SPECIAL REPORT

NO. 500 | AUGUST 2021 UNITED STATES INSTITUTE OF PEACE www.usip.org

The Impact of COVID-19 on South Asian Economies

By Uzair Younus

Workers sanitize the interior of a shopping mall in New Delhi, India, on June 6, 2021. (Photo by Atul Loke/New York Times)

Contents

Summary

- The COVID-19 pandemic has pushed millions of households into poverty and substantially increased income and wealth inequality in India, Bangladesh, and Pakistan. This situation poses a serious near-term challenge for policymakers, especially since rising food and commodity prices compound economic insecurities.
- Narendra Modi's government in India pursued pro-growth reforms in 2020, but a dramatic second wave of COVID-19 cases beginning in April 2021 not only caused emotional and socioeconomic trauma but created serious economic headwinds.
- A slow recovery in export earnings poses challenges for Sheikh Hasina's government in Bangladesh. The country is likely to remain economically and politically stable, however, and a return to high levels of economic growth is likely in 2022 and beyond.
- Pakistan managed to minimize the economic fallout of the pandemic in part through an early reopening of the economy, but will face significant challenges to robust growth because of long-standing structural issues in the economy.
- Failure to ensure equitable recovery could generate social and political instability and lead to heavy-handed responses from governments that in recent years have become less tolerant of dissenting voices.

United States Institute of Peace
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NO. 500 | AUGUST 2021

ECONOMICS & ENVIRONMENT

ABOUT THE REPORT

This report examines the impact of the coronavirus pandemic on Bangladesh, India, and Pakistan, highlighting the social and economic costs on each country's economy and underscoring the risk of political upheaval if the recovery is slow or unequal. The report is based on a research project funded by the United States Institute of Peace's Asia Center to assess the political and economic implications of the pandemic in South Asia.

ABOUT THE AUTHOR

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Special Report No. 500. First published 2021.

ISBN: 978-1-60127-865-4

UNITED STATES
INSTITUTE OF PEACE PRESS

One teacher checks a student's temperature while another dispenses hand sanitizer to help prevent the spread of COVID-19 as students arrive at their school in Peshawar, Pakistan, on April 19, 2021. (Photo by Muhammad Sajjad/AP)

Introduction

Home to more than one-fifth of the world's population, India, Bangladesh, and Pakistan are facing their most serious economic and public health crisis in recent years. The COVID-19 pandemic brought both the formal and informal economies in the region to a grinding halt. Lockdowns in each country created mass unemployment, pushing millions of households below the poverty line. And while each of the countries responded with fiscal and monetary stimulus programs, the breadth and depth of the economic crisis suggests that it will take many months, if not years, for the majority of households to recover.

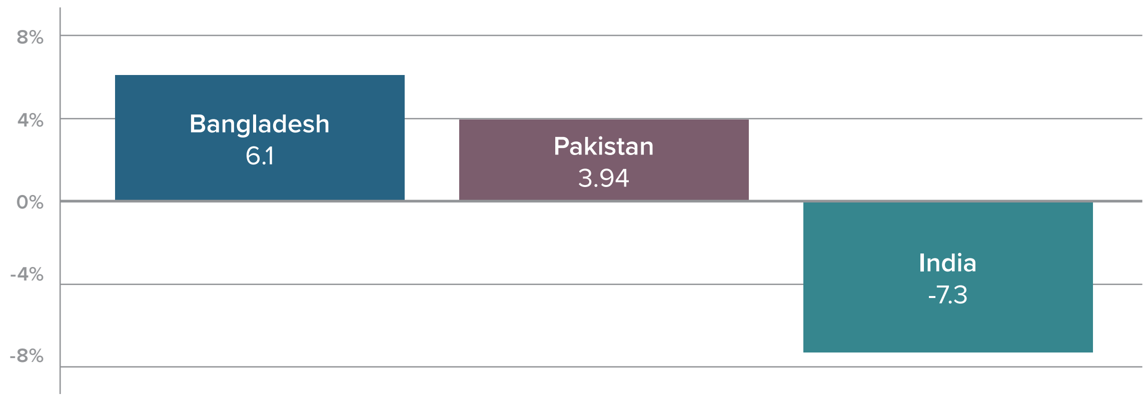
Each country has initiated mass vaccination programs and reopened their economies, but a second wave of infections that began in April 2021 forced policymakers to place new restrictions on social and economic activities. This resurgence of COVID-19 has put the region's nascent economic recovery in serious jeopardy, particularly in India where a significant spike in daily cases and deaths has created perhaps the most serious crisis the country has faced since the partition of the subcontinent in 1947.

