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Facing a Second Wave of COVID-19 in Sri Lanka: Economic Cost of a Lockdown Strategy

ASIA'S PATH FORWARD

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BACKGROUND

Sri Lanka is currently in the post-lockdown stage of the COVID-19 pandemic. Due to the surge in the number of infections in mid-March, the country was forced into a complete lockdown with all-day curfews-imposed island wide. The lockdown was in place for a period of nearly two months. Curfews were gradually eased with social distancing rules still in force.

As of 15 July 2020, 2665 cases have been reported, of which 653 were still active. The number of deaths officially attributed to COVID-19 was limited to 11. The lockdown was eased due to limited community spread, with few cases reported daily, mostly among repatriated citizens in quarantine centers. Since 9 July 2020, there has been a spike in the number of new cases with a new cluster developing in Kandakadu Rehabilitation Centre in the North Central Province with some initial evidence of community spread.

During the initial wave of COVID-19, Sri Lanka faced a two-pronged impact. The first impact was from the virus itself and its health effects on those infected and the costs of resources deployed to control the virus in the form of medical resources and quarantine centers. The second impact stemmed from the mitigation strategy adopted by the government. By implementing an elimination strategy using extensive indiscriminate curfews, the pandemic response had a substantial effect on livelihoods and the economy. Whilst the costs endured in meeting the first impact are largely unavoidable, the costs of the second are dependent on the chosen strategy.

At this stage, a second wave of the virus cannot be ruled out. Therefore, it is appropriate to draw insights from the response to the first wave to inform the policy response to a potential second wave. This article will examine the economic impact of the lockdown in terms of real GDP and suggest alternative ways to address a potential second major wave of infections.

Impacts on the Economy of a Lockdown

Sri Lanka was successful in controlling the spread of the first wave of infections in the community with a low death rate. However, the economic cost of the mitigation strategy was substantial.

The lockdown resulted in negative shocks in terms of supply and demand in the country. The inhibition of movement and workplace operation, along with disruption to the import supply chain resulted in a supply shock. Reduced income for daily wage workers and for many private sector employees, compounded by uncertainty of the outlook, resulted in a demand shock with lower consumer and business spending.

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Quantifying the Impact of the lockdown on GDP

Varying degrees of shocks were applied to each sector according to the estimated impact of the lockdowns on that sector. The official impact analysis tool established by the Department of Census and Statistics of Sri Lanka was used to calculate the resulting impact across sectors.[1] The impact of the lockdown was assessed in two scenarios: optimistic and pessimistic. In the pessimistic scenario, the level of negative shock is 50% higher than in the optimistic scenario. The optimistic scenario also assumes a positive recovery of 5% in non-essential manufacturing sector after the lockdown compared to the pessimistic scenario.

Sectors in which production or consumption is unviable due to lockdown rules, such as accommodation, food & beverage services, and transportation, are expected to have been the most adversely affected. Hence, during the lockdown, these sectors were expected to face a negative shock of 50% in the optimistic scenario and 75% in the pessimistic scenario. Sectors in which production or consumption is limited such as non-essential manufacturing, construction, and financial services are expected to face a moderate negative shock of 30% in the optimistic scenario and 45% in the pessimistic scenario. Sectors which were allowed to operate during the lockdown such as agriculture, and other essential manufacturing and services are estimated to face a lower negative shock of 10% in optimistic scenario and 15% in the pessimistic scenario. Although these sectors were allowed to operate throughout the lockdown, lower demand is still expected in these sectors due to limited mobility and income constraints of consumers. Sectors that are expected to experience a positive shock include manufacturing of cleaning materials.

[1] Impact Analysis Tool for the Sri Lankan Economy Using IO Table 2010. Accessed May 25, 2020. http://www.statistics.gov.lk/national_accounts/dcsna_r2/reports/sut2010/impact_analysis_tool.xlsx.

