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Socioeconomic Impact of Coronavirus Disease 2019 in South Asia:

Fiscal Policy Response and Fiscal Needs for Supporting the Economic Recovery

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About the COVID-19 Response and Recovery project

This paper is an output from the project "Response and Recovery: Mobilising financial resources for development in the time of COVID-19", which is co-ordinated by the Debt and Development Finance Branch of UNCTAD and jointly implemented with ECA, ECLAC and ESCAP. This project is one of the five UN Development Account short-term projects launched in May 2020 in response to the COVID-19 crisis.

The project aims to enable low-income and middle-income developing countries (LICs and MICs) from Africa, Asia-Pacific, and Latin America and the Caribbean to diagnose their macro-financial, fiscal, external financial and debt fragilities in the global context, and design appropriate and innovative policy responses to the COVID-19 pandemic leading toward recoveries aligned with the achievement of the Sustainable Development Goals (SDGs).

Abstract

This paper assesses the socioeconomic impacts of Covid-19 in three South Asian economies -- Pakistan, Afghanistan, Sri Lanka -- and corresponding fiscal policy responses to mitigate these impacts. Further, it appraises the sufficiency of these fiscal policy responses to support the economic recovery in respective economies. It also estimates fiscal needs to finance the economic recovery and assesses existing fiscal space to meet the fiscal needs. Based on the assessment, it proposes possible option to enhance fiscal space. It also proposes policy measures to align fiscal stimulus to SDGs agenda and possible venues for regional cooperation to reach to a shared recovery.

Keywords: Fiscal Policy; fiscal stimulus; fiscal needs; economic recovery; economic policy; COVID-19; South Asia

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List of Acronyms

COVID-19	CORONAVIRUS DISEASE
GDP	GROSS DOMESTIC PRODUCT
SBP	STATE BANK OF PAKISTAN
CSO	CENTRAL STATISTICS ORGANIZATION
SDGS	SUSTAINABLE DEVELOPMENT GOALS
ADB	ASIAN DEVELOPMENT BANK
IPC	INCOME PER CAPITA
FAO	FOOD AND AGRICULTURE ORGANIZATION
SMES	SMALL AND MEDIUM-SIZED ENTERPRISES
WTTC	WORLD TRAVEL AND TOURISM COUNCIL
IMF	INTERNATIONAL MONETORY FUND
WB	WORLD BANK
UNESCO	UNITED NATIONS EDUCATIONAL, SCINTIFIC AND CULTURAL ORGANIZATION
LMS	LEARNING MANAGEMENT SYSTEM
ICUs	INTENSIVE CARE UNITS
PPES	PERSONAL PROTECTIVE EQUIPMENT
SMEDA	SMALL AND MEDIUM ENTERPRISES AUTHORITY
CAA	CIVIL AVIATION AUTHORITY
IATA	INTERNATIONAL AIR TRANSPORT ASSOCIATION
OCHA	OFFICE FOR THE COORDINATION OF HUMANITARIAN AFFAIRS
EFF	EQIPPED FOR THE FUTURE
ODA	OFFICIAL DEVELOPMENT ASSISTANT
MSMEs	MICRO, SMALL AND MEDIUM ENTERPRISE
SANEM	SOUTH ASIAN NETWORK OF ECONOMIC MODELERS
ESCAP	UNITED NATIONS ECONOMIC AND SOCIAL COMISSION FOR ASIA AND THE PACIFIC
CGE	COMPUTATION GENERAL EQUILIBRIUM
MPC	MONETARY POLICY COMMITTEE
CPI	CONSUMER PRICE INDEX
YOY	YEAR ON YEAR
FDI	FOREIGN DIRECT INVESTMENT
WIR	WORLD INVESTMENT REPORT
UNCTAD	UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT
UNAIDS	JOINT UNITED NATIONS PROGRAMME ON HIV AND AIDS
CAD	CURRENT ACCOUNT DEFICIT
NRPS	NON-RESIDENT PAKISTANIS
DAB	DA AFGHANISTAN BANK
SOE	STATE-OWNED ENTERPRISES
DSA	DEBT SUSTAINABLITY OF AFGHANISTAN
ICT	INFORMATION COMMUNICATION TECHNOLOGY
NFC	NATIONAL FINANCE COMMISSION
WDI	WORKFORCE DEVELOPMENT INSTITUTE
MPC	MARGINAL PROPENSITY TO CONSUME
OECD	ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT

EODB	EASE OF DOING BUSINESS
IT	INFORMATION TECHNOLOGY
OOF	OTHER OFFICIAL FLOWS
CSRS	CORPORATE SOCIAL RESPONSIBILTY
PIBs	PERMANENT INTEREST-BEARING SHARES
UNDESA	UNITED NATIONS DEPARTMENT OF ECONOMIC AND SOCIAL AFFAIRS
NGO	NON-GOVERNMENTAL ORGANIZATION
CBSL	THE CENTRAL BANK OF SRI LANKA
APTTA	AFGHANISTAN PAKISTAN TRANSIT TRADE AGREEMENT
SAARC	SAOUTH ASIAN ASSOCIATION FOR REGIONAL COORPORATION

Contents

1. COVID-19 impact and policy response to date

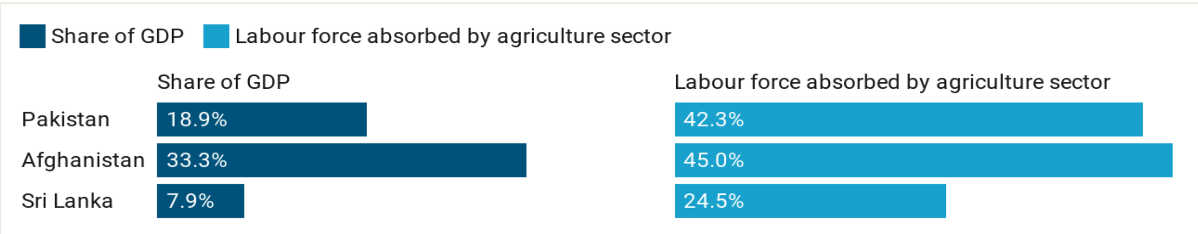
This section highlights impact of Coronavirus disease 2019 (COVID-19) on selected sectors of the economy and vulnerable groups of population for Pakistan, Sri Lanka and Afghanistan. It then traces the economic stress added by COVID-19 and corresponding fiscal policy responses, the fiscal stimulus. Finally, the section offers brief assessment of the impact of fiscal stimulus and identifies what can be done further to improve the impact.

1.1. Covid-19 impact on major sectors

1.1.1. Agriculture sector

Agriculture is the main source of income and livelihoods for an overwhelming majority of the

Figure 1: An agriculture share in GDP and labour force sector statistics



Source: Pakistan, Ministry of Finance, Afghanistan Living Conditions Survey 2016-17; World Development Indicators.

population in south Asian economies. The impact of Covid-19 on agriculture therefore has brought unprecedented challenges for the region. The agriculture sector contributes 18.9% to GDP and employs 42.3% of total employed labour force in Pakistan (figure 1) (Government of Pakistan-Ministry of Finance, 2020).

Agricultural exports formed around one fifth (19.1%) of Pakistan's total exports in 2019 (SBP, 2019). The dependence of Afghanistan on agriculture is highest and it accounts for one third (33.3%) of GDP in Afghanistan and generates 45% of the total employment (CSO, 2018). The sector contributes 7.9% to GDP of Sri Lanka and absorbs 24.5% of employed labour force.[1]

Stringent lockdown in Pakistan[2] disrupted the food supply chains of mainly high-value agricultural products such as vegetables, fruits, and milk, and farm inputs. The impact was lower on the wheat

1 Retrieved from World Development Indicators.

2 The governments of Sindh and Balochistan announced province-wide lockdowns on 24 March 2020. The federal government followed soon after, imposing on 1 April 2020 a nationwide lockdown, which lasted until 9 May 2020.

harvest as the lockdown was not fully imposed in the rural area. The harvest and marketing of wheat continued in rural areas. The socioeconomic impact of the pandemic on the farming community, particularly small and marginal farmers, however, may persist and jeopardize the performance on SDG 1 (No Poverty) and SDG2 (No Hunger).

Experts believe that the measures to control the pandemic have threatened the food security status of more than 10 million people in Pakistan. Around one-third of the farmers reported a decline in income (ADB, 2020). Another one fifth of farming households in Punjab, a province of 110 million people, reported that at least one employed member of household had returned home from urban areas (ADB, 2020) due to closing of markets and losing jobs.

While the impact of COVID-19 on Afghanistan's agriculture sector is limited compared to Pakistan, it may exacerbate the already severe food insecurity in the country. A recent Integrated Food Security Phase Classification (IPC) analysis, together with a survey conducted by the Food and Agriculture Organization of the United Nations (FAO) in collaboration with Ministry of Agriculture, Irrigation and Livestock (MAIL) of Afghanistan, indicate that compared to August–October 2019, the total number of people projected to be in emergency phase has increased from 2.4 to 3.3 million in May 2020, an increase of nearly 1 million (FAO and United Nations, 2020).

The impact of COVID-19 may be mild on harvest of crops as lockdowns were barely enforced in rural areas, while relatively strict movement restriction in urban areas may result in loss of income leading to urban food insecurity. Daily wage earners, small businesses, and populations dependent on remittances are expected to face higher food insecurity. Importantly, the impact of the pandemic may persist and inflate because of significant processing impact on agriculture and dairy products. According to FAO/MAIL *assessment for May-Decmber2020, "more than 50 percent of millers and processing units relating to cereals (50 percent), fruits (57 percent), vegetables (70 percent), and dairy (97 percent) were reported to be highly impacted and operating at reduced capacity or closed* (FAO and United Nations, 2020).

Sri Lanka declared lockdown on March 19, 2020. Not only is its dependence on agriculture lower compared to Pakistan and Afghanistan, but also the agriculture sector was less affected by the pandemic due to less integration in the supply chain. However, access to food and other dairy products became an issue for Sri Lanka as well due to the disruption of distribution channels. Some of the SMEs in the agriculture sector that were unable to continue business also had trouble with their liabilities. Non-performing loan ratios rose to around 4.5% as of 30th April 2020, of which 25% is attributed to the SME sector (Sri Lanka, Ministry of Finance, 2020). Overall, the agriculture sector is predicted to achieve a growth of 1% in year 2020.

1.1.2. Tourism sector

South Asia is highly dependent on travel and tourism. The sector contributed $234 billion, 6.6% of the region's GDP in 2019, according to World Travel & Tourism Council (WTTC) (IMF, 2020). It generated approximately 47.7 million jobs in 2019 (World Bank, 2020). COVID-19 is likely to affect these jobs. The adversely hit are jobs held by women and vulnerable communities working in the informal sector. Overall, the pandemic may wipe out more than $50 billion from GDP of the region from the travel and tourism sector alone.

Recent estimates of World Bank (WB) show that Pakistan has lower dependence on tourism. The sector contributed 5.9% to GDP and 6.2% to total employment in 2019 (World Bank, 2020). The estimates further show that the pandemic has imposed a tourism sector loss of $3.64 billion on Pakistan's GDP and has put 880,000 jobs at risk in the sector (World Bank, 2020). The total number of jobs generated by the tourism and travel sector in Pakistan is estimated at around 2 million.

The suspension of flight operations globally along with lockdown affected international and domestic tourism. SMEs operating in the tourism and transportation sectors have been significantly affected by the pandemic. Hoteling industry reported that bookings dropped from 90% to 40% in January-March 2020 (NTCB, 2020) due to international travel suspensions because of the pandemic.

Sri Lanka has high dependence on tourism which contributed 10.3% and 11% to GDP and employment in 2019 (World Bank, 2020). The World Bank estimates show that the pandemic can cause $1.99 billion potential loss to GDP from the tourism sector and put 200,000 jobs at risk. By the end of March, accommodation occupancy rates dropped to 15-20% in Colombo and nearly zero for hotels outside of Colombo. A prolonged closure of borders will severely impact the sector and the high number of SMEs that operate in it, especially in Sri Lanka that had just recently started to recover from the impact of the April 2019 Easter Sunday attacks.

Almost no tourism exists in Afghanistan currently due to the prolonged war on terror and internal armed conflicts. The Afghan government, however, is trying to rebuild its war-torn infrastructure to re-establish tourism (Afghanistan, Ministry of Finance, 2020).

Given poor health and safety protocols for travelers, absence of a rapid test and trace strategy, lower public & private sector collaboration and limited government support for the sector in terms of fiscal and liquidity incentives and measures to protect workers, the countries under analysis are more likely to face a worst-case scenario in 2020. They may end up with a 63% and 64% loss in jobs and 64% loss of GDP from the sector compared to 2019 (WTTC, 2020).[3]

1.1.3. Education sector

Educational institutes were one of the first to close when the pandemic broke out. UNESCO's COVID-19 Educational Disruption and Response estimates that Pakistan has 46.8 million affected learners due to COVID-19. Around 1.9 million of them are enrolled at the tertiary level. According to a World Bank report (World Bank, 2020), closure of institutions will directly affect youth aged 18 to 24 participating in higher education. Children in the poorest 20% of the households will face the greatest difficulty in accessing higher education (World Bank, 2020). Most importantly, *"school closures make girls and young women more vulnerable to child marriage, early pregnancy, and gender-based violence – all of which decrease their likelihood of continuing their education"*[4] Overall, the negative outcomes of prolonged closures are especially precarious for girls, most at risk of

3 This worst-case scenario is adopted from report of WTTC for Asia-Pacific which shows that Tourism and Travel Sector may lose 63% of jobs in the sector and 64% of GDP from the sector in 2020 compared 2019 under worst case scenario. For details of baseline and best-case scenario please refer to WTTC (2020).

4 Global Partnership for Education (GPE), "Opinion: Don't let girls' education be another casualty of the coronavirus".

permanently dropping out (United Nations, 2020).[5]

Governments and private educational institutions have tried to deliver this service online but the lack of preparedness from educational institutions such as no previous history of application of Learning Management Systems (LMS) combined with lack of Internet connectivity in rural and remote areas makes this task near to impossible to accomplish in the near future. According to LIRNEasia's latest report only 34% of Sri Lankan households with children have access to the Internet that can be used to access e-learning (Amarasinghe, 2020). Even lower, Pakistan's Internet access is 17%, less than half of Sri Lanka's. This means that most students were not able to access e-learning during the crisis. Unfortunately, no such statistics were available for Afghanistan.

Schools in Sri Lanka were reopened on 6 July 2020 but have closed again as a precautionary measure following a spike in COVID-19 cases. Schools nationwide have been shut down again from July 13 to July 17(Hua, 2020). In Pakistan and Afghanistan schools are to remain closed till September and will open depending on the situation. Furthermore, closure of educational institutions has affected children from poorer households' access to mid-day meals, impacting their nutrition which could further adversely impact stunting rates.

1.1.4. Health sector

According to the World Bank[6] Sri Lank has 3.35 hospital beds per 1000 people, compared to 0.60 and 0.47 for Pakistan and Afghanistan, respectively. In Pakistan and Afghanistan, isolated beds and wards, Intensive Care Units (ICUs) and ventilators were in limited quantity even before the pandemic. When the pandemic arrived, which was later than most countries, authorities were scrambling to secure Personal Protective Equipment (PPEs)and testing kits that were already in short supply in the global market.

As soon as cases surged, there were reports of hospitals turning away patients due to shortages of beds. Moreover, the weak health care infrastructure in Pakistan and Afghanistan at the local level and shortages in PPE had also affected the morale of doctors. Inequitable access to health care is also a problem that plagues Pakistan and Afghanistan along with the decision to either invest in economic recovery or health infrastructure.

The digital divide has also become more apparent in Pakistan and Afghanistan due to the closure of outpatient departments in hospitals. A growing trend in tele-medicine is the only option for the masses to get in touch with a healthcare professional. Around 57% of Pakistanis own a mobile phone as compared to 78% in Sri Lanka[7]. A Gallup survey in 2015 states that 6 in 10 adults (62.2%) in Afghanistan have access to a mobile phone while 18.9% stated they have access to a mobile phone through someone close to them.[8]

5 United Nations (2020), Education during COVID-19 and beyond.

6 Available from https://databank.worldbank.org/source/world-development-indicators.

7 Data retrieved from http://afteraccess.net/wp-content/uploads/After-Access-Website-layout-r1.pdf.

8 Data retrieved from www.usagm.gov/wp-content/uploads/2015/01/Afghanistan-research-brief.pdf.

The pandemic has pronounced inequities pertaining to gender equality and inequitable access to health care and broadband which impacts on the health sector. Sharing of good practices should be encouraged within the region that could help narrow these gaps soon. Furthermore, countries like Afghanistan that are dependent on international assistance could be provided with assistance in-kind through the provision of mobile testing labs particularly at border areas and other technical and medical expertise.

1.1.5. Transportation Sector

The transportation sector directly and indirectly impacts other sectors and has been specifically hard hit by COVID-19 due to lockdowns and restrictions in mobility at the local, national, regional, and global level. The SMEDA survey states that 38% enterprises faced transportation disruptions in their supply chains. The transportation sector contributes to 12.89% of Pakistan's GDP and absorbs 5.7% of the national labour force. The civil aviation authority (CAA) has faced losses of up to PKR 19 billion during the time air travel was suspended. This is almost 17.4% of total revenue for the CAA for FY 2018-19 (CAA, 2019).

