NOTE 1: 08 APRIL 2020

ECONOMIC FALLOUT OF COVID-19: GLOBAL ESTIMATES AND COUNTRY RESPONSES

Disruptions to supply chains, demand, international trade flows, and travel, along with lockdowns and collapsing stock prices, resulting from the coronavirus disease 2019 (COVID-19) have dealt a heavy blow to the global economy. The forecast risks are overwhelmingly on the downside and depend crucially on how governments respond. The impact is likely to be prolonged throughout 2020, and the recovery curve is also unlikely to be *V-shaped*, and rather could look more like a '*swoosh*' (think of the 'Nike' logo). In this note, we provide a recap of some of the global estimates and forecasts of the economic fallout due to COVID-19[1], provide a quick overview of economic relief packages announced by foreign countries, and give a snapshot of the recommendations by the International Monetary Fund (IMF) on economic relief measures.

Current Estimates of Global Economic Fallout

Macroeconomics and Growth:

- According to UN trade and development agency UNCTAD, the likely cost to the global economy is US$ 1 trillion in 2020, and in a so-called 'doomsday scenario' where global growth is just 0.5%, the cost would be as much as US$ 2 trillion[i]
- The IHS Markit forecast for world real GDP growth in 2020 has been revised down to 0.7%. Growth below 2.0% is classified as a global recession[ii]. They estimate a U-shaped rather than V-shaped cycle, as a sharp reduction in near-term growth is followed by a slow recovery.
- S&P Global Ratings believes the effects of the COVID-19 pandemic will push the world economy into recession, dragging full-year GDP global growth down to just 1.0 - 1.5%. S&P projects China's economy to expand 2.7% - 3.2%, and the Eurozone economy to contract 0.5% - 1.0% in 2020. Both S&P and IHS Markit predict US recession in Q2, if not sooner.
- Meanwhile, for Sri Lanka the estimates are few and far between. The Asian Development Bank estimates that COVID-19 will shave off 1.5% of annual GDP in 2020. The CBSL had originally forecasted 3.5-4.0% growth this year but is yet to release an official post-COVID-19 forecast.
- The Export Development Board has estimated a near 50% fall in exports this year to just above US$ 10 billion, from the original forecast[iii]. The rate of spread of the virus in Sri Lanka's key markets of USA, UK and Eurozone, as well as how effective the economic relief measures there will be, will crucially determine how soon our exports recover. Additionally, the ability of our exporter firms to survive the current dire conditions and have sufficient resilience and resources to respond when demand picks up, will also be a key factor to watch.

Unemployment and Jobs:

- The International Labour Organization (ILO) said the initial impact would be a loss of 25 million jobs globally[iv]. But in its latest report (April 2020) has warned that "there is a high risk that the end-of-year figure will be significantly higher"[v].
- Based on different scenarios for the impact of COVID-19 on global GDP growth, the ILO estimates indicated a rise in global unemployment of between 5.3 million ("low" scenario) and 24.7 million ("high" scenario) from a base level of 188 million in 2019. By comparison, the 2008-9 global financial crisis increased global unemployment by 22 million.

[1] Not meant to be an exhaustive review. Information collated between 19-26 March 2020

- Underemployment is also expected to increase on a large scale, as the economic consequences of the virus outbreak translate into reductions in working hours and wages.
- The ILO has just released an updated research note (07 April), and has estimated that COVID-19 is expected to wipe out 6.7% of working hours globally in Q2 2020 (equivalent to 195 million full-time workers). Large reductions are foreseen in the Arab States (8.1%, equivalent to 5 million full-time workers), Europe (7.8%, 12 million full-time workers) and Asia and the Pacific (7.2%, 125 million full-time workers).
- Upper-middle income countries (which Sri Lanka is now) is expected to shed 7.0%, or 100 million full-time workers, which "far exceeds the effects of the 2008-9 financial crisis"[vi]. The sectors most at risk include accommodation and food services, manufacturing, retail, and business and administrative activities.
- In the US, 9.95 million people filed for unemployment benefits in the two weeks up to 27th March[vii].