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Table 1: Shocks for various sectors during lockdown

High negative impact (-50% and -75%)	Medium negative impact (-45% and -30%)	Low negative impact (-10% and -15%)	No Impact	Positive Impact (+30%)
Transportation	Non-essential manufacturing	Agriculture	Health services	Manufacture of cleaning materials including soap
Accommodation	Construction	Manufacturing of essential goods	Public Administration	
Food & Beverages	Financial Service	Courier services	Broadcasting Services	
	Real Estate	Rent and lease activities	Energy generation and water supply	
	Other Services	Education	Research and Development	
		Entertainment	Manufacture of Pharmaceuticals	
		Legal and Accounting activities		
		Insurance and pension funds		

Even in the post-lockdown stage, there are certain sectors which may face a prolonged shock. These include accommodation (tourism sector), construction, transportation, and trade. There are also certain sectors, particularly among non-essential manufacturing, which may see increased production in the post lockdown stage as production was subdued in the lockdown stage. These impacts have also been considered in the GDP calculation for the second half of the year.

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Table 2: Shocks for various sectors after lockdown

Sector	Magnitude of Shock
Accommodation	-50%
Construction	-15%
Transportation	-5%
Trade	-5%
Non-essential manufacturing	(+5% optimistic, 0% pessimistic)
Other Sectors	0%

The analysis indicates that, considering a baseline growth of 3.75% (annual average growth during the last 5 years) during the period of lockdown, the overall impact to GDP is negative 24% in the optimistic scenario and negative 39% in the pessimistic scenario. In other words, if the lockdown lasted for an entire year, GDP would contract between 24% and 39%

In the case of the first wave in Sri Lanka, the lockdown lasted for 60 days: 10 days in March, 30 days in April and 10 days in May. Therefore, based on available data, the annual real GDP for 2020 is expected to be negative 2.4% in the optimistic scenario and negative 6.4% in the pessimistic scenario. A negative 2.4% GDP would be the worst economic growth contraction in Sri Lanka's post-independence history. These GDP estimates would change if there are additional lockdowns or other significant shifts in the second half of the year.

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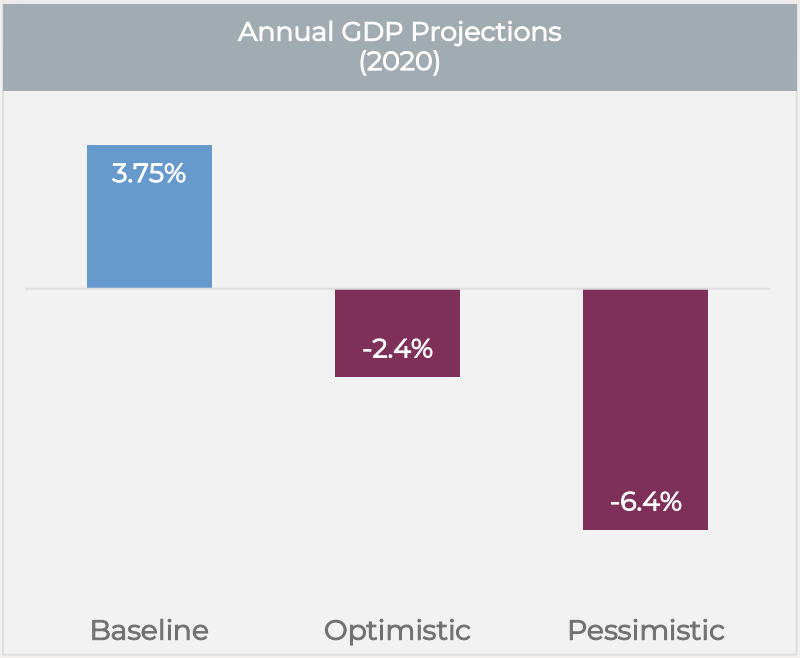
Figure 1: Projection of annual real GDP growth in 2020



Source: CBSL data[2] and Author's own calculation

Facing a Second Wave?