According to the International Air Transport Association (IATA) there is a 52% decrease in passenger demand as compared to last year in Pakistan. Revenue losses are expected to be around USD $1.83 billion and 259,400 jobs will be impacted. For Sri Lanka, the YoY decrease in passenger demand is 58%, revenue losses will approximately be about $0.715 billion with 408,200 to be affected.[9] The situation with Afghan airlines is no different either with most of them on the brink of collapse. Afghan airlines have recorded a loss of more than $20 million since March 2020 (Gandhara, 2020). Airlines are also a major source of employment for women in Afghanistan and will be affected by the pandemic.

A significant number of the refugee population is employed in the informal transport sector to survive. These people possess limited coping mechanisms and are the most impacted by lockdown measures (OCHA, 2020). Similarly, Sri Lanka has 1.2 million registered three-wheelers along with other vehicles registered with rideshare apps that people rely on for their daily incomes (KPMG, 2020). The transportation sector is primarily demand-constrained and points towards the fact that households reduced their expenditures on transport either directly or indirectly through the production network.

9 Data retrieved from www.iata.org/en/pressroom/pr/2020-04-24-01/.

It is difficult to differentiate between the reductions in economic activity that are unavoidable and avoidable. However, this problem needs to be solved to create effective public policy. Furthermore, it is important to manage aggregate demand to reduce unemployment in demand-constrained sectors. Research suggests untargeted aggregate demand stabilization would increase GDP by only half than in a typical recession that is driven entirely by a reduction in aggregate demand (Baqaee & Farhi, 2020). Due to the sectoral nature of the pandemic, it is important that spending is stimulated in demand-constrained sectors through targeted policies for effective results.

Table 1: Covid-19 and major vulnerable groups[a]

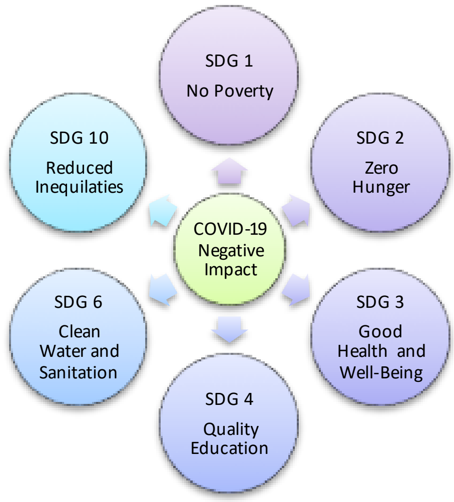
Country	Major vulnerable groups
Pakistan	Households working in agriculture and livestock (50%); Wage labour, including skilled/unskilled non-agricultural laborer's and forestry (22%) of total households); Under-five children at risk of missing out on immunization (17 million children for Pakistan); malnourished and stunted children (12 million); and pregnant women unable to access antenatal and postnatal care (4.7 million); Already food insecure population (the 40 million) and additional 2.5 million people food insecure because of Covid-19.
Afghanistan	Households working in agriculture and livestock (68%); (FAO-UN, 2020); employment with informal work arrangements and insecure tenure (75%); Population below poverty line (55%); already food insecure population (55%), additional population which become food insecure because of Covid-19 (13%); Returnees and Internally Displaced Population (15%).
Sri Lanka	Households engaged in irregular, non-skilled labor activities (42.8%); Households working in Tourism (10%); households working in agriculture sector (24%)

Note: [a] This is not exhaustive lists and identifies some major vulnerable groups.

1.1.6. Vulnerable groups

The COVID-19 crisis has created major challenges for the vulnerable groups. The impact of the pandemic varies in nature and severity across society. The venerable groups are perpetually at major risk. COVID-19 has inflated these vulnerabilities. A review of the relevant literature identifies the major vulnerable groups for each country as given in table 1.

Figure 2: SDGs adversely affected by the pandemic



Vulnerability of the elderly, persons with disabilities and migrant workers is also expected to increase. According to UNESCAP research, persons with disabilities are likely to face higher poverty rates of approximately 20.6% and their probability of securing employment is 2 to 6 times less (UNESCAP, 2020). Moreover, disruptions in both basic and essential lifesaving care and lack of access to social protection particularly in Pakistan and Afghanistan places persons with disabilities at high risk. Furthermore, one-third of Afghanistan's population may experience acute food shortages in Q2 and Q3 of 2020 (Ben, 2020).

In the case of the elderly, pre-existing health complications and more susceptibility to adverse socioeconomic impacts poses a risk especially for ageing populations such as that of Sri Lanka. Women that are facing the brunt of the crisis either by serving at the frontlines in health care or through increased household errands are also at risk of increased domestic violence and abuse. Women may also find it difficult to get access to continuous maternal or reproductive healthcare and are also at risk of losing their livelihoods (e.g. women agriculture workers and women led SMEs).

Overall, the pandemic may wipeout the progress made so far on SDGs agenda. Some of these are highlighted in figure 2. Moreover, impact though the financial channels such as increased short-term capital outflows, plummeting commodity prices, travel and tourism and migrant workers' job losses are all likely to adversely affect progress on SDGs 8 and 9.

Policy responses to COVID-19 have aggregate effects on economies. According to the Sustainable Development Report 2020 (Sachs, 2020) COVID-19 will adversely impact most of the SDGs.

1.2. Economic stress added by covid-19

The pandemic has stressed global economies. It has affected economic growth negatively beyond anything experienced in nearly the last hundred years (Jackson et al. 2020). Latest estimates show that the pandemic could trim global economic growth by 3.0% to 6.0% in 2020. A partial recovery in 2021 is expected assuming there is not a second wave of infections. According to a World Bank study, GDP in South Asia may contract by 2.7 percent in 2020.

COVID-19 caused Pakistan's GDP growth rate to fall to -0.4% against the pre-COVID-19 estimates of 2.2% (table 2), a contraction of 2.6%. At the rate of 2.2% growth rate, Pakistan's nominal GDP in 2019 was expected to increase to $321.5 billion from 314.6billion in 2018. This however turned to $284 billion in 2019, a loss of more than $30 billion. The adverse impact of COVID-19 on real GDP growth of Afghanistan and Sri Lanka was even stronger and GDP contracted by 5.9% and 8.6% respectively in 2019 against the estimates of growth rates of 2.4% and 3.4% respectively. The larger impact for Sri Lanka could be because of its higher share of vulnerable trade, 8.8% of its GDP, compared to 0.77% and 0.76% vulnerable trade for Afghanistan and Pakistan respectively (UNESCAP,2020). Additionally, smaller GDP size of these countries compared to Pakistan may also lead to higher percentages.

The pandemic widened fiscal deficits. The economies lost revenue collections on the one hand while expenditure grew exponentially on the other hand. Fiscal deficit for Pakistan widened by two percentage points, increasing from -7.2% to -9.2% of GDP. Sri Lanka registered the highest impact of COVID-19 and fiscal deficit increased from -5.3% to -9.45% of GDP (table 2). Pakistan witnessed the highest impact on inflation and post-COVID inflation was estimated to be 10.8% compared to estimates of 6.8% before the pandemic hit the economy (table 2).

Afghanistan and Sri Lanka are forecast to have economic growth rates of more than 3.9% in FY2021, compared to Pakistan's -1.5% (table 3).

Table 2: Macroeconomic indicators pre-COVID-19 and post-COVID-19 (2020)

Indicators	Pakistan		Afghanistan		Sri Lanka	
	Pre COVID-19 estimates 2019	Post COVID-19 baseline estimates 2019	Pre COVID-19 estimates 2019	Post COVID-19 baseline estimates 2019	Pre COVID-19 estimates 2019	Post COVID-19 baseline estimates 2019
Real GDP Growth	2.2	-0.4	2.4	-3.5	3.4	-5.2
Fiscal deficit % of GDP	-7.2	-9.2	-3.5	-4	-5.3	-9.45
Inflation	6.8	10.8	3.3	5	3.2	5.0
Employment	2.6	1.0	3.5	-1.3	0.4	-5.9
General government net lending/borrowing	-7.4	-8.6	-0.3	-2.5	-6.4	-8.9
General government gross debt (%GDP)	78.6	79.1	7.7	10.3	82.7	90.7

Source: UNESCAP Excel model to assess the impact of COVID-19.
Note: Fiscal deficit % of GDP retrieved from respective IMF staff reports.

In addition to a base effect, Pakistan's slower rebound can be partially attributed to policies under Extended Fund Facility (EFF) of IMF for Pakistan10. For example, Pakistan maintained the tax rate in the first post pandemic budget of FY2020-21. While this was celebrated as a success, these taxes were originally meant to slow down the economy in 2018-19 to manage a balance of payments crisis. It is important to note that Pakistan's economic growth rate in 2020-21 will be lower than its

10 On 3 July 2019, the Executive Board of the International Monetary Fund (IMF) approved a 39-month extended arrangement under the Extended Fund Facility (EFF) for Pakistan for an amount of SDR 4,268 million (about US$6 billion or 210 percent of quota) to support the authorities' economic reform program.

population growth rate, indicating another year of declining GDP per capita.

Fiscal deficits for the three countries are expected to increase in FY2021 (table 3). Lower government revenue may inflate the deficit further. Sri Lanka's remittances, which account for 7.8% of GDP, are expected to decline substantially as 70% of these are earned in the hard-hit areas of West Asia and Europe (Sri Lanka-Ministry of Finance, 2020).

Pakistan's remittances increased by almost 6% in FY 2019-20 as compared to FY 2018-19 against the World Bank's forecast of decline of 23% (Staff Report, 2020). Along with other factors, return migrants, who are people returning from abroad particularly from Gulf region, are sending all their earnings back to Pakistan. Another major reason may be the return of Hajj Fees from Saudi Arabia as no pilgrims could perform the Hajj due to COVID-19.

Afghanistan seems to be in serious trouble and may face the most severe constraints to financing economic recovery. At least half of Afghanistan's budget is covered by foreign aid (Strand, 2017).

The United States Scretary of State, Mike Pompeo, during his visit to Kabul warned of a $1 billion aid cut from the annual assistance package of $4.5 billion in 2021 (Pamuk et al., 2020). The United States' share in Afghanistan's total net Official Development Assistance (ODA) accounted for 28.24% in 2018 (OECD, 2018). It is also noteworthy that Afghanistan's $11 billion public expenditure is accounted for by $2.5 billion in revenues while the gap is financed by grants (Khan, 2020).

Table 3: Macroeconomic projections pre-COVID and post-COVID for 2021

Indicators	Pakistan		Afghanistan		Sri Lanka	
	Pre COVID-19 estimates 2020-21	Post COVID-19 baseline estimates 2020-21	Pre COVID-19 estimates 2020-21	Post COVID-19 baseline estimates 2020-21	Pre COVID-19 estimates 2020-21	Post COVID-19 baseline estimates 2021
Real GDP Growth	4.3	-1.5	3.8	3.9	4.1	5.2
Fiscal deficit % of GDP	-5.7	-6.47	-1.4	-2.01	N/A	-8.29
Inflation	5.8	4.1	3.8	2.8	3.5	3.0
Employment	2.5	0.4	3.5	3.5	0.5	1.0
General government net lending/borrowing	-5.5	-6.3	-0.2	-2.1	-5.4	-7.1
General government gross debt	76.1	82.9	7.7	12.1	80.7	89.3

Source: UNESCAP Excel model to assess the impact of COVID-19.
Note: Fiscal deficit % of GDP retrieved from respective IMF staff reports.

Limited fiscal space for domestic resources is likely to push the countries to go for public borrowing. Debt-to-GDP ratios are likely to inflate in 2020 and 2021. The debt-to-GDP ratio for Sri Lanka is expected to increase from pre-COVID-19 estimates of 80.7% to 89.3% in FY2021, according to Sri Lanka's Ministry of Finance (table 3). A similar trend in debt-to-GDP ratio for Pakistan and Afghanistan is expected.

A shrinking fiscal space will negatively affect financing of all the SDGs and adversely impact the spheres of poverty, inequality, social, economic, and environmental goals. Sustained financing to mitigate the effects of COVID-19 is bound to add to mounting fiscal deficits of these countries. In this backdrop, SDG 1 poses a significant risk as large segments of the population may backslide into poverty due to COVID-19. Hence, the importance of international community building upon SDG 17.4 to create fiscal space is now more important than ever, as countries such as Sri Lanka that are debt distressed risk losing the progress made towards the SDGs.

Constrained fiscal space affects developmental expenditures disproportionally, as the current expenditures are hard to cut down. Lower fiscal space in developing countries means rationalizing the expenditures. In Pakistan, the burden mainly falls on health, education, and social protection which may compromise the progress on many of the SDGs. Stimulus packages will lead to increased public borrowing. While using debt to finance spending in recession is in line with global practice, countries need to be careful about financial sustainability. The global community must help these countries in attaining long-term debt sustainability (SDG 17.4) through restructuring the external debt.

The COVID-19 crisis has led to countries revisiting their debt management strategies and prompted debt relief from the G20. The Paris Club has already provided a debt relief deferment of $1.1 billion under G20 debt relief. The total relief amounts to suspension of $1.8 billion, the principal and interest payment payable by Pakistan to 11 countries during May this year to June next year. Afghanistan has also received debt servicing relief under IMF's package for 25 countries. According to the World Bank and IMF, Afghanistan has received successful debt cancellation of $1.6 billion. Unfortunately, Sri Lanka, the most debt stressed of the three countries, is yet to get any debt relief.

1.3. Fiscal policy responses[11]

For a quick comparison across the countries, we decompose the initial responses to the pandemic into four broader categories i) healthcare spending, ii) Firm liquidity supports, iii) Employment retainment measures and iv) Transfers targeting lower income households (tables 4a,4b,4c). The rest of the measures are included in "other".

1.4. Brief assessment of the fiscal stimulus

With spending of 2% of its GDP on the health sector Pakistan has a poor healthcare system. The virus imposed further stress. The pandemic exposed the lower efficiency of the system in managing the infectious decease. A bulk of PKR144 billion, was allocated to import required equipment. The health system failed to communicate effectively the risks associated with COVID-19 which led to mass-scale apathy and indifference to the pandemic. Policy coordination fared very poorly. Different messages kept coming from different stakeholders, mainly from federal and provincial governments.

11 Responses are retrieved from www.imf.org/en/Topics/imf-and-Covid19/Policy-Responses-to-COVID-19, up to date as of 19 August 2020. This report focuses on fiscal policy responses. However, the information on monetary policy including regulatory measures can also be traced from this website.

While the measures helped improve hospital beds, quarantine facilities and procurement of ICU equipment ventilators, it largely failed to prepare staff to deal with the pandemic. The staff protested across the country about insufficient provision of protection gear and other accessories. The infection rate amongst medical staff was significantly higher than other countries. Contact tracing, laboratory testing, and isolation remained the weakest component at the critical times - March to June 2020. Management remained weak. Hospitals faced shortages of critical equipment, such as ventilators and oxygen, at the very early stage of the spread of infections.

Table 4a: Pakistan's fiscal responses

Type of socioeconomic impact	Fiscal response
Healthcare spending	- Elimination of import duties on emergency health equipment - Support for health and food supplies=PKR 15 billion - Transfer to NDMA for purchase of COVID-19 related equipment= PKR 25 billion - Support for health and food supplies = PKR 15 billion - 'COVID-19 Responsive and Other Natural Calamities Control Program' = PKR 70 billion **Total= PKR 144 billion**
Firm liquidity supports	- Accelerated tax refunds to the export industry=PKR 100 billion (65% disbursed) - Financial support to SMEs and the agriculture sector (in the form of power bill deferment, bank lending, as well as subsidies and tax incentives) = PKR 100 billion - Financial support to utility stores=PKR 50 billion **Total: 250 billion**
Employment retainment measures	Provision of tax incentives to the construction sector
Transfers targeting lower income households	- Cash transfers to 6.2 million daily wage workers=PKR 200 billion - Cash transfers to more than 12 million low-income families (fully executed) = PKR 150 billion **Total: PKR 350 billion**
Other	- Wheat Procurement = PKR 288 billion A reduction in regulated fuel prices with a benefit for end consumers estimated at = PKR 70 billion - Electricity bill payments relief = PKR 110 billion - An emergency contingency fund = PKR 100 billion **Total: PKR 568 billion**

Table 4b: Afghanistan's fiscal responses

Table 4c: Sri Lanka's fiscal responses

Type of	How the fiscal package to date addresses the impact
Type of socioeconomic impact	How the fiscal package to date addresses the impact
Healthcare spending	- Containment measures = 0.1% of GDP
Firm liquidity supports	- 2020 H1 payment deadlines for income tax, VAT and certain other taxes were extended until end-Dec.
Employment retainment measures	- Income tax arrears of SMEs have been partially waived off, more relaxed payment terms have been approved and legal actions against non-payers have been frozen.
Transfers targeting lower income households	- The President has announced cash payments totaling around 0.25 percent of GDP for vulnerable groups.
Other	- SAARC COVID-19 Emergency Fund = USD $5 million (0.01% of GDP)
	residence in Kabul for two months and paid utility bills of the past two months for 50 percent of households in Kabul. - Transfer to provinces to finance COVID-19 response: Af 2.3 billion - Package to support agriculture: Af 5.9 billion - Short-term jobs: Af 1.0 billion

Going forward, the spending on health must be doubled (4% of GDP). In addition to improving basic healthcare such as construction of health facilities in the remote areas, the country needs to invest in laboratory work, surveillance, risk communication, and monitoring and coordination to better deal with a crisis like COVID-19.