Supply Chains, FDI, Markets:

- The supply chain disruptions (mainly due to slowdown of manufacturing in China) could result in a US$ 50 billion decrease in exports across global value chains, according to UNCTAD[viii] (Figure 1 in Annexure).
- The outbreak could cause global foreign direct investment (FDI) to shrink by 5%-15%, the lowest levels since the 2008-2009 financial crisis (upper bound is if the outbreak lasts all of 2020)[ix]. A sample of the top 5,000 listed companies globally showed earnings forecasts for fiscal year 2020 have been revised down by an average of 9% (Figure 2 in Annexure). The automotive industry (-44%) and airlines (-42%) have been the hardest hit.
- The Dow Jones industrial average – a key gauge of share prices in the US – fell below its level on the day of Donald Trump's inauguration in January 2017 and has now dropped 10,000 points in a month.
- Oil prices have fallen by 8-10% with the cost of Brent crude hitting its lowest level in 18 years[x]. The sharp drop in oil prices will help energy consumers. For countries like Sri Lanka, It will greatly help our oil import bill (Balance of Payments benefit) and also will help public revenues (if GoSL keeps pump prices unchanged). But continued low oil prices will hurt energy producers. For Sri Lanka, these depressed oil prices will reduce incomes in oil producing countries, several of whom are host countries for Sri Lankan migrant workers and a source of large inflows of remittances.

Economic Relief Packages Announced by Countries

Below is a list of some of the measures taken by countries, especially those most affected. The most-affected countries are adopting a mix of measures - introducing cash transfers to give cashflow relief to people and businesses, easing tax regulations, and providing monetary stimulus to relieve credit conditions.

- **USA** has announced a US$ 2.2 trillion rescue plan called the CARES Act[xi], which includes direct cash payments to individual taxpayers (US$ 250 billion x 2), US$ 300 billion in loans to help small businesses avoid mass layoffs, US$ 50 billion to bailout the airline industry and US$150 billion to bailout other 'severely distressed sectors', which could include hotels and tourism.
- **EU** European Central Bank has announced a € 750bn asset-purchase programme to ease credit conditions.
- **UK** has announced a relief package amounting to 15% of UK GDP and worth around US$400 billion (£330 billion). This includes Government backed loans of US$ 398 billion (£330 billion) to support companies, a 3-month mortgage payment holiday for homeowners, and funding grants of up to £25,000 for smaller businesses

- **Italy** has announced a US$ 28 billion package for all aspects of the response. It extended tax deadlines for companies in affected areas and broadened the wage supplementation fund to provide income support to laid-off workers[xii]. The government has also allocated US$ 650 million to renationalize the Alitalia airline.
- **France** has announced a US$ 50 billion in emergency aid for small businesses who have lost out during the pandemic[xiii]. French Finance announced further tax breaks and a "solidarity fund" for struggling small businesses.
- **Spain** has committed US$ 220 billion (€200 billion) as a relief package, which includes $110 billion (€100 billion) of state loan guarantees, giving greater liquidity for all Spanish companies, a moratorium on mortgage payments and utility bills, US$ 658 million (€600m) to help vulnerable people and those depending on social services
- **South Korea** is providing income and VAT tax extensions to businesses in the affected industries. It has also introduced wage subsidies for small merchants and increased allowances for homecare workers and job seekers and expanded them to cover low-income households. Korea has also expanded lending for business operations and loan guarantees for affected small- and medium-sized enterprises.
- **China** is accelerating payments of unemployment insurance benefits and expanding social safety nets. It has also temporarily waived/suspended social security contributions for businesses. It is also easing the tax burden for firms in the most vulnerable regions and sectors, including transportation, tourism, and hotels.
- **Iran** has announced it will simplify taxation for corporations and businesses affected by the outbreak[xiv]. The government asked the IMF for a US$ 5 billion (€4.5 billion) emergency loan; the first time in six decades that the country has done so[xv]. US sanctions on the country are complicating the ability to receive international aid assistance.
- **Australia** has announced support package worth over $ 15 billion[xvi]. Under this, businesses will get up to $25,000 and instant tax relief, while welfare recipients will be eligible for one-off cash payments of AU$ 750. Nearly 700,000 SMEs will also be eligible for cash payments of between $2,000 - $25,000 to help pay wages or hire extra staff.
- **New Zealand** announced an economic support package worth $12.1 billion, almost half of which covers immediate wage subsidies for businesses and the rest for tax relief and sick leave support[xvii]. The package also includes a $100 million 'redeployment package', to help employees train to work in other industries; $ 2.8 billion in business tax changes, including a provisional tax threshold increase, and writing off interest on some late payments of tax; and a $ 600 million aviation support package. They have also announced the Government would providing insolvency relief to affected businesses, by way of special changes to the Companies Act[xviii].

