

The effect of Covid 19 on Sri Lankan Economy

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Abstract: The country doesn't have sufficient buffers to face the health crisis due to high public debt and large twin deficits. The pandemic risks weakening macroeconomic fundamentals further and impairing long-term growth and poverty reduction. Increasing public sector, current account deficits, public debt coupled with the shortage of external financing raise the risk of exchange rate depreciation and inflationary pressures. Fiscal pressures will increase due to Covid-19 expenditure and all the outflows have to be manage with USD 2 billion in 2021.

Keywords: Health Crisis, Covid 19, Sri Lankan Economy

1. Introduction

The first covid-19 case was diagnosed in China on December 10, 2019, and the first death was recorded one month later, on January 9, 2020. The World Health Organization declared it an emergency public health event on 30th January 2020. Nobody expected a lifestyle, livelihood, and economic disruption of this magnitude as a result of a health crisis. (Global Economic Effects of COVID-19, 2021) There are two sides' adverse effects on the domestic economy; external shocks and supply shocks. External shocks are with international trade which has diverse implications for commodity exporters and the oil demand. The supply shocks are with the supply chain in the domestic market at micro-level (Consumers, firms, household, businesses) to macro-level (GDP, Production Sectors, Inflation, Employment, and Unemployment).

2. Background of the Problem

For the last five years, the economic performance of Sri Lanka has been disappointing with growth rates being hardly positive on low (Annual Report of Sri Lanka). While slow growth had been one of the features of the country for several years, the emergence of social unrest was new with Covid19. Supporting the trends in social spending made possible by unusually high commodity prices with painful adjustments. In 2019, social unrest breaks out in Sri Lanka, reflecting a widening gap between popular expectations and economic and social realities with the Easter Sunday attack. The violence levels were high, leading to large numbers of dead and injured around 300, together with significant material damage in Christian Church. Some were directly related to economic developments, while others were clearly political in nature. These almost simultaneous but essentially uncoordinated outbursts of social unrest have been interpreted as manifestations of common, latent problems that affect the country at present. At the risk of satirizing, three main explanations; economic explanation, institutional explanation, and social explanation are emphasized in a different dimension.

In the economic explanation, years of slow economic growth and the need for painful fiscal adjustments are damaging the capacity of the population to cope. In the social explanation is the country with the highest levels of inequality, with wide gaps in living standards breeding frustration. In this case the response is to aim for better economic opportunities for the worse-off, with a determined focus on service delivery and social protection. In the institutional explanation, the ultimate cause of the unrest is the dissatisfaction with weak institutions unable to provide voice to the people and ensure the control of corruption. In this view, the country needs to focus on transparency and accountability, strengthening public financial management and especially public procurement.

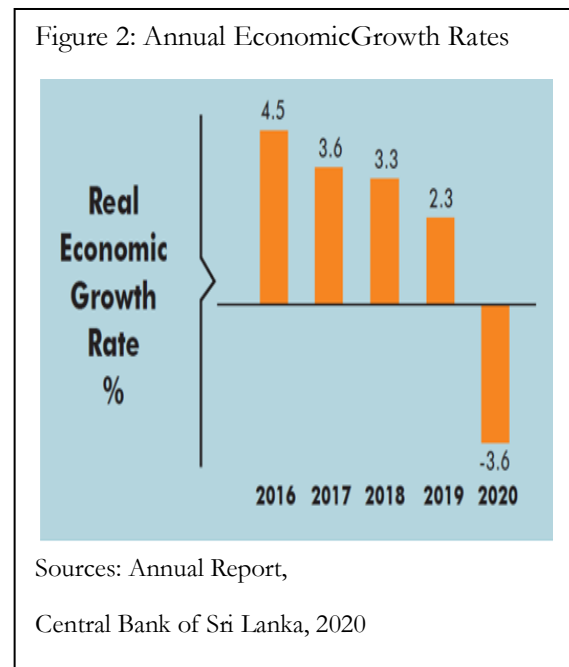
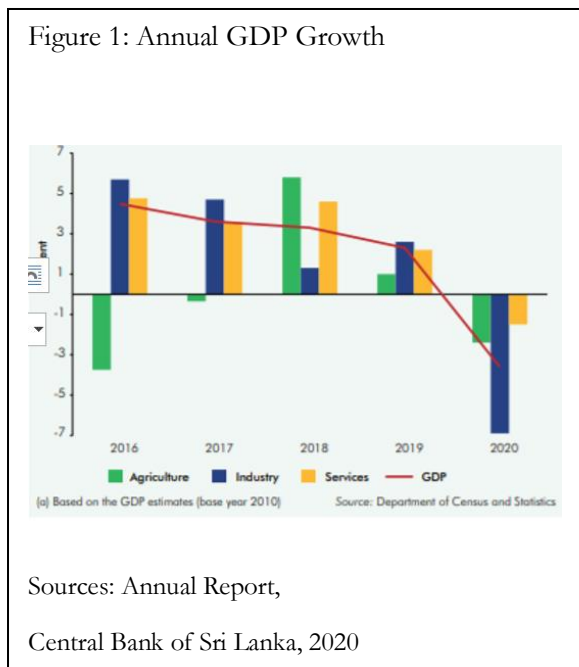
3. Methodology of the Study