Similarly, measures to provide liquidity to SMEs did not go to those most in need. SMEs engaged in the informal sector continue to suffer liquidity issues and substantially laid off workers. According to a survey of SMEs (Karandaz, 2020), more than half of SMEs in the country (58%) had laid off employees by April 2020. Around 47% of SMEs cut the salaries of employees. More than half of the SMEs in the textile sector reported laying of half of part-time (52.4%) and daily wage (61.9%) workers. These numbers show that the measures to avoid layoffs were largely ineffective.

On the one hand, the commercial banks did not effectively implement the measures to provide liquidity to SMEs due to higher risk of defaults. On the other hand, the SMEs working in the informal sector feared documentation and future taxation and avoided applying for the concessionary loans and other available support measures. This led to a low disbursement. The credit mainly went to larger firms. Going forward, Pakistan needs to focus on sustainable recovery of the SME sector. Now when the lockdown is lifted, policies must be put in place to integrate SMEs into supply chains and stimulate new demand and investment.

Finally, social protection support, both cash and in-kind, suffered setbacks. It did not reach in a timely manner. The lockdown was imposed on 24 March in a hurry, the day after federal government had dismissed the need for lockdown. This resulted in many in the population suffering from hunger and health issues. Second, there were no arrangements to reach the bottom section of the poor and marginalized. The poor suffered badly, particularly in the first three to four weeks of the lockdown. They lost their jobs and help was not reaching them. This also affected the implementation of lockdown. The situation however improved over the later stages of lockdown.

Inability of social and economic measures to reach the most deprived may exacerbate deprivation and strengthen already rampant inequalities. Developing countries in their response to COVID-19 face limitations pertaining to data availability and information management systems. The vulnerable groups, poor, living in rural areas, transgenders and other, lacked access to support measures. Moreover, lack of information management systems resulted in delayed relaying of information of shortages in PPEs and food supplies between local and federal tiers of government further compounding problems and at occasion causing public unrest. An unequal response will result in a direct negative impact to SDG 10.

Also, the support measures overlooked the vulnerable non-poor. Initial cash and in-kind disbursements were limited to the extremely poor. The cash and in-kind disbursements mostly ignored “social distancing” and the people were in large queues to collect the help.

Largely owing to its better healthcare system, Sri Lanka fared well in responding to the pandemic. The healthcare expenditure was comparable to Pakistan, up to 0.1% of GDP. However, the presence of a robust healthcare system enabled Sri Lanka to focus on surveillance, quarantine, and other containment measures. In addition to cash transfers, Sri Lanka effectively set price ceilings during the pandemic. In contrast, prices of essential goods in Pakistan continued to rise.

A lower poverty rate, 4.1% population living below the national poverty line in 2016, and robust data helped Sri Lanka design effective interventions during the pandemic. However, “*MSMEs, accounting for 99.8% of enterprises and employing 27% of the total labour force, are worst-hit with less reserves and limited access to relief and formal-sector credit”* (United Nations, 2020).

Compared to Pakistan and Sri Lanka, Afghanistan has the most constrained response to the pandemic. Prolonged conflict, tribal wars and poor social and economic systems limits the capacity to respond to the pandemic. Suboptimal policy responses coupled with poor implementation have impacted the efficacy of the responses to the pandemic. The supporting measures were not available to many hard-to-reach areas leaving the vulnerable suffering in the crisis. The pandemic inflated the already existing severe vulnerabilities. Overall, the size of the support package prevented it having any effective outcome.

The stimulus has implications for SDGs agenda. Policy measures undertaken so far to mitigate COVID-19 can positively affect many of the SDGs target. They have potentially contributed towards many of the SDGs targets, those under SDGs 1, 2, 3, 5, 8, 9, 10 and 17. Some of the examples are provided in figure 3.

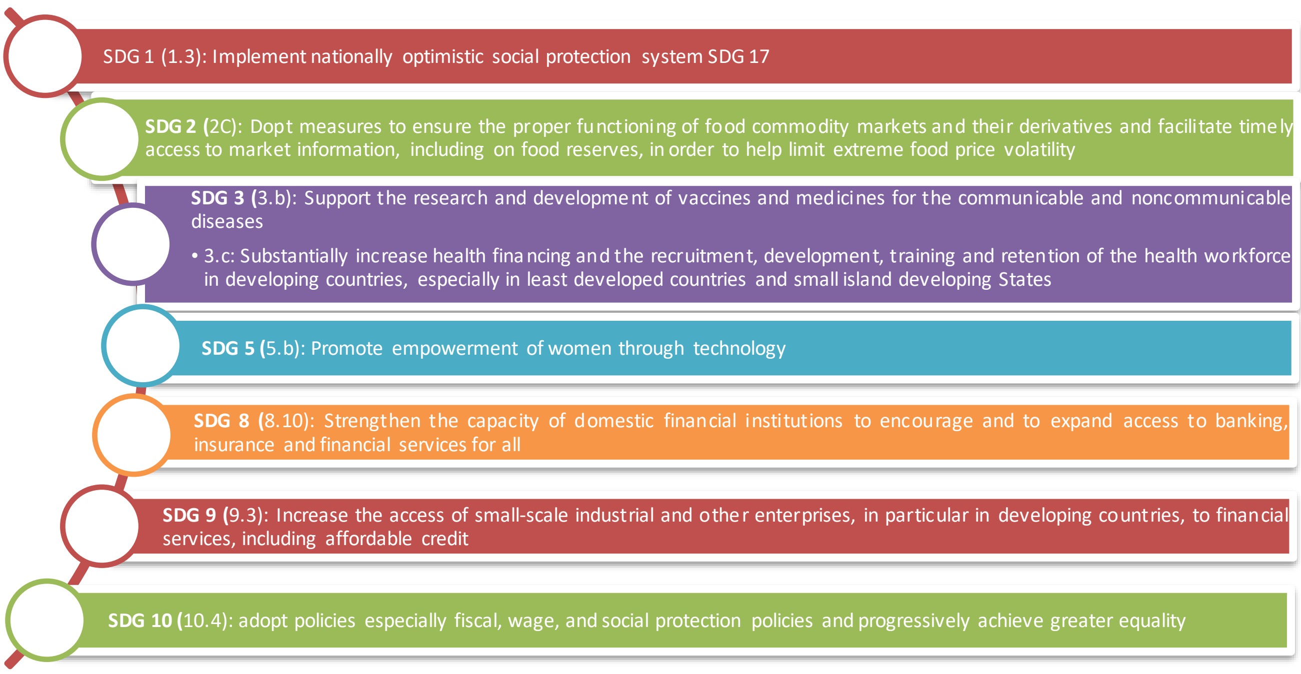
Finally, stimulus packages are not geared towards green measures. Environment-unfriendly activities have implications for SDGs 1, 8 and 12. It is important that stimulus measures are geared towards green measures including but not limited to transition to a green energy, cleaner transport and restricting approvals/financing of fossil fuel-based projects. Clearly, sustainable poverty reduction cannot be realized without accounting for environmental sustainability (Antoniades, 2019).

The crisis presents an opportunity, especially for developing economies to shift towards more sustainable and equitable growth patters by investing in new green technologies, closing the digital divide, and expanded social safety nets. In other words, it offers opportunity for "*building back better*".

I. Central Banks have played a key role in mitigating the effects of the pandemic. They can use the crisis to a) promote and scale up green banking providing preferential credit and other support to projects which are socially, economically, and environmentally responsible, b) provide special incentives for development of green bond markets can encourage private sector investment in SDGs.

II. Governments can provide targeted tax incentives such as preferential corporate tax treatments, reductions in withholding tax, increased investment limits for foreign investors and legitimizing social enterprises. Authorities also need to ensure that these incentives do not entail extra reporting or involvement of bureaucracy.

Figure 3: Impact of stimulus measures on SDGs



III. Taxation policies should not reduce income of the poor. Indirect taxes, particularly GST, adversely affect poverty and inequality. The respective share of indirect taxes must be gradually brought down compared to direct taxes. Extracting revenues from the poor through energy and fuel price hikes is also against the spirit of the SDGs Agenda.

IV. Governments also need to curb unsustainable consumption patterns through advocating for behavioural change. Extensive advocacy campaigns that cultivate an environment of reuse and recycling along with eco-labelling in respective national languages further reinforced by messages on electronic media to help citizens make better and more informed choices.

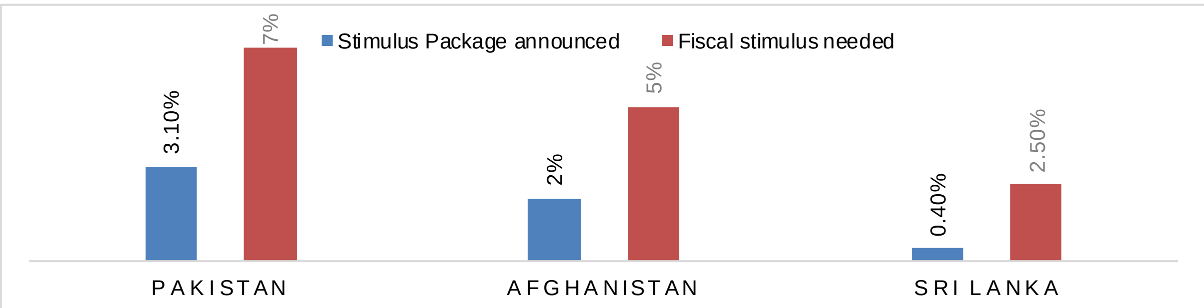
2. Outlook under alternative policy scenarios

According to the UNESCAP-SANEM South Asia CGE Model (hereafter ESCAP CGE model), stimulus packages ranging between 7-14% of GDP are needed in South Asia to mitigate the impacts of COVID-19 and stimulate revival.[12] The ESCAP CGE model estimates that stimulus package equal to 7% of GDP is required to mitigate the socioeconomic impact of the pandemic. The requirement is 5% and 2.5% for Afghanistan and Sri Lanka, respectively.

Figure 4 shows that none of the countries was able to meet the minimum required size of fiscal measures. Pakistan and Afghanistan were able to meet 44.3% and 40% of the required fiscal measures compared to 16% for Sri Lanka. With less than required packages, these countries may have managed the fiscal indicators in the immediate short run, but the economic recovery may be delayed, and economies may experience poor.

To understand and estimate these tradeoffs with greater clarity, we build some scenarios using UNESCAP Excel Based Model (hereafter UNESCAP Excel Model) to design policy responses. The UNESCAP excel model "*produces a snapshot of the socio-economic situation of the Asia-Pacific economies in the time of COVID-19, introduces the channels through which the economies are affected, and allows simple policy scenarios to be studied.*"[13] Following key scenarios are considered:

Figure 4: Current fiscal Stimulus compared to minimum required (%GDP)



Source: UNESCAP (2020).

12 *Note: No estimates recommended by ESCAP for Afghanistan. We assume that Afghanistan may need a stimulus equal to 5% of GDP.*

13 To understand the working of the model, refer to manual of "Assessing the impact of COVID-19 in Asia and the Pacific and designing policy responses An Excel-based Model" /www.unescap.org/sites/default/files/Manual%20Excel%20Sheet%20Model_final_12Sept.pdf.

I. **Baseline Scenario:** The current post COVID-19 stimulus and its distribution across four broader categories remain unchanged.

II. **No Fiscal stimulus Scenario:** Country does not have any fiscal stimulus to mitigate the impact of the COVID-19.

III. **Higher Side Scenario:** Country meets the minimum stimulus size required to mitigate the impact of the COVID-19 as estimated by UNESCAP CGE model (see figure 4).

IV. **Medium Scenario:** Fiscal stimulus higher than baseline sicario but lower than higher side scenario.

Table 5 provides baseline fiscal stimulus as given in the ESCAP excel model. These are the fiscal policy responses from respective countries. It is important to note that we use *revised baseline* of 3.1% of GDP for Pakistan compared to initial stimulus of 2% of GDP given in UNESCAP excel model as Pakistan has increased its fiscal stimulus over the time.

We then discuss the socioeconomic impact of these scenarios on fiscal (fiscal balance and public debt ratio), economic (GDP growth, inflation) and social (employment, poverty) indicators for the respective countries. Furthermore, we explore appropriate policy responses maximizing the outcome for each of the three countries under analysis using UNESCAP Excel model. It must be noted that UNESCAP excel model estimates percentage point change impact of fiscal stimulus on pre-COVID-19 estimates for respective indicators for each country.[14]

Table 5: Post COVID-19 baseline for fiscal stimulus as provided in UNESCAP-excel model

	Pakistan		Sri Lanka		Afghanistan	
	2020	2021	2020	2021	2020	2021
Total fiscal measures (% GDP)	3.1	-2.39	0.4	-0.2	2.0	-1.0
Transfers targeting lower income households (% GDP)	1.00	-0.50	0.2	-0.1	0.7	-0.3
Employment retainment measures (%GDP)	0.50	0.00	0.0	0.0	0.7	-0.3
Firm liquidity supports (%GDP)	0.70	-0.30	0.0	0.0	0.0	0.0
Healthcare spending (%GDP)	0.50	0.00	0.2	-0.1	0.7	-0.3
Other (% GDP)	1.50	-0.50	0.0	0.0	0.0	0.0
Carbon subsidies (%GDP)	0.00	0.00	0.4	0.4	0.0	0.0
Interest rates (basis point change)	-625.00	0.00	-250	0	0	0
Average national lockdown stringency	48.30	9.10	41.8	6.9	50.5	10.8
Average lockdown stringency in trading partners	47.50	8.90	47.4	9.0	41.2	8.4
Oil price	41.80	49.70	41.8	49.7	41.8	49.7
"Other" impacts on GDP growth (percentage point)	3.50	-8.60	-1.2	-2.7	0.4	-2.8

14 See tables 2 and 3 for pre-Covid estimates for Pakistan, Sri Lanka and Afghanistan.

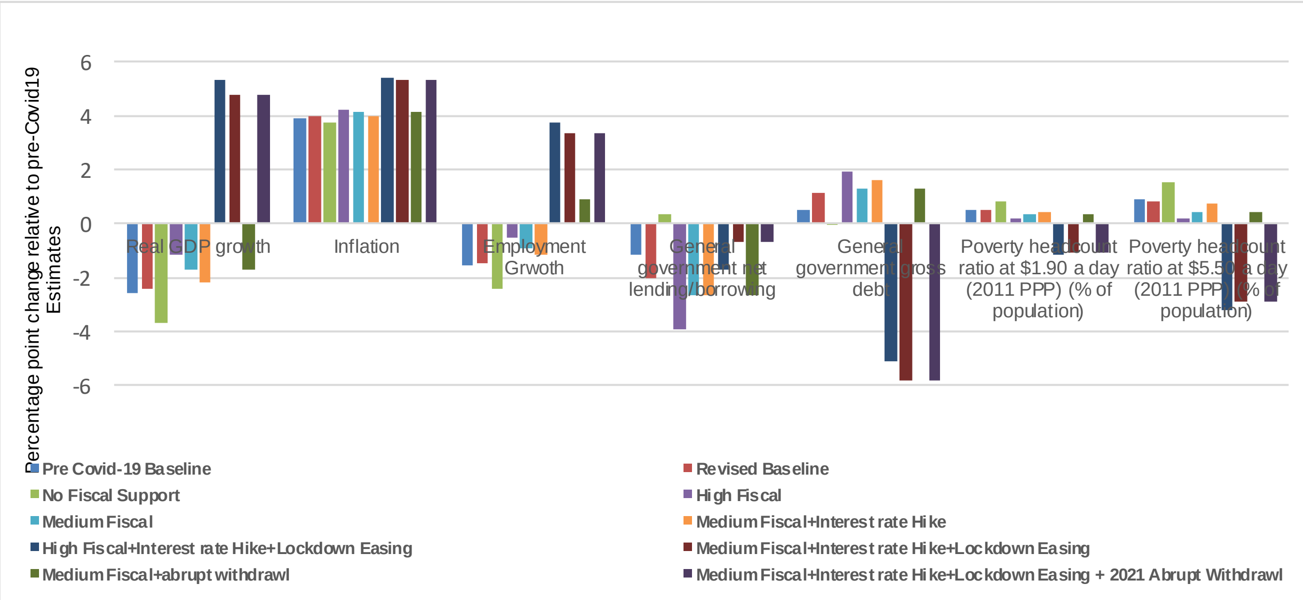
2.1. Pakistan

Figure 5 provides percentage point changes in socioeconomic indicators relative to the pre-COVID-19 baseline under different nature and size of stimulus under different conditions for Pakistan[15]. Pakistan would have faced highest decline in GDP growth in case of no fiscal support (figure 5). The country would have faced 3.7 percentage point decline in pre-COVID-19 GDP growth. The fiscal stimulus of 1.12 trillion reduced the decline to 2.7 percentage point, improvement of 1 percentage point (revised baseline, figure 5). No fiscal support would have reduced employment growth by another one percentage point (-2.4) compared to revised baseline for current fiscal stimulus (-1.5).