IMF Recommendations on Economic Relief Measures

The IMF has suggested the following 3-pronged approach to fiscal policies responding to COVID[xix]:
- Provide wage subsidies to people and firms to help curb contagion
- Expand and extend transfers both cash and in-kind, especially for vulnerable groups
- Provide tax relief for people and businesses who can't afford to pay

Targeted economic policies are needed
- Considering that the economic fallout reflects particularly acute shocks in specific sectors, policymakers will need to implement substantial *targeted* fiscal, monetary, and financial market measures to help affected households and businesses.
- IMF guidance is to "Provide timely, targeted, and temporary cash flow relief to the people and firms that are most affected, until the emergency abates".

- Households and businesses hit by supply disruptions and a drop in demand could be targeted to receive cash transfers, wage subsidies, and tax relief, helping people to meet their needs and businesses to stay afloat.
- Where paid sick and family leave is not among standard benefits, governments should consider funding it to allow unwell workers or their caregivers to stay home without fear of losing their jobs during the epidemic.
- Broad-based fiscal stimulus consistent with available fiscal space can help lift aggregate demand but would most likely be more effective when business operations begin to normalize.

Easing credit conditions is a priority

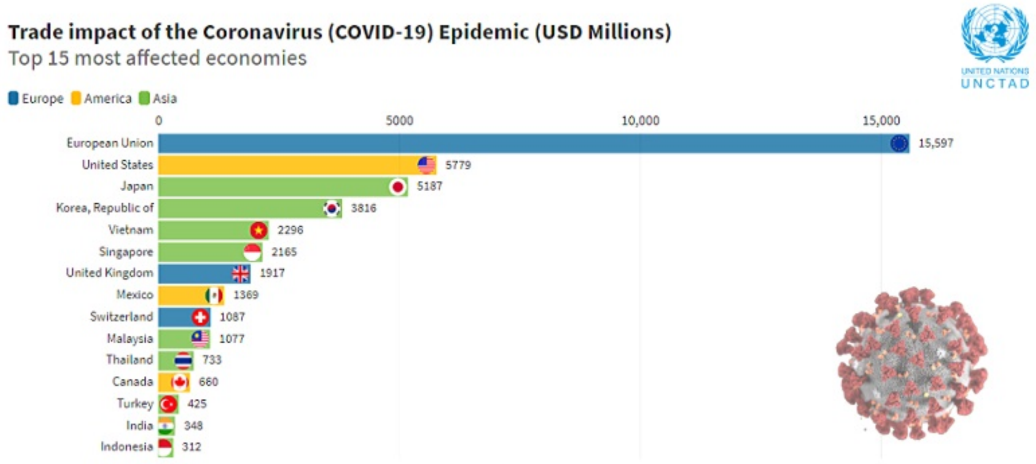
- Central banks should be ready to provide ample liquidity to banks and nonbank finance companies, particularly to those lending to small- and medium-sized enterprises, which may be less prepared to withstand a sharp disruption.
- Governments could offer temporary and targeted credit guarantees for the near-term liquidity needs of these firms. For example, Financial market regulators and supervisors could also encourage, on a temporary and time-bound basis, extensions of loan maturities.
- Broader monetary stimulus such as policy rate cuts or asset purchases can lift confidence and support financial markets if there is a marked risk of a sizable tightening in financial conditions (with actions by large central banks also generating favorable spillovers for vulnerable countries).

The Fund has made available US$ 50 billion via emergency financing to help low-income and emerging economies deal with the outbreak. Under this, Sri Lanka is also eligible for around US$ 400 million as proportion of its Special Drawing Rights (SDR) quota. Meanwhile the World Bank Group is preparing to deploy up to US$160 billion to developing countries over the next 15 months and already Sri Lanka has been given US$ 128 million as a fast-tracked funding package[xx].