All three explanations sound reasonable, that are necessarily supported by the secondary data and further data justified with household survey which was conducted with 150 household using purposively sampling in Sri Lanka and observations. Mainly, secondary data were collected from Annual Reports in Central Bank of Sri Lanka, The

World Bank, and Commercial Bank of Sri Lanka, HARTI Bulletins, UNDP, IMF Report and day to day media statements. One way to assess the relative merit of the three explanations is to analyze the descriptive way intensity of the social unrest and a set of economic, social and institutional indicators of the country.

4. Result and Discussion

On the economic explanation, According to the UN framework for the immediate socio-economic response to COVID-19 (2020, April) is with the factors; Incensement of poverty: about 60 million people have become extremely poor, Gender inequality: violence against women due to the domestic violence, Students out of schools: loss of opportunity for a large number of students to go to schools, Lack of adequate social protection: most of the people are not covered by social insurance or social assistance, Internally displaced people at risk, Income and job lost: most of the workers have lost their jobs and income, Remittances flows reduction, Decline in trade, Increase in food insecurity, Dramatic fall in tourism those same holds true for the magnitude of fiscal adjustment. Following the empirical analysis, the intensity of unrest can be measured through the number of people dying around 8000 so far and Covid infected number is around 4500 per day in connection with relative to the population. There is creating a huge correlation between the intensity of social unrest and the growth of income per capita over the last two years.

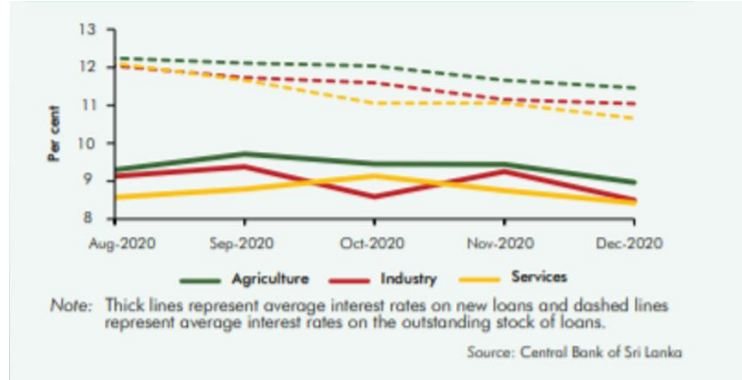


GDP at current market prices was estimated at US dollar 80.7 billion in 2020, which was a decline of 0.3 percent compared to 2019, where it stood at US dollar 84.0 billion (CB Annual Report, 2020). But in the absence of deep economic transformation, economic growth rates returned or even slower reducing any hopes of long-term convergence. Sharp decline of GDP have reported from industrial sector by -6.9% while decreasing reported from agriculture sector by -2.4% and services sector by -1.6% in 2020 with their some special features in Covid 19 pandemic. Services sector was run-out with work from home (WFH) method which is difficult in industrial sector with the essential of workers present in physical working environment. On that contest, government expenditure was increased by 9.8% with increasing of the health cost. Unfortunately, Gross domestic capital formation was decreased by 6.9% showing the weakling capabilities in the investment (Central Bank of Sri Lanka, 2020). Real economic growth rate was decreased continually from 2016 with miss-management of policies which was further accelerating with Covid 19 as -3.6% in 2020 (CB Annual Report, 2020).

The IMF recommended a combination of accommodative monetary policies characterized by low interest rates and central bank programs to facilitate credit availability, a continuation of fiscal support for individuals and firms, and engagement in a synchronized infrastructure investment program to promote growth. In the way of remarks by the government implemented the favorable fiscal adjustment of law rate of interest. According to an IMF analysis, all