It would have increased the poverty head count ratio by 0.8 percentage point and 1.5 percentage point at $ 1.90 and $ 5.50, respectively. Providing stimulus of 1.12 trillion reduced it to 0.5 and 0.8 percentage point (revised baseline), respectively (figure 5). The decline in GDP reduces and the socioeconomic indicators improve as the fiscal stimulus increases from 3.1% of GDP to 5% of GDP (medium scenario) and to 7% of GDP (higher side scenario).

However, one can notice that highest employment increasing and poverty reduction impact of the stimulus is observed when the lockdown was eased indicating that the impact of fiscal stimulus would depend on how well Pakistan can manage the coronavirus. Any second wave, pushing for the mass lockdown, will be wiping out most of the gains from the fiscal stimulus.

Figure 5: Socioeconomic outlook for Pakistan under different fiscal stimulus



15 Following scenario assumption apply for Pakistan:

Higher Side Scenario:

- Total Fiscal Measures as % of GDP= 7% for 2020 decreasing by -3.6% in 2021.
- Cash Transfers (2%), Firms Liquidity (1.5%) others (1.5%); Healthcare spending (2%).
- Interest rate increases 100bps in 2020 and 225 bps in 2021.
- Lockdown stringency in 2020 and 2021=10 & 5 for Pakistan; 15 & 5 in trading partners.

Medium Size Scenario:

- Total Fiscal Measures as % of GDP= 5% for 2020 decreasing by -3.6% in 2021
- Transfers (1%), Firms Liquidity (1%) others (1%); Healthcare spending (2%).
- Interest rate increases 100bps in 2020 and 225 bps in 2021.
- Lockdown stringency in 2020 and 2021=10 & 5 for Pakistan; 15 & 5 in trading partners.

Overall, the significant improvement in Pakistan's socioeconomic indicators is possible if it could spend 7% of its GDP in response to the pandemic. It increases the employment growth and reduces the poverty head count ratio. Percentage point addition to inflation is almost similar for medium (5% of GDP) and high (7% of GDP) fiscal stimulus. Importantly, the percentage point contribution to government debt (% GDP) decreases as fiscal stimulus moves from medium to high denoting the gains from increasing size of economic activity and economy.

It can be noted that increasing the interest rate reduces the gains from all fiscal stimulus. Figure 5 provides example of medium stimulus. The gains, both with and without easing of lockdown, decline immediately as interest rate is increased (figure 5). Pakistan is highly likely to increase the interest rate in the later part of FY2020 and 2021.

State Bank of Pakistan (SBP) did not hold a routine Monetary Policy Committee (MPC) meeting to indicate that any further cut in rate is unlikely. The pandemic is under control and the lockdowns are lifted. Markets are open. So, any pandemic-pushed cuts are over. In its September meeting of MPC, SBP kept the interest rate unchanged and the monetary policy statement hints that SBP may think to increase the rate going forward.

The policy rate may be increased by 100 base points (bps) in FY2020 and another 225 bps in 2021. Two plausible explanations can be offered. One, inflation has started picking up after a slight dip during the pandemic. Monthly CPI inflation in August 2020 over July 2020 stood 0.63% while the inflation rate in July 2020 over June 2020 was 2.50%. This may affect inflation expectations.[16] Second, Pakistan is likely to revert to tight monetary policy under the EFF facility of IMF. This however will compromise the gains from the fiscal stimulus. SBP must ensure provision of liquidity at current interest rate of 7% for a certain period, at least in FY2020.[17]

Finally, the analysis shows that abrupt withdrawal of fiscal stimulus in 2021[18] can compromise the gains (figure 5). The government must ensure that it continues the fiscal stimulus and decreases it gradually. The net gains from the fiscal stimulus depends on the size of multiplier and persistence of the stimulus. The COVID-19 has reduced the multiplier impact as it slowed down the economic activity. The persistence of the fiscal stimulus will be critical to compensate for the cut in multipliers, and consequently to gain stimulus impact. Abrupt withdrawal may cost the socioeconomic gains.

2.2. Sri Lanka

Of the three countries, Sri Lanka has the lowest stimulus, 0.4% of GDP. According to UNESCAP report.[19] Sri Lanka required to allocate 2.5% of GDP to effectively mitigate the socioeconomic impacts of COVID-19. Figure 6 present the impact of a different fiscal stimulus for Sri Lanka under varying

16 Monthly Price Indices, Pakistan Bureau of Statistics.

17 Refer to Javed, (2020) for brief discussion on "Pakistan's monetary policy for now".

18 Ending all the fiscal stimulus immediately at the beginning of FY2021.

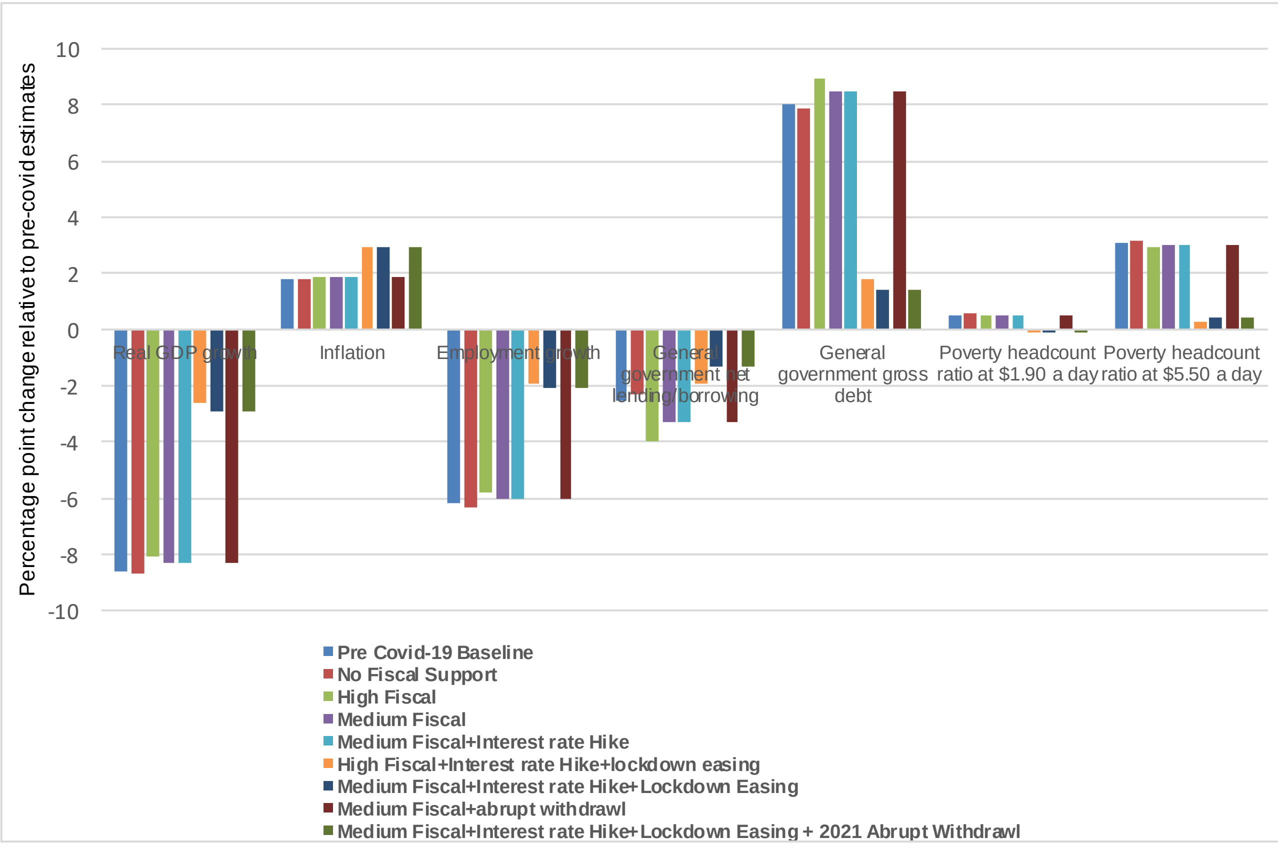
19 COVID-19 and South Asia (2020): National Strategies and Subregional Cooperation for Accelerating Inclusive, Sustainable and Resilient Recovery.

conditions.[20]

For any meaningful gains, Sri Lanka must implement high fiscal stimulus (2% of GDP). The gains however overwhelmingly depend upon easing the lockdown. High fiscal stimulus Coupled with lockdown easing can bring highest percentage point decline in real GDP and employment growth. The percentage point decline drops to -2.6 from -8.7 for no fiscal support and -8.1 for high fiscal stimulus without lockdown easing, despite increase in interest rate.

High fiscal stimulus coupled with rate hike and lockdown easing, reduces the poverty headcount though the decline is negligible. The marginal impact of stimulus on poverty is lower because of already extremely lower levels of poverty in Sri Lanka. Inflation increases slightly. Given that Sri Lanka is expected to increase interest rate going back to its long-term average, gains from fiscal stimulus are substantially reduced (figure 6). Fiscal stimulus of 2% of GDP has the lowest percentage point contribution to public debt (% GDP).

Figure 6: Socioeconomic outlook for Sri Lanka under different fiscal stimulus



20 Following assumptions apply for Sri Lanka.
Higher Side Scenario:
- Total Fiscal Measures as % of GDP= 2.5% for 2020 decreasing by -1.5 in 2021
- Transfers (0.4%, -0.2%), Firms Liquidity (1.5%) others (1.5%); Healthcare spending (0.4%, -.0.2%).
- Interest rate increases 125 bps in 2021.
- Lockdown stringency in 2020 and 2021=15 & 5 for Sri Lanka; 15 & 5 in trading partners.
Medium Scenario:
- Total Fiscal Measures as % of GDP= 1.5% for 2020 decreasing by -1.9 in 2021.
- Transfers (0.4%, -0.2%), Firms Liquidity (0.5%) others (0.5%); Healthcare spending (0.4%, -.0.2%)
- Interest rate increases 125 bps in 2021.
- Lockdown stringency in 2020 and 2021=15 & 7 for Sri Lanka; 15 & 7 in trading partners.

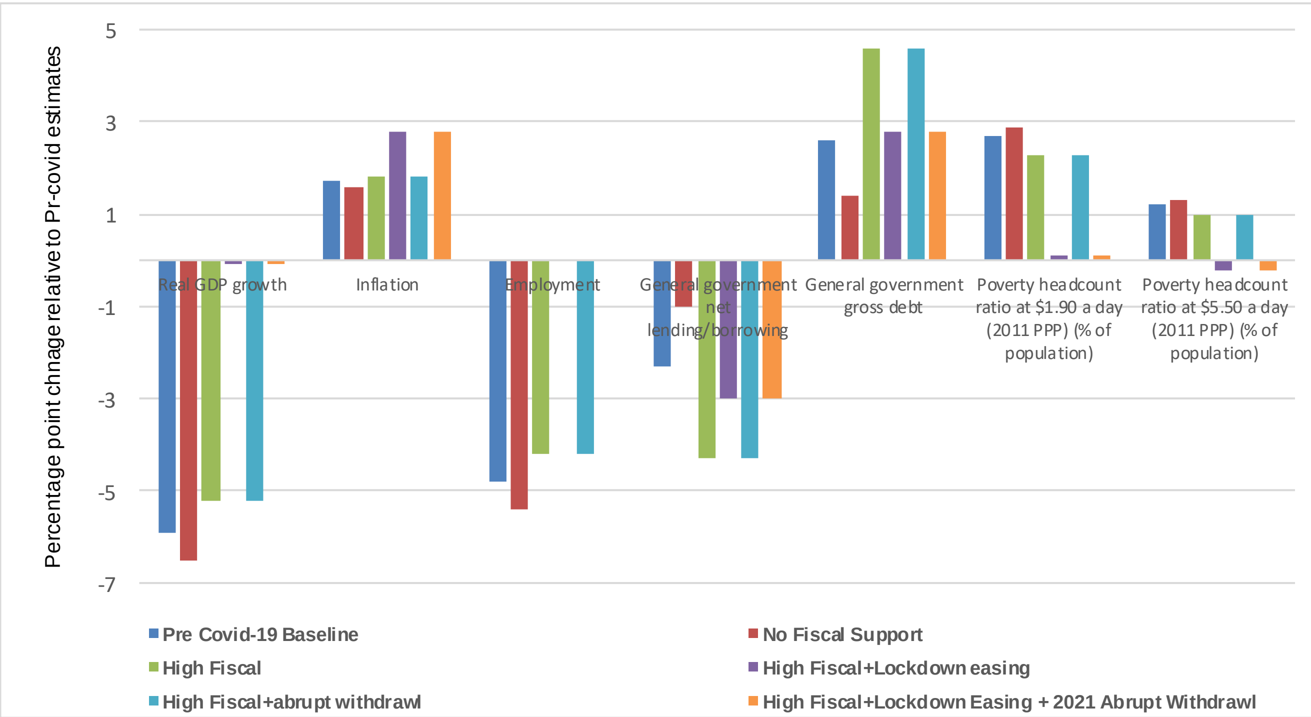
2.3. Afghanistan

Given a lower GDP, around $20 billion, and higher support from the international community, Afghanistan is likely to be able to manage a stimulus package of 5% of GDP from the current 2% of its GDP. The impact on socioeconomic indicators is provided in figure 7.[21]

Like Pakistan and Sri Lanka, Afghanistan would have been worst off if it did not put in place any fiscal stimulus. Contrasting with the other countries, the major focus for Afghanistan is increasing the stimulus package for food security and "other" activities. Substantial gains in socioeconomic indicators are visible. The negative percentage point contribution to GDP growth is lowest when the fiscal stimulus is coupled with lockdown easing (figure 7).

Not only that decline in employment, compared to pre-COVID-19 baseline is lowest, but increasing the fiscal stimulus to 5% reduces the impact of COVID-19 on poverty to minimum. Employment increases. Government debt-to-GDP ratio slightly declines, from 12.14% to 10.58% in 2020 and 12.01% in 2021 from 13.72% of baseline. Poverty decreases slightly in 2020 and 2021 compared to the baseline scenario.

Figure 7: Socioeconomic outlook for Pakistan under different fiscal stimulus



21 Scenario Assumptions:
- Total Fiscal Measures as % of GDP= 5% for 2020 decreasing by -2.5 in 2021.
- Transfers (0.4%), Firms Liquidity (0.5%), employment retainment (0.5); others (2%); Healthcare spending (0.4%).
- Lockdown stringency in 2020 and 2021=10 & 5 for Afghanistan; 15 & 5 in trading partners.

3. Medium-term financing needs and fiscal space

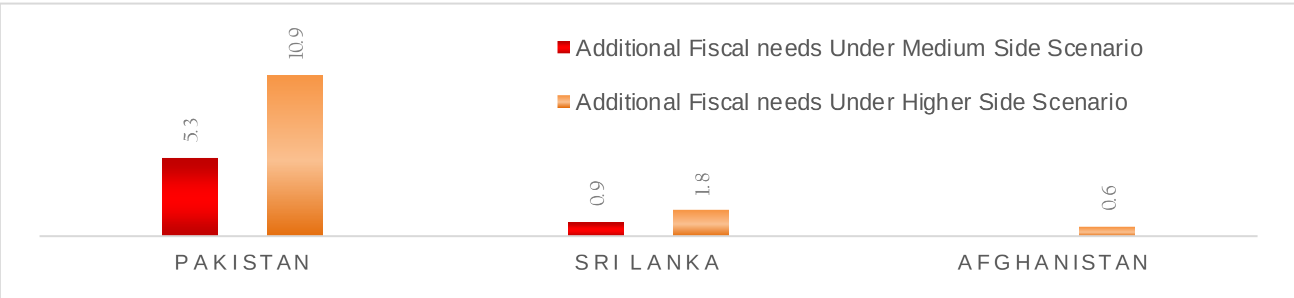
3.1. Financing needs

3.1.1. Increasing the fiscal stimulus

The analysis shows that these countries can better mitigate the impact of the crisis through expansionary fiscal policies. However, this will require additional sources of finance. Figure 8 provides estimates for additional fiscal needs to finance the stimulus under higher side and medium scenarios. Pakistan needs another $5.3 billion to increase the fiscal stimulus from 3.1% to 5% of GDP and $10.9 billion to expand the stimulus to 7% of GDP, the required stimulus as per UNESCAP report titled COVID-19 and South Asia.[22] The additional financing requirements for Sri Lanka to finance medium (1.5% of GDP) and higher side (2.5% of GDP) fiscal stimulus is $0.9 billion and $1.8 billion, respectively. Afghanistan can expand the stimulus to 5% of GDP by spending additional $0.6 billion (figure 8).