This note was prepared at the invitation of AMCHAM by Anushka Wijesinha, Team Leader – Trade, PARTNER (Partnership for Accelerating Results in Trade, National Expenditure and Revenue), a USAID project implemented by Deloitte.
Disclaimer: The data featured in this note are believed to be from reliable sources. Any commentary expressed in the note are based on the views of the author and may not necessarily reflect those of USAID, Deloitte or the PARTNER project. For any comments, clarifications or feedback, write to anushka.wijesinha@pfmtsl.lk

Annexure

Figure 1: Trade Impact for Top 15 Most-Affected Countries



Source: UNCTAD estimates • Estimates are based on a drop of Chinese supply in February 2020 as measured by the Chinese PMI. The list does not include Taiwan Province of China and Hong Kong, SAR of China

Figure 2: Earnings Revisions and Capex of Top 5000 Listed Firms

Sector/industry	Number of companies with earnings revisions	Average earnings revision (%)	Share of capital expenditures (%)
Basic Materials	389	-13	8
Consumer Cyclicals	671	-16	16
Airlines	45	-42	2
Hotels, Restaurants & Leisure	111	-21	2
Consumer Non-Cyclicals	351	-4	6
Energy	243	-13	20
Healthcare	195	0	3
Industrials	739	-9	14
Automobiles & Auto Parts	142	-44	9
Technology	358	-3	11
Telecommunications Services	105	1	11
Utilities	175	-5	10
Grand Total	*3'226*	*-9*	*100*

Source: UNCTAD, based on data from Refinitiv SA.

Note: Top 5000 public companies that had at least one revision of earnings forecast for the fiscal year 2020 since 1 February 2020. A few outliers (5 in total) were excluded as extreme revisions of earnings were driven by idiosyncratic factors not related to Covid-19.

References:
[i] https://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=2300
[ii] https://ihsmarkit.com/research-analysis/the-global-economy-headed-for-recession.html
[iii] http://www.ft.lk/top-story/EDB-cuts-2020-export-target-by-7-75-b-on-COVID-19-worries/26-698531#.XoquxJYodLA.twitter
[iv] https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_738742/lang--en/index.htm
[v] https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_740893/lang--en/index.htm
[vi] *ibid*.
[vii] https://www.theguardian.com/business/2020/apr/02/us-unemployment-coronavirus-economy
[viii] https://unctad.org/en/PublicationsLibrary/ditcinf2020d1.pdf?user=1653
[ix] https://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=2299
[x] https://www.wsj.com/articles/u-s-oil-prices-plunge-to-lowest-level-in-more-than-17-years-11584538442
[xi] https://context-cdn.washingtonpost.com/notes/prod/default/documents/c6ca5eb3-9e59-4ed6-815a-807a559c7022/note/a9b21202-a1c9-48c1-b7ff-75213dbc9149.pdf#page=1
[xii] http://www.mef.gov.it/ufficio-stampa/comunicati/2020/documenti/DM-Proroga-Termini-Zone-Rosse.pdf
[xiii] https://www.forbes.com/sites/daviddawkins/2020/03/17/economic-cost-of-corona-us-eyes-on-europe-as-economic-rescue-packages-are-unveiledlatest/#1abd0f88709f
[xiv] http://mefa.ir/fa-IR/mefa/11352/news/view/15182/190870/Staging
[xv] https://www.dw.com/en/covid-19-hit-iran-asks-imf-for-aid-amid-us-sanctions/a-52763114
[xvi] https://www.abc.net.au/news/2020-03-12/coronavirus-economic-stimulus-combatting-the-spread-of-covid-19/12047050
[xvii] https://www.newshub.co.nz/home/politics/2020/03/covid-19-12-billion-package-includes-wage-subsidies-tax-relief-and-sick-leave-support-amid-coronavirus-pandemic.html
[xviii] https://www.companiesoffice.govt.nz/about-us/what-we-do/insolvency-relief-for-businesses-impacted-by-covid-19/

[xix] https://blogs.imf.org/2020/03/05/fiscal-policies-to-protect-people-during-the-coronavirus-outbreak/ and https://blogs.imf.org/2020/03/09/limiting-the-economic-fallout-of-the-coronavirus-with-large-targeted-policies/
[xx] https://www.worldbank.org/en/news/press-release/2020/04/01/world-bank-fast-track-support-covid19-corona