The choice of COVID-19 mitigation strategies has important implications for the overall wellbeing of communities in an affected country. Particularly for developing countries like Sri Lanka, with large proportions of vulnerable communities reliant on the informal economy and daily wages, the adverse economic impact of curfew-type mitigation strategies could be more severe than the impact of the disease.

Unemployment in the first quarter of 2020 reached an eleven-year high of 5.7% even before the full impact of curfews set in, in Sri Lanka. Based on the GDP contraction estimates of the current analysis the unemployment levels are expected to increase further in the course of the year.[3] Given the high impact of curfew-type mitigation on GDP and employment, it would be advisable to evaluate such

[2] Sri Lanka. Central Bank of Sri Lanka. *Annual Report.* Accessed June 25, 2020. https://www.cbsl.gov.lk/en/publications/economic-and-financial-reports/annual-reports/annual-report-2019.

[3] De Mel, Nishan., and Perera, Mihindu. "Impact of COVID-19 mitigation on unemployment in Sri Lanka". Forthcoming.

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mitigation strategies against other non-pharmaceutical mitigation strategies for GDP and employment impact to inform the decision making process.[4]

Such mitigation strategies could include more intensive testing, better quarantine arrangements, increasing healthcare capacity, and behavioral incentives for social distancing and good hygiene within communities.

Mitigation strategies can also be more targeted, for instance, by focusing exposure restrictions to the most vulnerable groups. The available global death data on COVID-19 based on age groups suggests that 98.7% of deaths occur in people above the age of 50. Only 1.3% of deaths are below the age of 50.[5] Therefore, targeting escalated mitigation strategies to people above the age of 50 or those with respiratory illness and other pre-existing conditions would be a possible method for containing the negative impact on GDP and employment, while continuing to contain the negative impact from the spread of COVID-19.

[4] Loayza, Norman V., and Steven Pennings. "Macroeconomic Policy in the Time of COVID-19." 2020. doi:10.1596/33540.

[5] Distribution of Coronavirus (COVID-19) Deaths in Italy as of May 7, 2020, by Age Group. Accessed March 11, 2020. https://www.statista.com/statistics/1106367/coronavirus-deaths-distribution-by-age-group-italy/. Data for China as of 11 February 2020,

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Distribution of Coronavirus (COVID-19) Deaths in Germany as of May 8, 2020, by Age Group. Accessed March 11, 2020 https://www.statista.com/statistics/1105512/coronavirus-COVID-19-deaths-by-gender-germany/.

Distribution of Coronavirus (COVID-19) Deaths in Spain as of May 12, 2020, by Age Group. Accessed March 11, 2020https://www.mscbs.gob.es/profesionales/saludPublica/ccayes/alertasActual/nCov-China/documentos/Actualizacion_103_COVID-19.pdf.

Distribution of Coronavirus (COVID-19) Deaths in South Korea as of May 8, 2020, by Age Group. Accessed March 11, 2020 https://www.statista.com/statistics/1105080/south-korea-coronavirus-deaths-by-age/.

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Deshal de Mel is an economist who has experience across government, private sector, and academia. He served as Economic Advisor to the Ministry of Finance of Sri Lanka from 2017 till 2019, working on tax reforms and other public finance matters. He was also a member of the National Trade Negotiation Committee where he led negotiations on trade in services completing Sri Lanka's first bilateral trade in services agreement with Singapore. He previously worked in the corporate sector as Senior Economist at the Hayleys Group, one of Sri Lanka's largest diversified conglomerates. He has served on a number of corporate and non-corporate boards, including at present Sampath Bank PLC, and previously Sri Lankan Airlines, Sri Lankan Catering, and the Centre for Poverty Analysis. He was also a Commissioner at the Securities & Exchange Commission of Sri Lanka in 2018-2019. He has a degree in Philosophy, Political Science, and Economics from the University of Oxford and a Masters in International Political Economy from the London School of Economics. He was recognized by the World Economic Forum as a Young Global Leader in 2019.

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