Increasing the stimulus package to an optimal size, as discussed above, will not only mitigate the adverse impact of the pandemic but can also lower debt-to-GDP ratios through early economic recovery at a higher real GDP growth rate. This will however require support of the international community through debt relief, development aid and concessional finance. Failing to do this may lead to slower economic recovery, and consequently prolonged recession. This will further deteriorate unemployment, poverty, and other socioeconomic indicators.

Figure 8: Fiscal needs to increase the stimulus (additional to the current fiscal stimulus)



3.1.2. Projected financing requirements before and after COVID-19[23]

The COVID-19 crisis has affected financing for sustainable development in low- and middle-income countries. Table 6 provides the comparisons of financing requirements of Pakistan and Afghanistan. Unfortunately, post COVID-19 estimates of financing requirements are not available for Sri Lanka. Post-COVID-19 financing requirements for Pakistan and Afghanistan both increase as a ratio to GDP

22 COVID-19 and South Asia (2020): National Strategies and Subregional Cooperation for Accelerating Inclusive, Sustainable and Resilient Recovery.

23 Post-Covid estimates for Sri Lanka were not publicly available to date, 15 September 2020.

(table 6).

Though financing requirements for Pakistan and Afghanistan decline gradually after 2020, financing requirements are higher than pre-COVID-19 estimates over the entire period (Table 6). Given lower domestic fiscal space, the COVID-19 crisis will push these countries to seek more debt-creating capital inflows.

3.2. Fiscal space assessment

This section assesses the space to finance the fiscal stimulus required to mitigate the socioeconomic fallout of the pandemic with key focus on revenues from:

3.2.1. Real GDP growth

A negative shock, such as COVID-19 reduce fiscal space by dampening growth.[24] A (s)lower GDP growth implies a shrinking fiscal space in the short run. With reference to this study, the GDP growth is likely to remain negative for Pakistan, Sri Lanka, and Afghanistan into 2020 followed by improvement in 2021 for all the three countries. The lowest rebound in 2021 is observed for Pakistan. The fiscal space will remain lower in 2020 and 20021 compared to the pre-pandemic year, 2019 (figure 9).

To adjust for differences in population and economy size, we also provide data on GDP per capita growth. Pakistan's GDP per capita growth rates exhibit consistent improvements from 2010 onwards (figure 10). However, the decline from 2018-19 could be partially attributed to contractionary fiscal and monetary policy adopted by the country under IMF's Extended Fund Facility (EFF) which aims to control fiscal and current account deficits to manage BOP crisis.

Table 6: Gross financing requirements (% GDP)

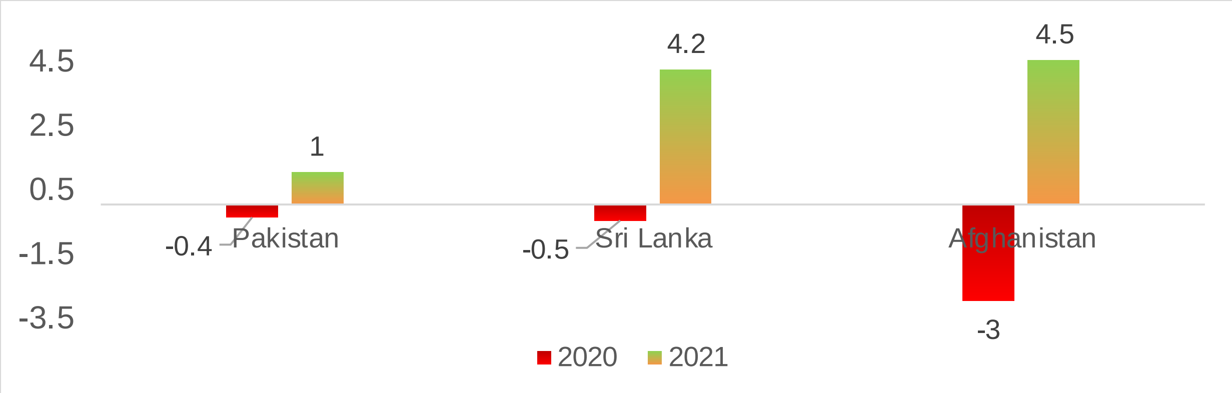
Years	Pakistan		Sri Lanka		Afghanistan	
	Pre COVID-19	Post COVID-19	Pre COVID-19	Post COVID-19	Pre COVID-19	Post COVID-19
2020*	*7.5*	*9.2*	*17.9*	-	*0.5*	*3.6*
2021*	*5.4*	*6.5*	*18.5*	-	*0.2*	*1.6*
2022*	*3.9*	*5*	*18.7*	-	*0.1*	*1.1*
2023*	*2.7*	*4*	*15.4*	-	*0.1*	*0.7*
2024*	*2.5*	*3.9*	*14.8*	-	*0.1*	*0.7*
2025*	-	*3.5*	-	-	-	*0.6*

**** Projected values***

Source: IMF Staff Reports of Selected Countries.
Note: For detailed assessment of gross financing requirements Refer to IMF Country Report No. 20/114 for Pakistan, IMF Country Report No. 19/335 for Sri Lanka and IMF Country Report No. 20/143 for Afghanistan.

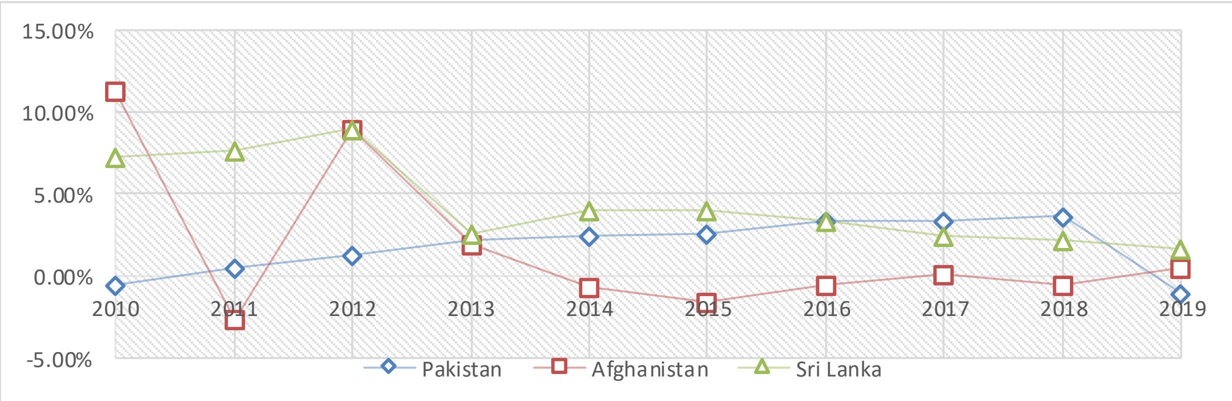
24 See table 2 for the negative impact of Covid-19 on GDP growth of the respective countries.

Figure 9: IMF's estimates of real GDP growth (annual %) (2020 - 2021)



Source: IMF Data Mapper, April 2020. Available from www.imf.org/en/countries#I.
Note: Estimates are from IMF Economic Outlook April 2020 except for Pakistan's revised in June 2020.

Figure 10: GDP per capita growth



Source: World Bank, World Development Indicators.

The GDP growth rate dropped to 1.9% in 2018-19 from 5.48% in 207-18. Further, appreciation of dollar against rupee, conversely depreciation of rupee against dollar, led to decreased size of economy in dollar terms and thus lower GDP per capita growth in dollar terms. One of the key policies under EFF was to let the rupee adjust to its market value which led to depreciation of rupee by 24% between July 2019 and September 2020. A US dollar traded at rupee 164.39 on September 30th, 2020 against rupee 131.75 on July 3rd, 2019 when the EFF was approved. Overall, rupee dropped to dollar by 45% since the Government of Pakistan Tahreek-e-Insaaf (PTI) took over in July 2018.

Sri Lanka has increased its GDP per capita by more than $1000 to $3,853 between 2010-19, it experienced a steep decline in GDP per capita growth after 2018 that could be partially explained by the April 2019 terrorist attacks.

The final impact on fiscal space however is conditioned on revenue elasticity of GDP growth and the composition of tax revenues. Tax revenue elasticity of GDP growth for Pakistan is 1.01 for direct taxes which account for 33% of total tax revenues. Sales tax which accounts for 37% of total tax revenues has a growth elasticity of almost one (0.99). Lower economic growth elasticities of Excise Duties (0.47) and Custom Duties (0.32) renders a lower tax revenue elasticity of economic growth for Pakistan (0.64) (Fauzia Mukarram, 2001). The tax elasticity of GDP growth is also less than 1 for Sri Lanka. It means that growth in tax revenues was mainly based on increasing the tax rate and not the tax base. The impact of lower growth on fiscal space therefore will be less mild.

3.2.2. Revenue collection capacity

Pakistan's tax revenues are expected to decline by 10% while expenditures are projected to increase by 25% (Nasi et al., 2020). Table 7 shows the difference in revenues and expenditures which is quite stark in Pakistan and Sri Lanka. Revenue as a ratio of GDP declined even before COVID-19 hit Pakistan from 15.40% in 2017 to 12.80% in 2018 and to 14.30% in 2019, even though GDP in dollar terms declined in 2018 and 2019 compared to 2017. Increase in revenue in 2020 is mainly because of lower GDP of the economy, and not growth in GDP.

The gap is lower in Afghanistan due to specific grants targeted towards the operating budget. Domestic revenue collection is a smaller and secondary source of revenue (table 8). Moreover, a significant portion of Afghanistan's budget (40%) is covered by aid. The country may not be able to attain economic recovery without the support of external funding (Strand, 2017). Domestic revenue collection declined in Afghanistan by 19% even before the pandemic (World Bank, 2020). Moreover, during the pandemic revenues declined by more than 34% against Ministry of Finance targets. Year on Year (YoY) growth in exports was 11% for the first quarter, with the projection likely to be negative due to border closures. It is also noteworthy that Afghanistan's entire trade deficit was financed by aid inflows (World Bank, 2020).

Table 7: Expenditure and total revenue comparison as % of GDP

	PAKISTAN		AFGHANISTAN		SRI LANKA	
	EXPENDITURE	REVENUE	EXPENDITURE	REVENUE	EXPENDITURE	REVENUE
2014	20.00	14.50	25.4	23.70	17.80	11.50
2015	19.60	14.30	25.95	24.50	20.35	13.30
2016	19.90	15.30	26.0	26.10	19.46	14.10
2017	21.30	15.40	25.88	25.70	19.30	13.70
2018	21.60	12.80	27.03	28.50	18.70	13.40
2019	23.50	14.30	28.21	27.0	19.40	12.60

Source: Ministry of Pakistan, Ministry of Afghanistan, Ministry of Sri Lanka, IMF.

Table 8: Revenue composition as % of GDP

	PAKISTAN		AFGHANISTAN		SRI LANKA	
	TAX	NON-TAX	TAX	NON-TAX	TAX	NON-TAX
2014	10.2	4.3	8.5	15.2	10.1	1.4
2015	11.0	3.3	10.0	14.6	12.4	0.9
2016	12.6	2.7	10.7	15.4	12.2	1.9
2017	12.4	3.0	12.4	13.3	12.5	1.2
2018	11.6	1.2	13.3	15.2	11.9	1.4
2019	11.0	3.3	13.9	13.1	11.6	1.0
2020*	13.3	2.5	12.9	13.6	12.4	1.4
2021*	14.3	2.5	14.0	13.7	13.3	1.4
2022*	14.9	2.5	15.3	13.9	13.9	1.4
2023*	14.9	2.6	16.6	14.1	14.1	1.4
2024*	14.9	2.5	16.9	14.1	14.1	1.4

Source: Ministry of Finance Pakistan, Ministry of Finance Afghanistan, Ministry of Finance Sri Lanka, IMF.
*Note: * Projected.*

According to the IMF Country Report Afghanistan (May 2020), the World Bank along with other development partners is developing a relief package of in-kind or cash transfers to support food security among the vulnerable segment. The cost of implementing a nationwide scheme such as this in remote areas and village councils for two months is estimated at $300 million (1.5% of GDP). Thus, Afghanistan's total fiscal response to the pandemic will amount to 3.5% of GDP in 2020 with half of it expected to be funded by donors. However, the other half still must be funded by the government itself (IMF, 2020) which is most likely to be filled by borrowing.

3.2.3. Trends in external sector performance (2008-2019)

Pakistan has a dwindling export sector with a lower export to GDP ratio of 10.1% in 2018 compared to 23.1% for Sri Lanka (figure 11). Pakistan critically depends on remittances to fund current account deficit, development financing and stabilization of the financial sector. In 2019, remittances stood around 8% of GDP for Pakistan and Sri Lanka. It was almost double than that of Afghanistan, 4.54% (figure 12).

On the external sector front, remittance flows to Pakistan increased to a record high in June 2020 with a surge of 50.7% as compared to June 2019 (Iqbal, 2020). Some plausible explanations for this include savings from Hajj-related activities that are now postponed which are remitted back to Pakistan. Furthermore, due to the counter-cyclical nature of remittances, inflows from abroad may also increase to provide relief to distressed families in the country of origin and returning migrants bringing their earnings back to Pakistan (Ahmed, 2020).

FDI inflows to South Asia remain lower when compared with East Asia and South East Asia (WIR, 2019). Pakistan attracts lowest inflows (figure 13). According to UNCTAD's World Investment Report 202025, South Asia attracted higher flows and FDI to the region reached $57 billion in 2019, up from $52 billion in 2018, increasing South Asia's share in total global FDI flows from 3.5% in 2018 to 3.7% in 2019. India received the largest share of $51 billion. Inflows to Bangladesh were $1.6 billion, a fall of 56 per cent compared to 2018. According to the report, "*the decline reflects an adjustment from a record-high level in 2018*".

FDI flows to Pakistan grew by 28% in 2019 compared to 2018 reaching $2.2 billion, after a deep fall of 30% in 2018. FDI inflows to Pakistan may not have a sustained impact on fiscal space because of smaller size and their nature. Pakistan fails to attract efficiency-seeking FDI inflows (Jalil and Javed 2020). The UNCTAD's World Investment Report of 2020 confirms that "*the growth [in FDI inflows] was driven by equity* investments *in the energy, financial, and textiles industries, with major investors from China and the United Kingdom*".

International aid which is composed of net aid from total bilateral aid from DAC donors, UNAIDS, and ODA, has a slight declining trend over time and a sharp fall after 2013 (figure 14). Pakistan received around 15 times less foreign aid in 2018 ($0.36 billion) than what was received by India ($5 billion) and Bangladesh ($5.5 billion). Most importantly, foreign aid to Pakistan and Sri Lanka has been declining since 2010. This trend is expected to continue.

Figure 11: Total exports (as % of GDP - 2008-2019)

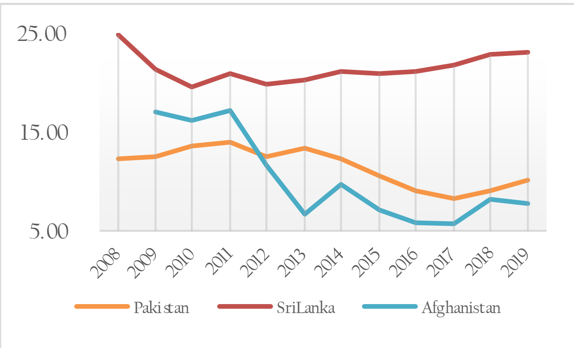


Figure 12: Total remittances (as % of GDP -2008-2019)

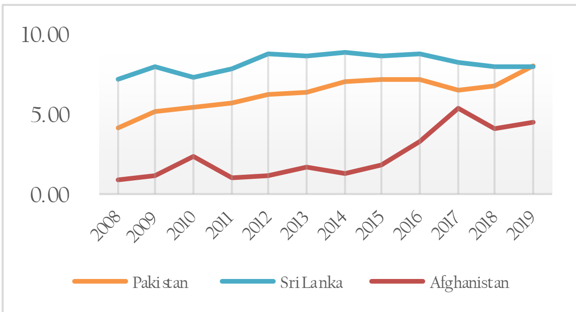


Figure 13: FDI (as % of GDP -2008-2019)

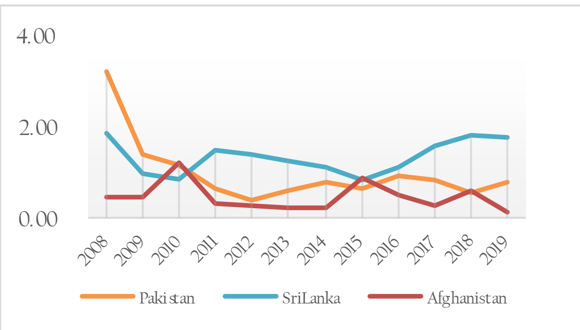
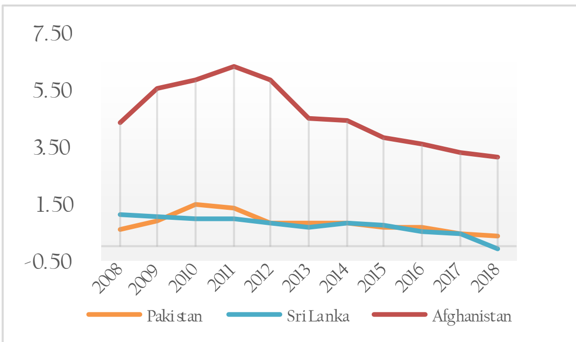


Figure 14: Total aid (US$ Billion - 2008-2019)



25 World Investment Report (2020): International Production Beyond the Pandemic. It can be retrieved from https://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=2769

3.2.4. External sector performance (2020-2025)

Remittances inflows to Sri Lanka are expected to remain stagnant, from $5.85 billion in 2019 to US$5.90 in 2024[26] (figure 15). As in the past, remittances are likely to continue to relive pressure on CAD. Remittances inflows to Pakistan are expected to pick up after 2021 reaching to US 24.36 billion in 2025. Initiatives like SBP Digital Roshan Account may boost the remittances inflows to Pakistan further. Roshan Digital Accounts, providing innovative banking solutions for millions of Non-Resident Pakistanis (NRPs), can be opened fully digitally and require a basic set of information and documents. This contrasts with the standard practice where one must visit the banks and fill in lengthy forms to open commercial bank accounts.