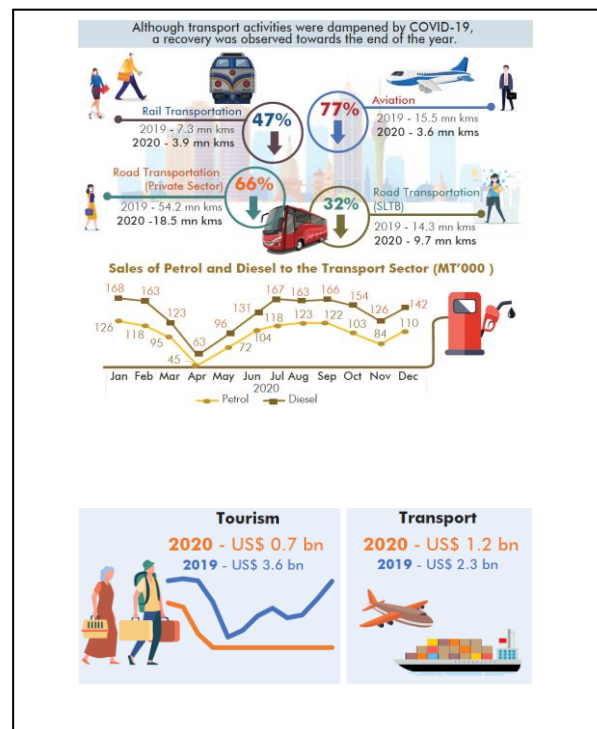
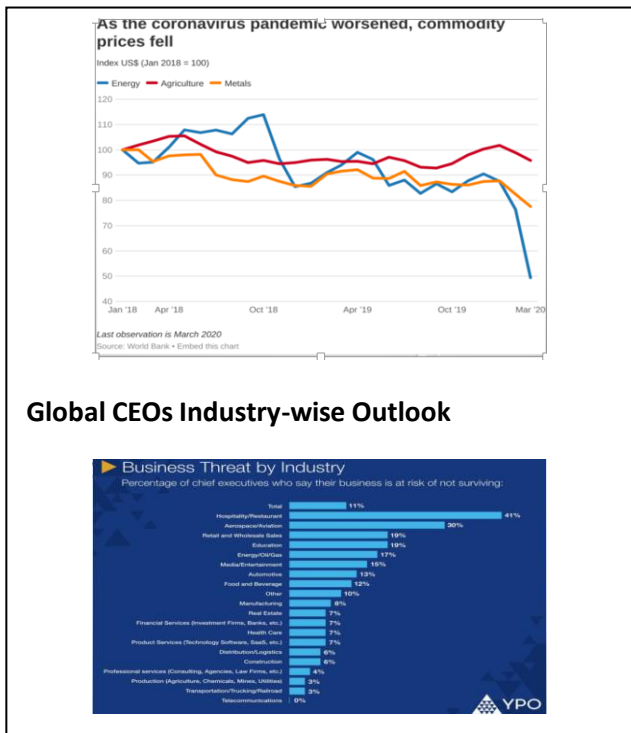
other things being equal and 1% in 2022 through 2025 would increase global GDP by 2% in 2025, compared with under 1.2 % growth for an unsynchronized approach.

Figure 3: Average rate of interested on loan granted to MSMEs by sectors



Minus economic growth rate was a result of the supply shocks which are created with health crisis in the pandemic reported the massive damage from industrial sector than that to the agriculture sector in 2020 (World Bank, 2020) in globally. Basically, supply shock is with industry explanation; 41% of the industry-wise Global CEOs have identified the highly treated business is hospitality and tourism with Covid 19 which way following 30% reported for aerospace/ aviation and 19% for retail/ wholesale and education. The situation was truly reported from Sri Lanka decreasing the tourism income from USD 3.6 billion to USD 0.7 billion in 2020 that was directly affected to reduce the foreign reserves to USD 5.7 billion in 2020 with minus balance of trade deficit which will show the direct high adverse relationship between institutional explanation and economic explanation.

Figure 4: Economics and Industry explanation



Source: Annual Report, Central Bank of Sri Lanka, 2020

High fluctuations were not reported from the Sri Lankan agriculture sector. Compared to the same period of last year, wholesale prices of most of the vegetable varieties had decreased by 7%-51%. The countries faced with

COVID-19 pandemic, adequate stocks of vegetables were available throughout the country as the harvesting of Maha season continued through April and May. However, regular vegetable distribution channels were interrupted at the beginning of shut down due to COVID-19 pandemic. Nevertheless, alternative distribution channels such as home delivery and online purchasing platforms emerged to deliver vegetables as well as other essential food commodities. Particularly, a Presidential Task Force was established during late March, and 13 the monitoring the distribution of agricultural produces was one of the main tasks of the Task Force.(Monthly food information Bulletin, HARTY, April / May 2020)