The near-term challenge for the region's policymakers will be to accelerate their vaccination programs, minimizing the likelihood of a third wave of infections and lessening the need for new restrictions and lockdowns, and to work toward an economic recovery that uplifts the majority of households, not just a privileged minority. Failure to ensure an equitable recovery could generate social and political instability and lead to heavy-handed responses from governments that in recent years have become increasingly authoritarian and less tolerant of dissenting voices.

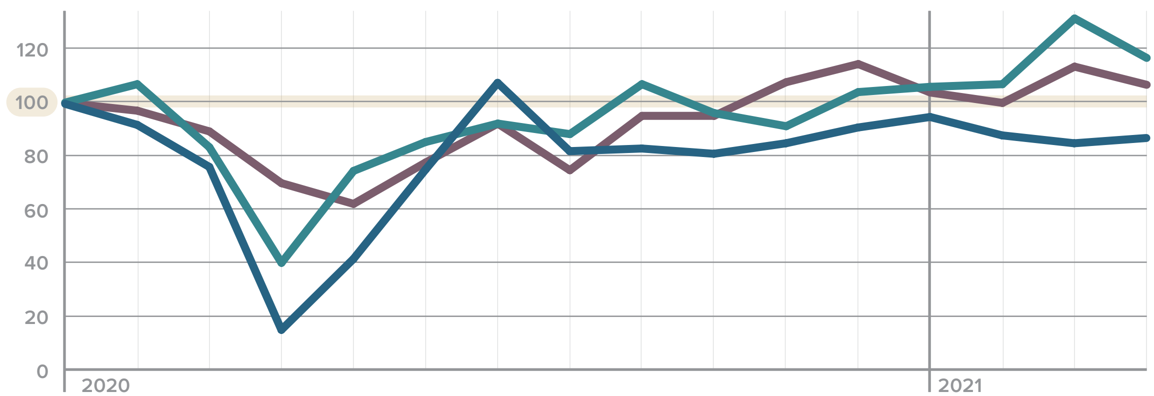
Major Economic Indicators

Bangladesh India Pakistan

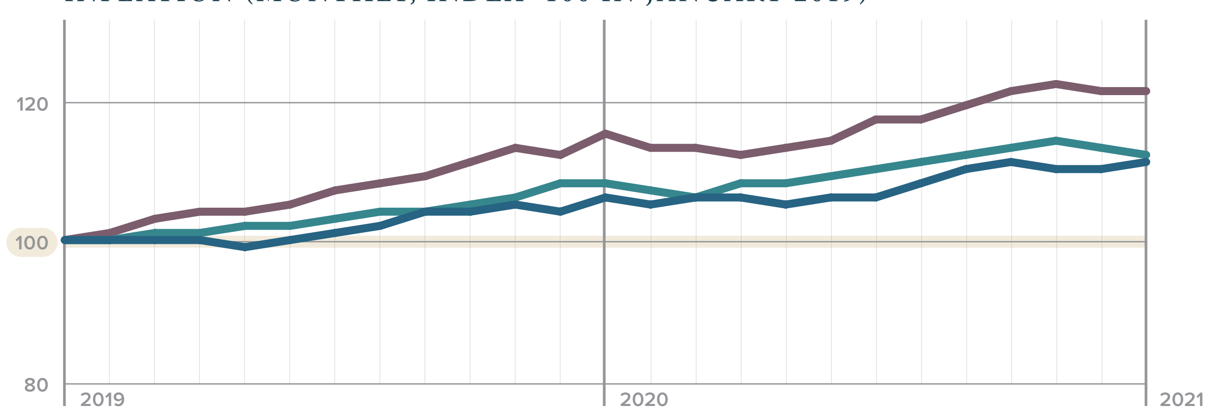
GDP GROWTH FOR FISCAL YEAR 2020–21 (PERCENTAGE)



EXPORTS (MONTHLY, INDEX=100 IN JANUARY 2020)



INFLATION (MONTHLY, INDEX=100 IN JANUARY 2019)



Sources: GDP growth data from each country's finance ministry; export and inflation data from Pakistan Bureau of Statistics, Press Information Bureau (India), and Bangladesh Bureau of Statistics.