Exports of Pakistan are expected to rise after 2021, reaching $33.94 billion in 2025 from 24 billion in 2019[27]. Exports for Sri Lanka are also expected to marginally grow, from $12.30 billion to $15.81 billion in 2024. Exports of Afghanistan, already the lowest in South Asia, are expected to remain stagnant (figure 16). FDI inflows to Pakistan are expected to increase from $1.7 billion in 2019 to $5.7 billion in 2025. FDI inflows to Sri Lanka are expected to witness a net outflow over the period of projection, from 2020 to 2025 (figure 17). Overall, Pakistan is expected to perform better relative to Sri Lanka and Afghanistan. Afghanistan however is expected to witness sharp increase in foreign aid after 2021 which can release some of the fiscal stress as it makes around 40% of its budget (figure 18)

Figure 15: Projected remittances (US$ Billion)

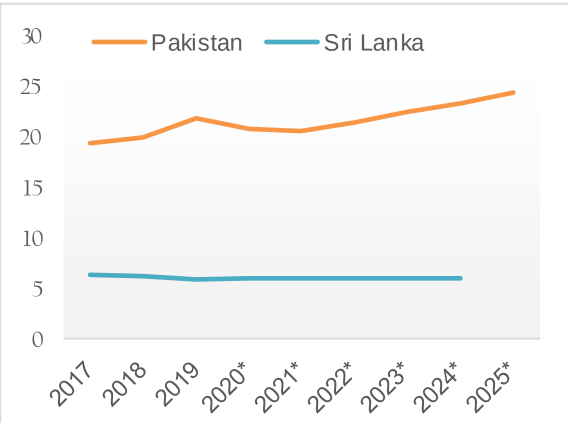
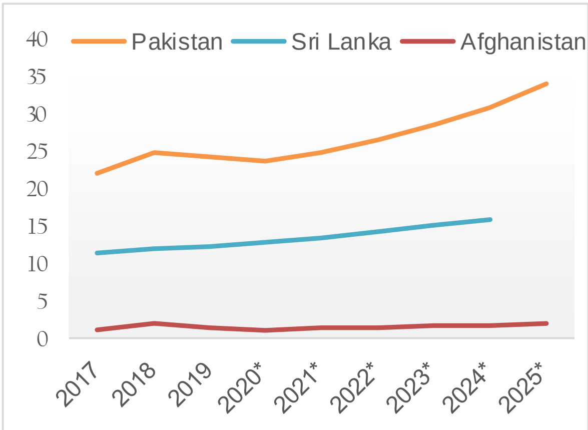


Figure 16: Projected total exports (US $ Billion)



26 IMF Country Report No. 19/335 for Sri Lanka. Importantly the remittances for Sri Lanka may fall below these pre-Covid estimates. In worst case scenario, Sri Lanka may experience a decline of 21.9% compared to baseline remittances in 2018 (Takenaka and others, 2020).

27 IMF Country Report No. 20/114 for Pakistan.

Figure 17: Projected FDI inflow (US$ Billion)

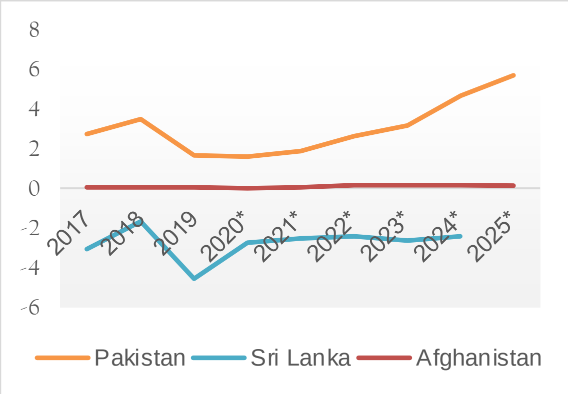
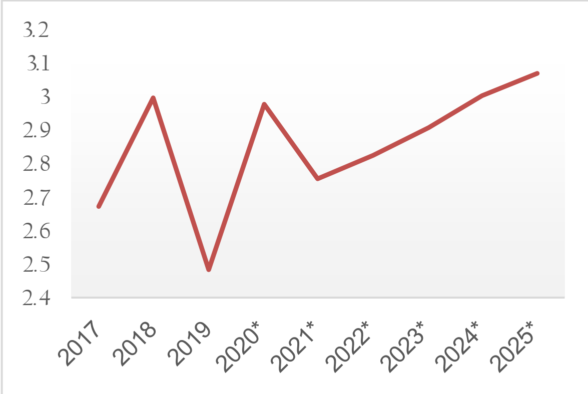


Figure 18: Project aid (US$ Billion)



3.3. Debt and fiscal balance

The sustainable debt-to-GDP ratio can vary with market and economic conditions. Pakistan has set this ratio at 60%[28] which is above the IMF's "prudent" limit of 40% (Chowdhury and Islam, 2020). Sustainability of public debt critically depends on share of foreign currency denominated debt. It is recommended that foreign currency denominated debt must not be more than 70% of the total public debt for low-income countries (Pienkowski, 2017). Elevation of debt-to-GDP ratio does not mean low fiscal space. Higher share of external debt having a short maturity period coupled with poor market and economic conditions however may reduce fiscal space.

Both Sri Lanka (86.8%) and Pakistan (85.4%) had higher debt-to-GDP ratios in 2018-19 before the COVID-19 crisis (table 9). But Pakistan seems to have higher fiscal space relative to Sri Lanka. First, it has a higher share of domestic debt (53.8%) in total debt. Second, it has lower total debt service to GDP (4.76%) than Sri Lanka (13.5%). Third, the short-term debt to total external debt is 6.9% compared to 15.5% for Sri Lanka (table 9). Lower exports however may create stress for Pakistan. In contrast to the share of 59.1%, short term debt is 113.1% of exports for Pakistan.

Given lower fiscal space from domestic resources, the stimulus to mitigate the immediate impacts of the COVID-19 and to finance the economic recovery are expected to inflate the public debt. The debt-to-GDP ratios of Sri Lanka and Afghanistan are expected to rise in 2020 and 2021 before declining gradually till 2024 (figure 19). The highest rise and lowest decline are forecasted for Sri Lanka. The ratio is expected to increase to 92.4% in 2020 from 86.8% in 2019 before declining to 77.9% in 2024 (figure 19). In contrast Pakistan is expected to witness a substantial improvement, from 83.3% in 2020 to 68.8% in 2024. Debt-to-GDP for Afghanistan increases from 9.9% in 2020 to 12.5% in 2024.

28 Fiscal Responsibility and Debt Limitation (FRDL) Act, 2005, which states "within a period of ten financial year, beginning from the 1 July 2003 and ending on 30 June 2013, the total public debt at the end of the tenth financial year does not exceed sixty percent of the estimated gross domestic product for that year and thereafter maintaining the total public debt below sixty percent of gross domestic product for any given year.

Table 9: Debt sustainability indicators

Debt Sustainability Indicators	Pakistan	Afghanistan	Sri Lanka
	2019-20	2019-20	2019-20
Current fiscal deficit % of GDP	8.85	0.98	6.77
Public debt to GDP	85.4	6.8%	86.8
Domestic debt to GDP	53.8	0.5	44.1
Total debt service to GDP	4.76	0.741	13.5
Total external debt to exports	271.4	51.2	167.6*
External debt service to exports	59.5	2.9 (GOA, 2020)	36
External debt % of GDP	42.2	6.3	42.6
Short term % of external debt*	6.9**	14	15.5
Total reserves % of external debt*	13	315	13.2
Short term external debt % of forex*****	113.1	6.31	59.1
Short term external debt % of exports*****	55.81	16.1	37.25

Current and projected debt obligations						
	2019-20	2020-21	2019-20	2020-21	2019-20	2020-21
Total external debt service (Millions USD)****	13,538	17,720	133,726	129,794	4,447.7	4,208.60
Total domestic debt***	22,577	23,994	7.2	N/A	6,629	N/A

Source: IMF Country Report Pakistan April 2020, Ministry of Finance Government of Afghanistan, Ministry of Finance Sri Lanka, Ministry of Finance Pakistan, World Bank.

*Noted: *For the year 2018.*

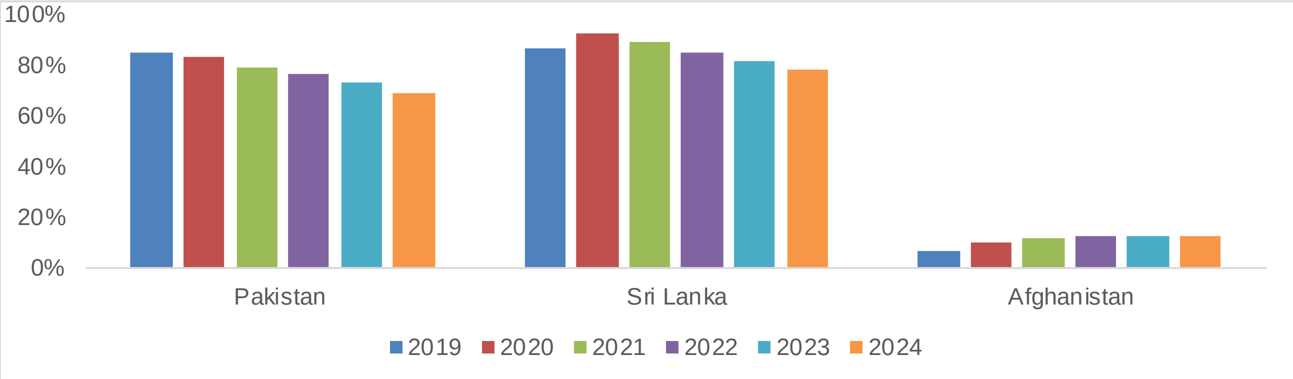
*** Statistic is for 2019.*

****Total domestic debt is in each country's local currency (billions).*

*****Afghanistan's external debt service is in Thousands of USD.*

****** Author's own calculations.*

Figure 19: Current debt to GDP ratios and forecast



Source: IMF Country Report, Pakistan, April 2020. Ministry of Finance Afghanistan, Ministry of Finance Sri Lanka.

3.3.1. Pakistan

The maturity profile of external debt for Pakistan is sufficient, liquidity and rollover risks associated with commercial debt have been reduced. Pakistan's debt obligations to the tune of $1.8 billion are due in 2020 between July and December. Furthermore, Pakistan's debt payment towards 11 bilateral lenders between May 2020 and June 2021 currently stands at $2.58 billion. In the aftermath of COVID-19, Pakistan's external financing requirements are $25.8 billion with a financing gap of $2 billion (IMF, 2020).

For the fiscal year 2021, the projected financing requirements are $29.3 billion with a financing gap of $1.6 billion. According to the IMFs Pakistan Country Report April 2020, Pakistan's public debt is sustainable. It is reinforced by rolling over maturing debt from main bilateral creditors (China, Saudi Arabia, and UAE). Urgent demand and payment of $1 billion to cash deposits of Saudi Arabia tested Pakistan. However, Pakistan was able to manage to obtain the same amount from China.

In its April 2020 Global Economic Outlook, IMF projected that Pakistan's recovery is expected to be a gradual V shaped one as annual growth reaches approximately 2% in FY 2021. However, in its World Economic Outlook June 2020, IMF downwardly revised Pakistan's annual growth rate to 1% in FY 2021 (World Economic Outlook, 2020). This assumes that sectors such as services and transport sectors will bounce back quickly. The World Bank Global Economic Prospects (World Bank, 2020) report forecasts Pakistan's real GDP growth for the FY 2020-21 at -2.6% and -0.2% in the subsequent fiscal year. Asian Development Bank's forecast for Pakistan's growth rate for the year 2020 is -0.4% followed by growth of 2.0% in FY2021.[29]

Domestic tax mobilization however will remain low in as mentioned earlier due to low economic activity and tax relaxations to boost economic recovery. Moreover, IMF conditions dictate that the Pakistan government cannot borrow from SBP. This leaves the authorities with the choice to either borrow from commercial banks or external finance. For Afghanistan, this is limited to only external finance as the only borrowing done in the domestic market is related to the outstanding debt to Da

29 Data retrieved from www.adb.org/countries/pakistan/main.

Afghanistan Bank (DAB) and the resolution of the Kabul Bank crisis (IMF, 2007). Pakistan has its biggest challenge of State-Owned Enterprises (SOE) debt. Debt in steel, cement and energy could have a significant impact on the country's fiscal position.

Sri Lanka

Sri Lanka's total government debt is equal to $34.7 billion at the end of 2019 of which 65% is in USD (figure 20). Additionally, one fifth (21%) of the external debt stock will mature in the next five years. Debt payments in foreign denominated currency accounted for approximately 42% of government revenue in 2019, this is up from 27% in 2018 (Government of Sri Lanka - Ministry of Finance, 2020). Sri Lanka to date has not received any relief package or rapid credit facility from the IMF. The tourism-dependent economy with almost no receipts from the sector has further exacerbated the financial constraints. This may add stress to Sri Lanka' lower fiscal space if debt repayments are not rescheduled.

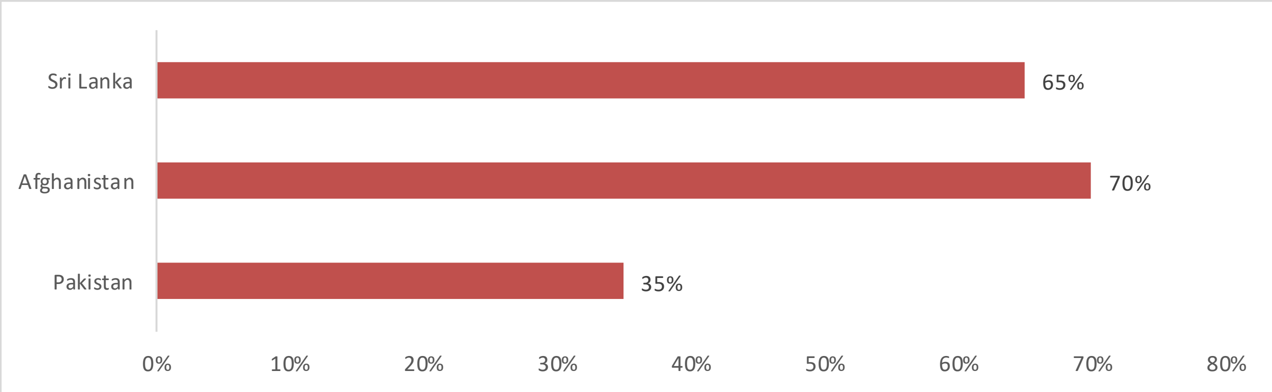
Overall, Sri Lanka is one of the most sovereign debt-distressed countries in South Asia. Its foreign exchange reserves amounted to $6.5 billion at the end of May 2020, while external debt service payments are to the tune of $3.8 billion from the period of June to December 2020 that includes a $1 billion international sovereign bond payment due in October. Due to these obvious external financial constraints, Fitch ratings lowered Sri Lanka's sovereign rating to B- (FitchWire, 2020).

The COVID-19 has risked the sustainability of government debt in Sri Lanka. The country faces short maturity of external debt, limited financing options and lower foreign exchange reserves. Negative outlook from Fitch may limit options to raise finance from market. This is already evident. Sri Lanka offered $60 million worth of bonds but was only able to raise $28 million (Gunadasa, 2020).

With this low demand and the pandemic, the government cannot increase interest rates to reward investors for the greater risk as banking sector liquidity also needs to be ensured. The government also cannot increase taxes and reduce their expenditure leading to a very tight fiscal situation. This will in turn cause both the fiscal positions and current account to deteriorate and further degrade credit ratings. Sri Lanka is facing a rollover risk and could face external funding strains if it is unable to secure substantial support. This would make borrowing even more costly and further limit access to finance.

COVID-19 can significantly hurt foreign exchange earnings of Sri Lanka because of country's higher dependence on remittances and tourism. The pandemic has adversely affected remittances inflows and tourism sector. Sri Lanka's debt sustainability largely depends on help from the IMF and the global community's willingness to reschedule its debt.

Figure 20: Foreign currency debt stocks (% of total government debt)



Source: Ministry of Finance Pakistan, World Bank, Ministry of Finance Sri Lanka.