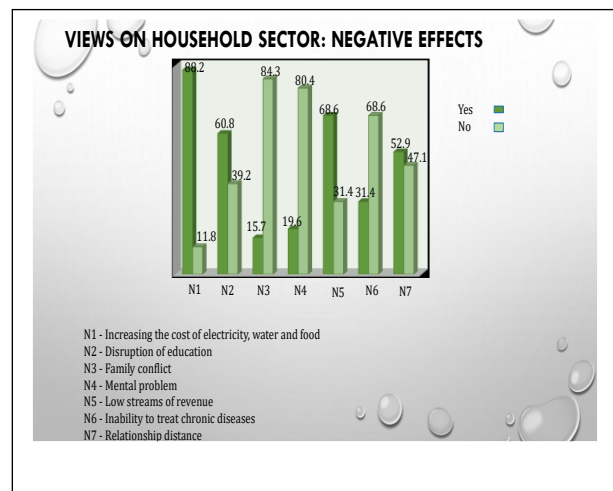
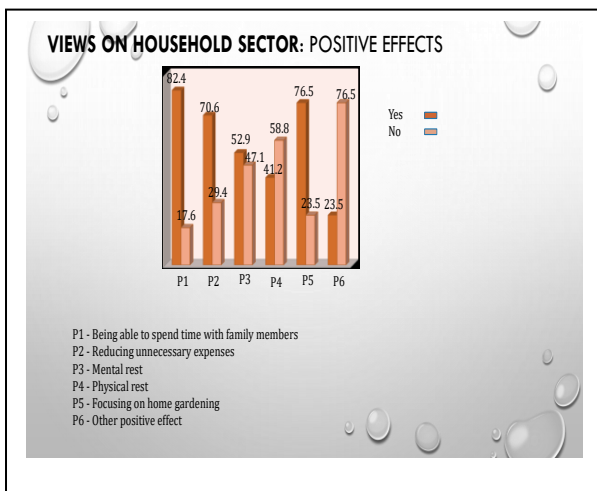
Table 01: Vegetable Prices

Vegetables	May 2020	May 2019
	Rs/kg	Rs/kg
Beans (green)	106.67	181.50
Carrot	62.67	118.25
Leeks	94.00	56.25
Beetroot	36.61	92.21
Knolkhol	40.00	82.25
Raddish	37.33	70.13
Cabbage	34.00	53.11
Tomato	58.78	78.00
Bittergourd	105.44	156.15
Luffal	95.67	103.25
Capsicum	89.33	140.75

Sources: Monthly food information Bulletin, HARTY, April / May 2020

On the social explanation, there has been more social unrest in the country with lower income inequality, and from an institutional point of view, social unrest was not significantly correlated with stronger democratic institutions or better control of corruption (World Bank, 2020).Over 2021, social unrest erupted across the country, reflecting a widening gap between popular expectations and economic and social realities from newly appointed government in 2020 and domestic oil prices collapsed in 2021 with the collapsing of international oil prices. Farmers, factory workers, government employers in various sectors protested against to the Sri Lankan government time to time in 2021 showing their social unrest. According to the household survey in 2020 in Sri Lanka has not been indicated the unrest which was not reported family conflict and psychological problem within the 80% of families those who have use the covid 19 period for physical and mental rest.

Figure 5: Views of Households



Sources: Primary data on Household survey, 2020

5. Concluding Remarks

- Employer-employee matches that took a long time to build and would remain profitable when the economy goes back to normal may be permanently dissolved due to this temporary shock. 61% CEOs in Sri Lanka point out that the Labour laws to support new reforms of work such as remote work, part time work, contract employment and flexible hours (Research & Development Unit, Commercial Bank, 2020). Therefore, proposed to protect workers, not jobs in the presence of adverse shocks affect specific firms, sectors, locations, and allowing sectorial restructuring is bound to increase efficiency.
- Job-specific human capital may be lost and ramping up production later may become more difficult. Therefore, recommended a dual approach to protecting jobs is worth considering.
- Strategically important firms and sectors may get obvious support, in exchange to a commitment to keeping their workers.
- Smaller firms can be reached by banks or other intermediaries. These financial institutions may be incentivized through risk sharing and guarantees, so that they ensure the availability of liquidity in a context of getting higher working capital needs. 55% CEOs in Sri Lanka ensure the bank and financial institution mitigate the burden they have to bear the economic stimulus and recovery program (Research & Development Unit, Commercial Bank, 2020)
- Facilitate to conduct of business during the social distancing period simplify the administrative processes such as procurement and the payment of taxes in several cases. 44% CEOs in Sri Lanka requested the tax concession to encourage large scale investment and 38% CEOs in Sri Lanka agreed with all export oriented business to be tax free for five years (Research & Development Unit, Commercial Bank, 2020).
- The governments expand the e-government in a way that is bound to increase transparency and efficiency over time. 59% CEOs in Sri Lanka view is loss making state own enterprises by making them more efficient and cost effectively. eg. Ceylon petroleum cooperation, CEB, Sri Lankan Airlines and Sri Lanka Railway.
- An unsuccessful renegotiation could result in another sell-off round of Sri Lankan assets, leading to pressure on official and alternative exchange rates, erosion of international reserves, acceleration of inflation, deepening and extending the recession, and increase unemployment and poverty. Financial market volatility adds to already high uncertainties on the amount of debt relief necessary to restore debt sustainability.

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