This report reviews the economic environment in South Asia's three largest economies at the onset of the pandemic and how policymakers responded to the economic impact of COVID-19. It then analyzes the countries' prospects for an economic recovery in 2021 and beyond, and discusses how their bilateral economic relations with the United States can be deepened to generate an equitable and inclusive post-pandemic recovery.

India

On May 23, 2019, the National Democratic Alliance, led by Prime Minister Narendra Modi of the Bharatiya Janata Party (BJP), won a resounding electoral victory, giving India's second-term prime minister a broader mandate to rule. Almost immediately, the Modi government began to implement aspects of its right-wing social agenda. On August 5, 2019, the government revoked the statehood and semiautonomous standing given to Indian-administered Jammu and Kashmir; and on December 12, 2019, it pushed a controversial Citizenship Amendment Bill through parliament, which critics have said will disenfranchise millions of Muslim citizens.[1]

Modi's focus on political issues, however, left serious economic concerns unaddressed. After sustaining high rates of economic growth for years, India's economy was showing clear signs of weakness in 2019. Economic growth had fallen from 8.3 percent in 2016 to 4 percent in 2019. As growth slowed, youth unemployment reached highs not seen in decades, and private sector investment stagnated.[2] Two key economic events exacerbated India's economic slowdown: demonetization and a complicated rollout of the Goods and Services Tax. On November 8, 2016, the government had announced that to "break the grip of corruption and black money," 500- and 1,000-rupee banknotes would be taken out of circulation.[3] This drastic action sucked liquidity out of the economy—almost 90 percent of cash in circulation was removed overnight—leading to shortages of cash and long lines at bank branches. The Goods and Services Tax, implemented on July 1, 2017, was a major reform that eliminated a complicated and cumbersome tax system with a simpler, uniform tax code. The tax, however, increased the cost of goods and services across the economy, and its complicated tiered system led to increased friction in the economy and tensions between the central and state governments.[4]

EARLY IMPACT OF THE PANDEMIC

On January 30, 2020, India reported its first domestic case of COVID-19.[5] Just two months later, on March 23, Modi ordered a national lockdown that shuttered all nonessential businesses and activities for twenty-one days.[6] Modi's announcement gave citizens only a few hours to plan for the lockdown, the world's largest. To varying degrees, the Indian economy would remain in lockdown till January 1, 2021. Despite these measures, India became one of the worst-hit countries in the world, reporting more than four hundred thousand cases of COVID-19 by the summer of 2020. Economic activity collapsed, with unemployment rising from around 8 percent in mid-March 2020 to 23.4 percent by the first week of April.[7] Both manufacturing and services activities were hard hit, with the services industry collapsing by almost 90 percent in April.[8]

A health worker takes a nasal swab sample to test for COVID-19 in Guwahati, India on July 16, 2021. (Photo by Anupam Nath/AP)

In response to the economic fallout of the lockdowns, the prime minister announced a $260 billion stimulus package on May 12.[9] According to the International Monetary Fund (IMF), the amount of new spending on social protection measures and health care amounted to just 1.8 percent of GDP.[10] The limited scope of the response was driven by a desire to maintain fiscal prudence. This decision did not have the intended effect, however: Moody's downgraded India's credit rating in June, noting that "the pandemic had amplified vulnerabilities in India's credit profile that were present and building prior to the shock."[11] In November, a Reserve Bank of India report revealed that the economy had likely "entered a technical recession in the first half of [the 2020–21 fiscal year] for the first time in its history" with two successive quarters of negative growth.[12]

In response to the crisis, the government announced additional stimulus measures in October and November 2020.[13] These measures included plans to increase capital expenditures, provide interest-free loans to states to shore up their finances, and create production-linked incentives for priority sectors. Announcing the package, Finance Minister Nirmala Sitharaman said that "India's economy is seeing a strong recovery." Yet by the end of 2020, India's economy had shrunk by 23.9 percent in the April to June quarter (the first of the 2020–21 fiscal year), and annual economic growth estimates were revised downward, with Goldman Sachs estimating that the economy would contract by 5 percent over the course of the fiscal year.[14] This decline in growth was mainly driven by the national scale of the lockdown, which brought economic activity in both the formal and informal sectors to a grinding halt.