3.3.2. Afghanistan

Most of Afghanistan's debt is on a concessional basis making the repayment threshold relatively safe due to long average loan maturity at about 14 years (World Bank, 2020). The financing fiscal requirements for Afghanistan are estimated at $700 million for 2020 and $400 million for 2021. However, due to the absence of domestic debt and limited options of external debt, financing these fiscal requirements is severely strained. Furthermore, as most of Afghanistan's debt stock is in foreign currency, small fluctuations in the exchange rate can bring about huge changes. Low domestic revenue mobilization and exports make Afghanistan's concessional debt sustainability highly vulnerable to shocks. The debt sustainability (DSA) of Afghanistan is a difficult task as it depends on donor grants inflows (currently around 38% of GDP). A decline in grants can lead to higher debt distress (IMF, 2020).[30]

According to the World Bank, Afghanistan's recovery could look smooth if it is able to attract enough aid inflows but could turn into a W-shaped recovery if a new infection wave arrives in winter (World Bank, 2020). Analysts predict Sri Lanka's recovery will be a flattened U shaped as economic growth would only turn positive in 2024 due to the prolonged impact of COVID-19 (Wijewardene, 2020). This constrained fiscal space would translate to lesser amounts of resources spent in the way of development programs making a quick recovery or a V-shaped recovery difficult to realize.

30 See "IMF (2020), request for disbursement under the rapid credit facility—debt sustainability analysis" for a detailed debt sustainability analysis for Afghanistan.

4. Fiscal strategy options for further revenue mobilization

4.1. Deploy existing resources better

Taxation reforms aimed at expanding the tax base, improving export competitiveness, and creating an enabling environment are some of the most relevant medium-term measures for the economies under analysis for reasons underlined below. Moreover, the role of investment promotion agencies and how they can attract FDI will be critical to aid recovery efforts. These key areas will be pivotal to open other avenues of finance such as private philanthropy and blended finance.

Tax authorities will have to digitize their processes with a user-friendly ICT system as a foundation to widen the tax base. Tax collection authorities' human resource skills and capacity needs to be enhanced. Even though there is mixed evidence, collectors could be given incentives or more specifically financial incentives to collect more revenue that may also discourage them to take bribes and write off loans (Bolotnikova, 2020).

Federating units and local governments must take initiatives to increase domestic resource mobilization. In the medium to long run municipal taxation may be imposed. Sales taxes that are a major source of revenue in the developed world for provinces may be transferred to provinces. Property and taxes can be transferred to local governments increasing their autonomy.[31] Local governments can also be utilized to identify and target the most vulnerable with specific grants rather than formula grants and enhance their communication and engagement with taxpayers to encourage long-term compliance.

With global trade being heavily impacted, government would have to take some aggressive measures to increase export competitiveness and promote export led growth. Import duties, regulatory duties, and additional customs duties on essential raw materials for main and potential export industries need to be reduced permanently to eliminate anti-export bias. In the budget for FY2020-21, Pakistan reduced rates of customs duty on around 200 tariff lines mainly for raw material and intermediate goods (Government of Pakistan-Ministry of Finance, 2020). Afghanistan being a predominantly agrarian economy may also benefit from measures that reduce input costs to increase exports.

4.2. Expenditure switching and efficiency enhancing policy reforms

Expenditure switching and efficiency enhancing policy reforms represent a powerful instrument to enhance fiscal space to finance economic recovery from the pandemic. Reprioritizing and shifting the resources from low productivity and low priority sector to higher productivity and high priority sectors increases the productivity gains from specific public expenditures which, in turn, create fiscal space (Roy 2007). In the face of the pandemic, governments in the respective countries may

31 Local governments are present in Sri Lanka. Afghanistan is governed mostly from the center with some autonomy to provincial governors. In Pakistan, the 18th Amendment that involves devolution of powers was not implemented properly making the local governments rather ineffective in-service delivery.

prioritize the sectors to be focus under fiscal stimulus and routine fiscal policy over the last couple of years.

Among others, there can be two major criteria for reprioritization. First, investments in health sector and social protection have emerged as the key lesson from the COVID-19. The countries with a better social protection and string health system were better able to cope the pandemic. Efficient social protection system allowed the government to timely respond to protect the people from the immediate impact of COVID-19. Particularly, Pakistan and Afghanistan need to shift public expenditures towards health and social protection system.

Second, government must assess the distributional effects of public expenditures. The expenditures reducing inequality must be prioritized. Poverty, social and income inequality, and unemployment are interrelated. A disconnect between macroeconomic and social policy can lead to structural inequalities of access to health, education, productive jobs, and other income opportunities. Low social mobility - inequitable distribution of opportunities - creates systemic deprivation of marginalized and poor which translates to low productivity, poor schooling, and health trap through intergenerational mechanisms.

Reducing inequalities in the subsidies can be one the major tool. Evidence suggests that larger share of health subsidies goes to top 20% of population, the rich quintile. Interestingly, the poor quintile of population benefits from subsidies in primary education while ethe subsidies in higher education mainly go to rich quintile. It holds true for labour market. Pensions and other forms of social protection in labour market do not reach to the most vulnerable workers employed in low skilled occupations. In equitable subsidies can be reduced to improve the public expenditure efficiency. The countries must ensure to provide targeted subsidies to the population groups most vulnerable to the pandemic and other similar shocks.

Pakistan has a huge margin to undertake reform in multiple sectors (table 10). The estimated impact of the selected reforms for Pakistan shows that a significant portion of government's future financing needs could be met by reforms in the four major areas can provide additional resources equal to 1.9% to 2.8% of GDP.[32]

32 Measured in 2015.

Table 10: Major areas of reforms in Pakistan and estimated fiscal impact

Reform Area	Reforms	Fiscal Impact (%GDP)
Tax reforms	Reforms at federal and provincial level, focusing on tax policy as well as administration.	0-5-1.0
Public debt	Debt management reforms, to reduce the cost and term structure of government debt.	0.4 – 0.8
Power Sector	Reforms: reducing the cost of electricity subsidies by adjusting the price and improved governance; and improving the efficiency of subsidies through better targeting to deserving groups	0.5
State Owned Enterprise	Reforms of State-Owned Enterprises	0.5
Total fiscal impact of these reforms		1.9–2.8

Source: Pakistan's Public Expenditure Insights & Reflections, Rafter Public Expenditure Report 2015.

A strong accounting and accountability system for project/program design and implementation can help save resources to finance the economic recovery. Studies on public expenditure management shows that "*on average in Pakistan it takes twice the originally projected time and almost twice the originally estimated cost to complete a development project. Another weakness is a strong bias in favor of development spending at the expense of recurrent expenditure. This results in a poor mix of public expenditure that results in insufficient funds being provided to maintain existing assets*".

Afghanistan has higher level of public expenditure, which is unsustainable levels, primarily due to very high security expenditures which count to around 30% of GDP. A fundamental overhauling is required. Around 66 percent of security sector expenditure and 34% of civilian expenditure is currently off-budget (WB)[33]. Reducing the off-budget share of expenditures can significantly improve the public expenditure efficiency.

4.3. Expanding tax base

The tax base is very low in all three countries. Pakistan collects half of the economy's tax potential, according to World Bank estimates. It loses almost two thirds of GST liabilities and more than half of income tax remains uncollected. According to IMF estimates, Pakistan had a "tax revenue gap" of roughly $28 billion in 2016, equivalent to 10 percent of national GDP (Cevik, 2016). In other words, it could double its tax revenue-to-GDP ratio if the gap is bridged.

A complex taxation system, poor tax governance, blanket tax emptions and subsidies and untaxed

33 For details, refer to World Bank report on "Afghanistan Public Expenditure Update", http://documents1.worldbank. org/curated/en/696491564082281122/pdf/Afghanistan-Public-Expenditure-Update.pdf.

sectors are the key factors behind lower tax base. To collect the potential tax revenues by expanding the tax base, government needs to:

- have political will, not giving in to pressure groups
- simplify the tax filing and payment.
- harmonize the tax collection-definition, code, and rate-between federal government and provinces.
- reduce the burden of the withholding regime on firms and individual taxpayers.
- focus on sustainability of the reforms
- improve tax administration (capacity building, use of technology)

Taxing the untaxed is crucial. The agriculture sector contributes 20% to GDP. But its share in federal taxes for the year FY2016 was only 0.09%. The same year it accounted for less than 1% in provincial taxes (Khan, 2017). The agriculture sector presents a classic example of fiscal indiscipline. The subsidies to the sector outweighed the income tax collected from the sector by a factor of 24 in 2016. Government can start by taxing the top 1% of farmers, which hold about one fifth of the total farmlands. The gap between income tax from the sector and subsidies to the sector must be minimized. One way is to design targeted subsidies instead of blanket exemptions and subsidies.

In the medium to long run, Pakistan needs to improve the National Finance Commission (NFC) award. The current NFC award formula for distribution of resources between federal government and provinces lacks any incentives for provinces to invest in revenue mobilization. First, it assigns only 5% weight to revenue collection. Second, it does not adjust the size of revenues to the potential of revenues of a province. New arrangements must consider revenue efforts (revenue collected compared to potential revenues) and assign a higher weight of at least 10% (Javed and Ahmed 2019).

Sri Lanka experienced decline in tax to GDP ratio over the time, from 19% in 1990 to approximately 12% in 2018 (WDI). Overall government revenue to GDP ratio dropped to 12.2% in 2019 from 13.4% in 2018. The Government must work to increase the focus on effective implementation of the new Inland Revenue Act of 2017 with the major focus to increase the income tax net and simplify the tax system.

Afghanistan has the lowest tax-to-GDP ratio of only 7.3%. The ongoing conflict, tribal wars and poor institutional capacity seems to constrain any serious improvements in tax system, base, and revenues. According to IMF, *"in the near term, larger deficits will be financed partially by official support plus the government using its deposits at the central bank. In the medium and long term, declining grants will be replaced by external concessional loans with 35 percent grant element"* (IMF, 2020).

4.4. Carefully timed and well-targeted fiscal stimulus for economic recovery

The pandemic has caused an economic recession and fiscal policy needs to tackle it. The recovery from the pandemic demands well thought-out fiscal policy stimulus. Governments must accept temporary reduction in revenues along with increasing expenditures. Fiscal policies aiming to extract revenues at a time of recession may prolong the recessions and slow down recovery. Despite the limited fiscal space from domestic resources, all three countries must continue with the measures put in place to protect people and businesses during the pandemic, till end-2020 at least. A premature ending of the support measures may cause a prolonged period of unemployment, and poverty as countries fail to promote a robust recovery.

Support measures must aim for a comprehensive socioeconomic recovery which improves human development. While the policies should focus on "long-term growth", exclusive focus on "recovering economic growth" must be avoided. The recovery from the pandemic must be associated with lower poverty, increased employment, and social inclusion of the marginalized. Not only must the public sector be prepared to enact additional measures as conditions require, but also ensure that the policies remain in place until the recovery is clearly underway.

Income support measures directed towards low-income households must continue at least till March 2021. Not only are they required to protect people during the prolonged layoffs even after the lockdowns are lifted and businesses are open, but they also support the economic recovery as poor individuals/households will spend any additional resources they receive quickly. Higher marginal propensity to consume (MPC) leads to a higher multiplier effect. The size, nature and duration of these measures however must continue to respond to the changing circumstances for a gradual exit (UN,2020). To those who are in the tax net, government must continue and expand refundable tax credits. Deficit and debt concerns should go on the back burner in a recession.

Extension and expansion of support to SMEs is crucial for inclusive recovery from the pandemic. Particularly, the concessionary loans and other relief measures must reach the SMEs and those working in the informal sector. SMEs from the tourism and hospitality sectors are the most relevant for this type of relief as they are among the hardest hit in this crisis with almost a complete shutdown of economic activity making them a large unemployment risk as well. Similarly, deferring payment of excise duties and custom duties on import of machinery for the most vulnerable sectors in the aftermath of COVID-19 is essential for similar reasons highlighted above.

SMEs must be encouraged to adopt modern methods of production and management through these support measures available in period of economic recovery. SMEs owned by women and those working in the most vulnerable sectors must be given preferential access to subsidies, interest-free loans, and tariffs rebates. In the wake of disrupted supply chains, Government must ensure timely supplies of essential inputs without price hikes. Respective countries must finalize SME policies integrating SMEs into broader development policy.

A well-targeted fiscal stimulus will need to create conditions that encourage sustainable consumption and investment. Pakistan, Sri Lanka, and Afghanistan fare poorly on sustainable consumption and investment. Despite all the challenges, the COVID-19 crisis provides an opportunity to promote green investments. Data from the 2008-09 global financial crisis shows that the Republic of Korea which geared 70% of its stimulus toward green measures recovered faster and the impact was long-lasting.[34]

At the policy level, these countries must work together with the private sector to develop responsible trade and industrial policies that address sustainability needs. The stimulus measures, such as restructuring tariffs, para-tariffs, and regulatory measures, must be used to incentivize value chains to move towards sustainability.

Sri Lanka, Pakistan, and Afghanistan must integrate stimulus with green energy and transport. Support measures to SMEs must be provided to switch to green energy. Appropriate business models must be developed to promote rooftop solar. The protectionist import duties on the solar and other equipment for renewable energy must be slashed. These countries must also invest in long term behavioral changes toward sustainable consumption through increased awareness and engagement of consumers.

International coordination will be critical in this regard, fiscal support is especially required for low-capacity countries to complement domestic measures (OECD, 2020). Furthermore, countries should be careful and not run permanent fiscal deficits. Governments need to strike a balance between a prudent response while paying attention to the fundamentals.

As Pakistan's health situation improves day-by-day, restrictions have eased. To aid recovery efforts Pakistan would need to invest in its agricultural sector and accelerate improvements in service delivery by enhancing institutional capacities. These efforts can be financed by Pakistan's banking sector that is currently exceptionally sound (Adil and Javed, 2020). Aggressive facilitation from commercial banks at the recovery stage may not only help in mitigating the pandemic's socio-economic impacts but also help further the government's financial inclusion agenda.

With Afghanistan's economy also on the brink of reopening, the Afghan government should focus on careful management of existing resources, as international assistance is likely to decline soon. Furthermore, the government should look to secure more grant support to create confidence in investment that should be coupled with efforts towards a better regulatory environment. Finally, the Afghan government should provide liquidity support especially to the most vulnerable and affected sectors to promote recovery.

Investments in social protection such as universal lifecycle cash transfers (UN, 2020) may help preserve Sri Lanka's high social progress in the subregion and kick-start economic recovery. This combined with consistent liquidity support to SMEs in the aftermath of the crisis may not only help avoid lay-offs but also generate short-term employment opportunities. Finally, the government's focus should be on securing short-term debt moratoriums from major creditors that will help preserve fiscal space vital in financing recovery.

34 Republic of Korea's climate change laws.

4.5. External sector and other financial inflows

4.6. Trade

Trade needs to be promoted proactively through the respective trade bodies of each country encouraging better data and regulatory governance. It is evident from figure 21 that all three countries have substantial room to improve the regulatory environment and ease of doing business (EODB).

Inadequacy of online and digital payments infrastructure to support e-commerce coupled with weak linkages to regional value chains severely limits these countries in harnessing the untapped financial potential of the IT industry. These costly, time-consuming business regulations and weak automation of business-related procedures are a major hurdle in the way of attracting good quality FDI.

Bangladesh can be taken as a good example from the sub-region that has improved their export competitiveness in similar conditions. Bangladesh moved from highly protectionist policies in the early 1990s to a more liberalized regime. This included tariff cuts, rationalization, elimination of quantitative restrictions and most importantly improving market orientation through deregulation (Patel, 2005).

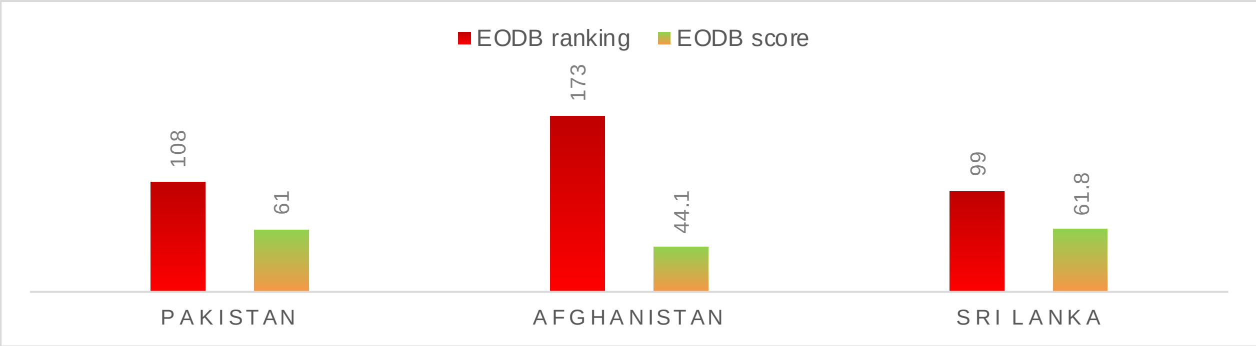
Even though the export quota system was phased out in the beginning of 2005, the government supported the local industry through measures such as back-to-back letters of credit, cash incentives, duty drawback schemes and bonded warehouse facilities (Haider, 2007). This was combined with other initiatives such as encouragement of FDI and establishment of export processing zones that helped lead the government's idea of export-led industrialization.

