needs, communications, and the services provided by public utilities, must be given priority. The logistics activities needed for delivering the goods are also indispensable • Determination of the input-output linkages that lead to the desired output. Detailed real-time information at the firm and individual level will be essential for estimating demand by region and by type of good, and to monitor production chains. • Determination of which resources may be allocated to the industries in the essential input-output linkages. • Large stimulus packages to address the health, economic and social impacts of the pandemic • Targeted at enhancing capacities of national health sectors to ensure the availability of medical supplies, free and aggressive COVID-19 testing and enhanced healthcare coverage, and funding for research and development of vaccines and treatments with coordination with federal and local level government.
Federal Government	• Making a plan according to the central government, ease for medical supplies to the local level, training, supervision and monitoring. • Need to organize the production of basic weaponry — testing kits, cleansing chemicals, masks, protective clothing, and ventilators— across the country.
Local Government	• Implementation of the whole Plan adopted by central and Federal government, capacity building, finding the required human resource and equipment, what type of infrastructure is needful and management of infrastructure in a well manner.

6. Long- Term challenges and policies

While confronting the near-term impact of the coronavirus pandemic is the primary focus of policy efforts, the economy eventually need to return to targeted structural reforms that are essential to improve long-term productivity and generate long-term growth. Specifically, reforms are needed to strengthen governance, reassess the role of the state in the economy, improve the business climate, and promote the appropriate diversification of commodity-dependent economies. Weak external demand highlights the importance of policies that expand domestic sources of productivity and long-term output growth, such as investment in human and physical capital. Mitigating the risks associated with climate change and other disasters, such as pandemics, highlights the need for emergency preparedness.

The following are six priorities need to be followed.

- **First, continue with essential containment measures and support for health systems.**
  - Prioritizing health spending for testing and medical equipment; pay doctors and nurses; make sure hospitals and makeshift clinics can function i.e. carefully reallocating limited public resources.
  - It also means *increasing the flow of resources* to these countries. That includes the flow of vital goods: we must minimize disruptions to supply chains and, with immediate effect, refrain from export controls on medical supplies and food.
- **Second, shield affected people and firms with large, timely, targeted fiscal and financial sector measures.**
  - It includes tax deferrals, wage subsidies and cash transfers to the most vulnerable; extending unemployment insurance and social assistance; and temporarily adjusting credit guarantees and loan terms.
  - Some of these measures have been taken in the first wave of policy support i.e. *Lifelines for households and businesses are imperative.*
  - Need to prevent liquidity pressures from turning into solvency problems *and avoid scarring of the economy that would make the recovery so much more difficult.*
- **Third, reduce stress to the financial system and avoid contagion.**
  - Banks have built up more capital and liquidity over the past decade, and their resilience will be tested in this rapidly changing environment.
  - Monetary stimulus and liquidity facilities play an indispensable role. Interest rates have been lowered in many countries.
  - Central banks have activated swap lines and created new ones to reduce financial market stress.
  - Enhancing liquidity for a broader range of emerging economies would provide further relief. Importantly, it would also *lift confidence.*
- **Fourth, even as we move through this containment phase, we must plan for recovery.**
  - Minimizing the potential scarring effects of the crisis through policy action now. This requires careful consideration of when to gradually ease restrictions, based on clear evidence that the epidemic is retreating.
  - As measures to stabilize the economy take hold and business starts to normalize, we will need to move swiftly to boost demand. A coordinated fiscal stimulus will be essential. Where inflation remains low and well-anchored, monetary policy should remain accommodative. Those with

greater resources and policy space will need to *do more*; others, with limited resources will need *more support.*

- **Fifth, redefined the role of the state**
    - Governments must invest in, and in some cases create, institutions that help to prevent crises, and make us more capable to handle them when they arise.
    - Injecting stimulus into the economy while desperately trying to slow the spread of the disease, to protect vulnerable populations, and to help create new therapies and vaccines.
    - Governments need to better coordinate research and development activities, steering them towards public health goals.
    - Governments need to structure public-private partnerships to make sure both citizens and the economy benefit.
- **Sixth, enhancing the environment for growth by strengthening governance and fostering competitive markets.**
    - Addressing these weaknesses requires reforms to improve governance and the business climate.
    - Growth was only stronger in the economy with higher levels of government accountability.

7. Conclusion

The COVID-19 pandemic will not only suppress economic growth, it will also adversely impact sustainable development in the short run. In Africa, an outbreak of the virus is of extreme concern because of the fragility of countries' healthcare systems and because many of these economies already face significant public health challenges, particularly malaria, measles, HIV, and tuberculosis. During the 2014–16 Ebola outbreak, many of the deaths were due to resources being diverted away from other diseases. In Western Asia, the pandemic is likely to impact humanitarian action of the international community in Iraq, Syria and Yemen, where ongoing conflict still requires timely responses. The pandemic is also likely to undermine poverty eradication efforts. A pandemic-stricken economy that grinds to a halt puts the employment of many people at risk—either in the form of lower income, less paid working hours, or outright unemployment. Without prompt government support, households could quickly fall into poverty, reversing past gains. The pandemic will have differentiated employment and income effects, even in most developed economies. Evidence suggests that those at the lower end of the income distribution will suffer the most. Lower-income workers tend to enjoy less labor market protection —a considerable share of them work in informal sectors where protection is minimal; and even for those in the formal sectors, many are paid by the hour, with typically little or no paid sick leave. Furthermore, a high share of lower-income workers is employed in industries that are most affected by the pandemic, such as retail sales and food service industries, which require close physical proximity to others.

Lessons from previous infectious disease outbreaks, as well as the experiences of the countries that were hit early by COVID-19, clearly show that severe containment measures, such as social distancing requirements, shutdowns of nonessential businesses and entertainment, and school closures, are important measures in saving lives by "flattening the curve" of infections and preventing health care systems from being overwhelmed. Policy makers face difficult trade-offs between the health benefits of these policies and their economic costs, however, since the more successful the containment policies are, and the flatter the infection curve is, the deeper the economic recession becomes. The immediate policy priorities are bolstering health care systems to save lives, strengthening safety nets to provide relief to households, and providing support to the private sector to cushion the downturn and preserve jobs. To the extent fiscal space is available, broad-based fiscal stimulus can also help lift aggregate demand, but it will probably be more effective after the immediate crisis has passed and business operations begin to normalize .Monetary policy can also play an important role. Central banks should be ready to provide ample liquidity to banks and nonbank financial institutions, particularly to small and medium-size enterprises, which are prone to suffer more from the sharp disruption. Broader monetary stimulus, such as policy rate cuts or asset purchases, can lift confidence and support financial markets to offset the risk of a sizable tightening in financial conditions, given the volatility in markets. International coordination in monetary easing could further alleviate the volatility.

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