In addition to the stimulus packages, the government used the crisis as an opportunity to push much-needed economic reforms. Production-linked incentives had the intended effect of catalyzing new investments in priority sectors, with companies like Apple and Samsung announcing they were shifting production to the country.[15] Central and state governments also pushed through changes to labor laws, giving the private sector greater discretion to hire and fire workers.[16] As part of these reform efforts, Modi pivoted to a new vision for economic growth and recovery. The initial stimulus announcement in May 2020 drew attention to this new program, dubbed the Self-Reliant India Scheme (Atmanirbhar Bharat Abhiyan), which set a goal of helping millions of small businesses across the country expand and included a $9.3 billion fund to support them during the pandemic.[17] Although the vision sought to accelerate India's integration into global supply chains, it also led the government to impose additional tariffs and trade barriers on imports to protect domestic businesses.[18]

One of the biggest reform efforts focused on reducing the government's role in the agriculture sector. For decades, India's farmers have sold products such as rice and wheat through government-run markets. High minimum support prices for these products led to oversupply, with the government doling out billions of dollars annually to absorb the excess stock. Although domestic and international analysts lauded the reforms, they were greeted with derision by India's farmers, who feared that over time the government would do away with minimum support prices, leaving them at the mercy of market forces.[19] Protests erupted across the country, with farmers descending on Delhi in order to force the government to repeal the farm laws. The Modi government held talks with the protesting farmers, but at the same time suggested they were a front for anti-national elements affiliated with Pakistan and the Sikh separatist Khalistani movement.[20] The allegations backfired, fueling further anger among the protesting farmers. In January 2021, roughly five months after the protests began, the Supreme Court ordered the suspension of the laws after talks between the government and the farmers deadlocked. The government countered by proposing an eighteen-month delay in implementing the laws, a signal that it was open to rolling back the reforms.[21] This gesture did little to break the impasse, however, with farmers vowing to hold a major protest rally in New Delhi on India's Republic Day, January 26. These protests turned violent, with some protesters overwhelming security forces to breach the capital's Red Fort, a symbol of India's independence.[22]

If the protests continue and the risk of further violence rises, it is likely that the government will back down and bring an end to this latest round of reforms. With the economy requiring bigger and bolder reforms, however, an early end to the reform cycle will likely hinder India's post-pandemic recovery.

PROSPECTS FOR 2021

The easing of the lockdown catalyzed growth, with pent-up demand driving a strong recovery. After nine consecutive months of decline, the country's year-on-year imports grew by 7.6 percent in December 2020; collection of the Goods and Services Tax in December 2020 reached a record high, growing by 12 percent compared to December 2019.[23] In the early months of 2021, the overall impact of the government's stimulus packages and the reopening of the economy was positive. Economic activity sharply rebounded and the unemployment rate declined to under 7 percent, returning to pre-pandemic levels.[24] The announcement of the budget for the 2021–22 fiscal year, with significantly higher spending on health care and infrastructure investments, further stoked optimism. The budget also contained inducements for attracting foreign direct investment to key sectors, outlined over $25 billion in production-linked incentives to increase its exports, and set goals for privatizing state-owned assets to raise additional funds.[25]

This momentum led experts to argue that India would be the world's fastest-growing major economy in 2021, with growth expected to hit close to 10 percent. International companies were also bullish: in a December 2020 announcement, Walmart committed to growing its sourcing footprint in India and purchase over $10 billion of goods annually.[26] Other US companies were expected to follow suit as they shifted supply chains away from China.

By April 2021, however, a devastating second wave of the pandemic caused confirmed new cases of COVID-19 to exceed four hundred thousand a day, while coronavirus-related deaths, reported to be grossly undercounted, rose to four thousand per day.[27] The crisis was so devastating, and the government's response so inadequate, that one expert argued that India had "transitioned to a failed State."[28] Oxygen shortages were reported across the country, the health-care system virtually collapsed, crematoriums ran out of space, and bodies were seen floating in rivers.

The resurgence of COVID-19 in April and May of 2021 upended India's nascent recovery, eroding economic optimism and forcing the central bank to cut its growth target for the 2021–22 fiscal year from 10.5 percent to 9.5 percent.[29] This decline in expectations came after data showed that India's economy contracted by 7.3 percent in the 2020–21 fiscal year.[30] While India has led the way on the subcontinent in terms of vaccine rollout, the Modi government's failure to control the devastating resurgence of the pandemic has led analysts to conclude that India will continue to face economic headwinds for the foreseeable future.[31]

The human and economic toll of the pandemic are rapidly eroding Modi's political standing. Uttar Pradesh, the country's most populous state and a bastion of the BJP, is slated to have elections in 2022, and the ongoing crisis may further incentivize the BJP to double down on its right-wing social agenda in order to rally the party's base. Such an outcome, especially if it distracted the government from focusing on its vaccine rollout and pro-growth economic reforms, could in turn lead to more protests and violence, particularly against the country's Muslim population.