4.7. FDI

As figure 22 shows, FDI to Pakistan increased while it declined for both Sri Lanka and Afghanistan. Of the three countries, Pakistan has a comparative advantage with a larger domestic market and increasing middle class. Sri Lanka's tourism sector can generate growth and advance the 2030 Agenda (Munasinghe et al., 2019). Afghanistan's mineral reserves, specifically coal, quarries, sand, salt, gemstones, and copper reserves, have the potential to generate $253 million in value from a current value of $60 million (World Bank, 2005).

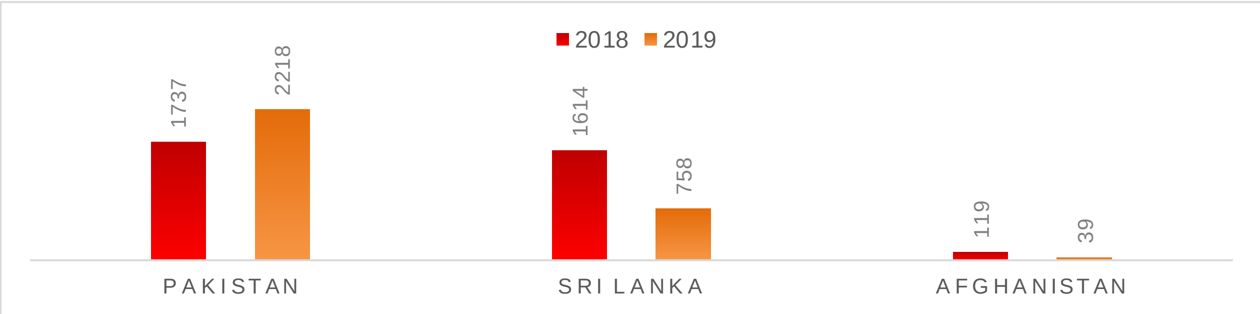
However, the role of investment promotion agencies needs to be amplified to effectively attract FDI. Investment promotion agencies need to make sure their marketing strategies are on point. Furthermore, investment promotion agencies need to be an autonomous body and be able to provide investors one window support. Tiers of scrutiny for any investment project need to be minimized which would give confidence to investors that they have an effective facilitator.

Figure 21: EODB ranking and score (2020)



Source: World Bank.

Figure 22: FDI Inflows (Millions of USD)



Source: UNCTAD World Investment Report 2020.

A favorable domestic environment is also crucial to attract financing from private foundations. The importance and potential of private foundations can be gauged by the fact that the Bill & Melinda Gates foundation provided over $3.9 billion[35] of funding in the form of Official Development Assistance. Additionally, philanthropy from the private sector, albeit much smaller to ODA or Other Official Flows (OOF), could finance the SDGs Agenda. Finance raised from Corporate Social Responsibility (CSRs) could also aid in effective service delivery.

Furthermore, promoting innovative sources of finance such as blended finance needs to be introduced into these economies. Blended finance allows private investment to be leveraged with foreign concessional finance. Blended finance instruments such as Investment grants, Loan Guarantees, and equity investment[36] can help in unlocking private sector finance and undertake investments that have social, environmental, and economic gains.

The most important supporting mechanism of blended finance in the context of developing countries such as Pakistan, Afghanistan and Sri Lanka would be to provide technical assistance. This involves reducing high transaction costs and risks for investors linked to relatively new ventures.

35 Data retrieved from https://stats.oecd.org/qwids/

36 For more information please refer to Javier Pereira, "Blended Finance: What it is, how it works and how it is used," 2017.

Technical assistance can help strengthen project capacity especially SMEs and take the form of monetary contributions when multilateral development partners are involved (OECD, 2018). The central banks of the countries under analysis should take the lead in employing this new and innovative tool to raise finance.

4.8. Stopping illicit capital outflows

Illicit financial flows, mainly capital outflows to developed countries for safer investment returns, need to be curbed. Approximately two-third of these financial flows end up in developed countries (Kar, 2011). Figure 23 provides estimates for illicit capital outflows for Pakistan and Sri Lanka.

4.9. Debt moratoriums and concessional finance

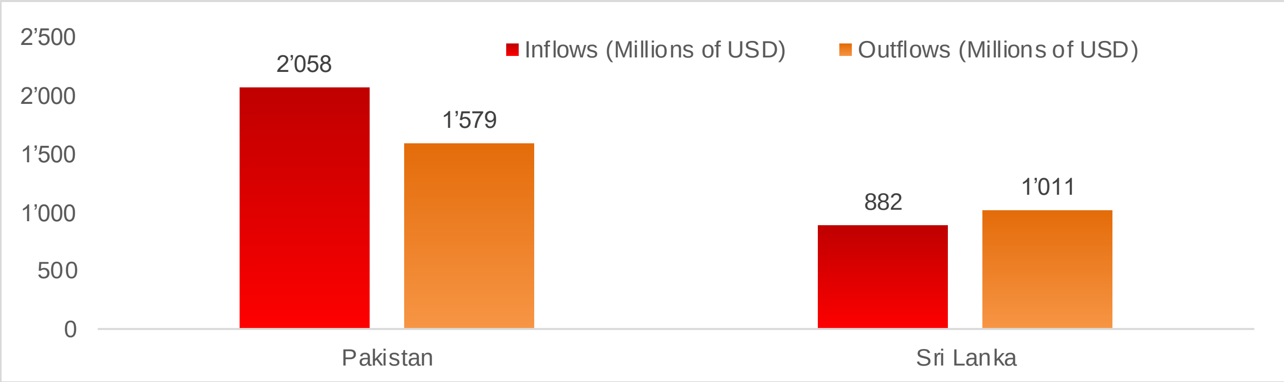
Shares of concessional sources of external finance such as the Paris Club in developing countries' debt stock is steadily decreasing and being replaced by more non-concessional forms of debt. Countries should look towards attaining concessional forms of finance with longer grace periods from official creditors to increase their debt sustainability. Pakistan's debt servicing obligations form almost 41% of this fiscal budget while Sri Lanka's debt obligations from Jan-Apr 2020 form almost 36% of its budget. This can give a perspective of the amount of resources tied with debt and how revising the debt management strategy and annual borrowing plan can ease fiscal conditions for a country.

4.10. Attracting financial capital inflows

Changes in the structure of debt of indebted countries in a fluid creditor landscape are exposing these countries to interest rate, exchange rate and rollover risks. With the share of non-concessional borrowing contributing to a larger share of debt than before has further placed countries face to face with external shocks and capital flow reversals.

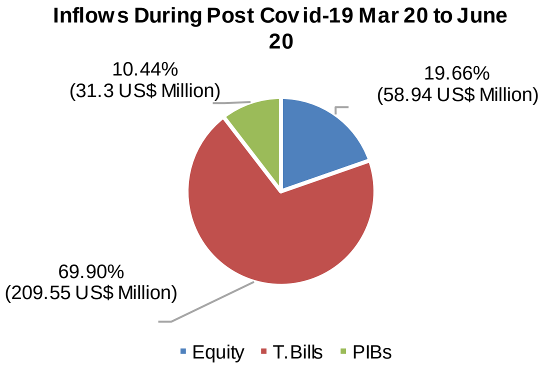
This is especially relevant for Pakistan where foreign investors have invested at least $200 million into Pakistan's rupee based 3-12-month Treasury bills (T-bills) in April 2020. The composition of inflows and outflows is shown below Figure 24, left and right side, respectively. It suggests that 69.90% of capital inflows to Pakistan over the period of 4 months went to short-term T-Bills. The share of capital inflows in private equity and PIBs is 19.66% and 10.44% of the total inflows, respectively (figure 24). The composition of outflows shows that 81.95% of total outflows were from T Bills. The remaining 18.05% is from Equity.

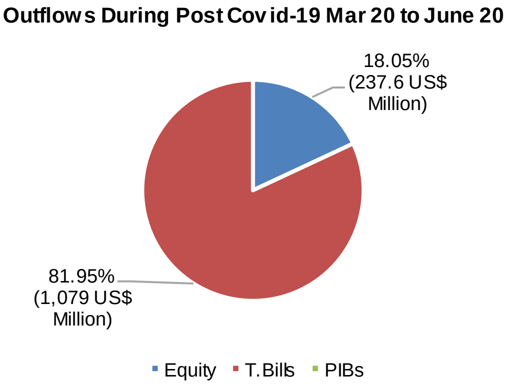
Figure 23: Comtrade-based estimates of potential trade mis-invoicing for the year 2015



Note: The respective mis-invoicing for Afghanistan are US$ 3 million and US$ 5 million. Broadening the tax base, maximizing compliance with a gradual shift from indirect to direct taxation, may help curb the outflows. This combined with strong regulatory oversight from central banks and other financial institutions as well as mandatory reporting of transactions that are suspicious of being illicit may make a sizeable difference.

Figure 24: Share of hot money inflows and outflows in Pakistan





Source: State Bank of Pakistan.

State contingent debt instruments that help countries preserve fiscal space in difficult times could also help generate more fiscal space. These instruments contain a trigger mechanism that can automatically defer debt service payments that are payable during a crisis of a specified type. Governments that are looking to restructure their debt have only utilized these bonds so far. The most recent example for these type of debt instruments is Barbados' Sovereign Debt Restructuring in 2018-19.

Other types of state-contingent bonds include GDP linked bonds that include the drafting of a term sheet (UNDESA, 2017). These bonds essentially have their cash flows linked to a country's national output. For GDP-linked bonds, servicing obligations grow larger when countries experience high growth and contract when economic conditions worsen. However, it is noteworthy that bonds that pay additional interest in conditions of strong growth have been issued while no bonds that risk the bondholder receiving less than baseline interest have yet been issued. Official creditors and financial institutions could potentially use such instruments to create additional fiscal space for debt distressed economies and help stabilize the debt to GDP ratio (Barr and others, 2014).

Debt swaps involve using funds occupied in debt servicing either for a social or environmental cause. Debt for nature swaps allows an international NGO to purchase external debt from a developing country at a discounted and offer it for cancellation in return for environment related action. These swaps were popular and relevant especially in the 1980s debt crisis (UN, 2012). These swaps could also be used to exchange debt for local currency government or donor organizations to finance projects in the indebted country. To date €200 million worth of debt has been swapped under this initiative (The Global Fund, 2017).

On 24 July 2020, Sri Lanka signed a $400 million currency swap with the Reserve Bank of India to boost its foreign reserves and maintain financial stability. This currency swap facility will be available with Sri Lanka till November 2022. There are further discussions to secure an additional $1 billion under a special bilateral swap arrangement (CBSL, 2020).

Likewise, an SDG debt swap programme that could support SDG related investments such as financing education, health, water, and sanitation etc. could be initiated. The process would be the same as for the debt for nature but the beneficiary countries would be required to deposit the debt service amounts from their previous creditors into an SDG investment fund or directly into a project or programme. (UNCTAD, 2019) It is also noteworthy that swaps as financing tools are politically attractive to donor countries and beneficial to recipient countries by way of cancelling external debt and funding development projects (Buckley, 20111). Afghanistan could aim for grant assistance towards SDGs by the same way.

SDG related concessional lending programmes would allow participating countries access to concessional finance to progressively repurchase the outstanding stock of external debt issued on commercial terms. This would increase the maturity profile of the debt swapped and lower the interest rate.

5. Priority areas for subregional or regional cooperation

The pandemic has triggered regional action to mitigate economic and social impacts. Regional policy coordination is critical to mitigate and isolate the pandemic shock. South Asia remains the least integrated region in the world due to geo-political undercurrents. According to the Asia-Pacific Regional Cooperation and Integration Index, evolution of regional integration has been largely steady over the years. However, the countries under analysis can build back better through regional cooperation on at least three fronts (figure 25).

5.1. Intra-regional trade

Intra-regional trade in South Asia contributes to only 5% to total trade of the region (World Bank, 2020). This has affected South Asia's economies. Pakistan currently has a Free Trade Agreement with Sri Lanka and a Pakistan Afghanistan Transit Trade Agreement (APTTA). Pakistan has a trade surplus to Sri Lanka but the APTTA has always been a bone of contention between Pakistan and Afghanistan. Pakistan claims most of its goods sent to Afghanistan are smuggled back into Pakistan causing a loss to the exchequer while Afghanistan states Pakistan changes rules frequently to hinder the trade.

Transport facilitation measures are required along with streamlined and automated border procedures (especially at borders with Afghanistan) to facilitate paperless transit transport systems. High container processing times (figure 26) are a result of complicated tariff regimes. Trade bodies need to provide a unified direction to this entire chain of processes to enhance facilitation and reduce trade costs.

Figure 25: Priority areas for regional cooperation

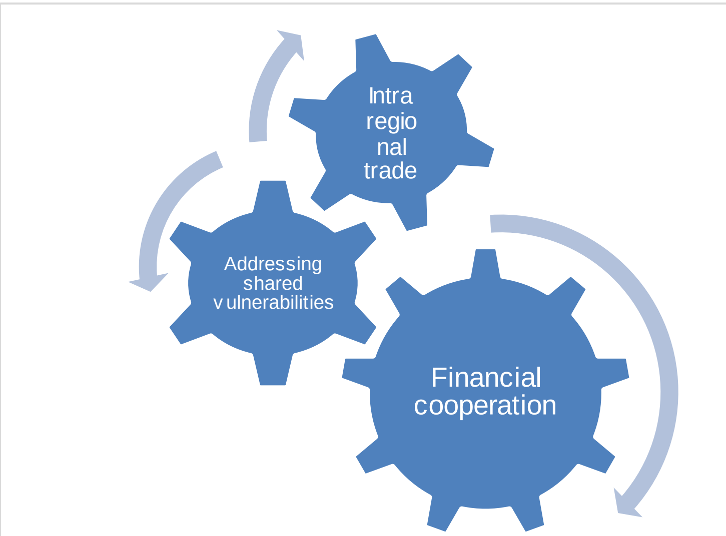
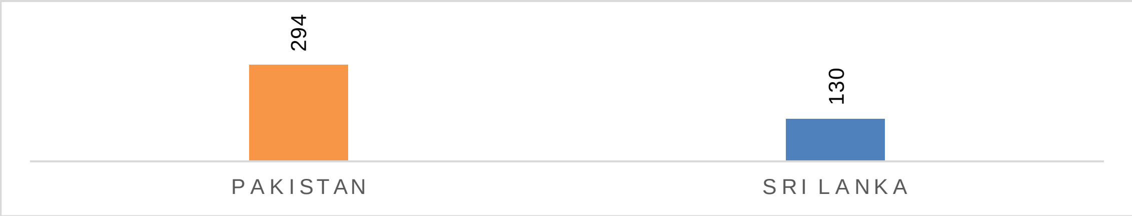


Figure 26: Hours to process container through customs



Source: Lopez-Acevedo and Robertson (2016).

5.2. Addressing shared vulnerabilities

According to the World Bank, 50% of the population of South Asia (more than 800 million people) has been affected by at least one natural disaster (World Bank, 2015). Agriculture and food security in the region recently have been threatened by both COVID-19 and locust swarms. SAARC can play a pivotal role in addressing food security. The SAARC Food Bank needs to be operationalized allowing the reserves to provide food security in times of crisis and food scarcity.

SAARC can be used to share knowledge and data between local and regional institutions on ways to mitigate climate change, multi-hazard early warning systems for disaster risk reduction and mainstreaming renewable energy initiatives. Regional action towards mitigation of climate change can be accelerated through the development of regional carbon markets (Saxena & Srivastava, 2020). Knowledge sharing can help pave the path to recover better.

5.3. Financial cooperation

SAARCFINANCE is a regional body composed of central bank governors and finance secretaries that aims to bring about economic reforms in member states through experience-sharing on economic and financial policies. However, SAARCFINANCE meetings have not been held since October 2018 mainly due to geopolitical tensions. Recent developments at high level political forums related to SAARC during the pandemic indicate that the platform can indeed be revived and is of utmost importance to the region.

SAARCFINANCE can play a pivotal role in the region especially during the current times and support a better recovery by building closer cooperation on macroeconomic policies of SAARC member states. The platform can help liberalize financial services, build a more efficient payment system mechanism and forge higher monetary and exchange cooperation. This can help in cutting the costs of cross border remittances and developing a SAARCFINANCE database.

The SAARC Swap arrangement facility needs to be more streamlined to address immediate liquidity issues of member states. Furthermore, the SAARC Development Fund should cooperate with other financial institutions to unlock more capital to fund regional infrastructure projects. The current capital base of $511.52 million is relatively small compared to the size of the region. The SAARC Development Fund could help provide funding toward social, economic or infrastructure projects to member states that are particularly hard-hit by the pandemic and are struggling to recover.

Recovery and rehabilitation in the aftermath of COVID-19 will take a long time, enough to create regional economic activities, financial cooperation, and support to MSMEs etc. The SAARC secretariat needs to be empowered to actively perform its role of facilitating these regional interests.

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