Bangladesh

In recent years, economic development has lifted millions of Bangladeshi citizens out of poverty and led to marked improvements in life expectancy and literacy levels. Bangladesh's GDP per capita, which was about 40 percent lower than Pakistan's in 1971, is now about 40 percent higher, and the country has positioned itself as an attractive destination for foreign companies looking to tap into its middle class of 30 million people. As a result, in the two years before the pandemic, total investment in Bangladesh set records of 31.2 percent of GDP in 2018 and 31.6 percent of GDP in 2019.[32] In 2019, the economy grew by 8.2 percent—making it the fastest-growing economy in South Asia and the subcontinent's second-largest economy (after India)—and the Asian Development Bank projected growth rates of 7.8 percent in 2020 and 8 percent in 2021.[33]

Prime Minister Sheikh Hasina, who has led the country for seventeen of the last twenty-five years, set a goal of making Bangladesh a "high-value, knowledge-intensive society" with a diversified industrial and export base.[34] To achieve this goal, the country has built on its investments in human capital to develop its information technology sector. This diversification drive led to investments in manufacturing smartphones for exports, with the country's electronics conglomerate Walton planning to begin exporting "Made in Bangladesh" smartphones to the United States.[35]

Despite Hasina's increasing focus on the tech sector, the primary driver of Bangladesh's recent growth has been the export of ready-made garments, which account for over 80 percent of the country's export mix.[36] With strong demand for these products in Europe and the United States, Bangladesh's economy has stayed on track to sustain its growth trajectory.

On the political front, Hasina has consolidated her party's control over the political system. In the 2018 elections, Hasina's Awami League won 288 of 300 seats in parliament.[37] Opposition

Volunteers from Bidyanondo Foundation assemble care packages for COVID-19 patients in Dhaka, Bangladesh on June 6, 2020. (Photo by Al-emrun Garjon/AP)

leaders, however, called the election result "farcical." The largest opposition party, the Bangladesh National Party, alleged that it faced "violent attacks and intimidation, including shootings and arrests, that have stunted their ability to campaign."[38] The US State Department also expressed concerns, decrying Bangladesh's "inability to grant credentials and issue visas within the timeframe necessary" to accommodate an international observer mission.[39] The elections were also marred by violence, with at least seventeen people dying in clashes between Awami supporters and the opposition.[40] While the authoritarian bent of Hasina's government has led to criticism from international observers and human rights groups, the overall political environment was stable before the onset of the pandemic; international criticism about the elections was also muted.[41]

EARLY IMPACT OF THE PANDEMIC

The pandemic hit Bangladesh at a time when its economic and human development outlook was extremely positive. Shortly after the first confirmed case of COVID-19 was reported on March 8, 2020, Hasina's government imposed a strict lockdown beginning on March 26.[42] By the end of the month, over $6 billion in export orders had been cancelled, with the president of the Bangladesh Garment Manufacturers and Exporters Association calling the situation "apocalyptic."[43] In April, over a million workers in the country's garment sector had been laid off as export orders plummeted by over 80 percent.

The closure of markets across the country hurt workers in the informal sector as well, with daily wage earners facing a catastrophic loss of income.[44] The spread of the virus increased as migrant workers returned home, including many from hard-hit Italy. In March, remittances dropped to $1.29 billion, registering a year-on-year decline of 13.3 percent. The World Bank forecast that remittance inflows—an important source of income for Bangladeshi households—would decline by 25 percent in 2020.[45] On May 26, Hasina announced that the lockdown would be relaxed starting May 31. However, rising cases forced the government to reimpose lockdowns in at least ten of the country's sixty-four districts in June.[46] The proliferation of new cases also strained the country's health-care system: by the end of June, at least forty-two doctors in Bangladesh had died from the virus.[47]

According to the IMF, the Bangladeshi economy grew by 3.8 percent in 2020, making it one of the few major countries in the world to register a positive growth rate during the pandemic.

Just two weeks after the initial lockdown in late March, Hasina announced an $8.6 billion stimulus package, amounting to about 2.5 percent of the country's GDP.[48] The package included low-cost loans to small businesses, large industrial units, and services companies; expansion of the food security and social protection programs; and disbursement of credit to the agriculture sector. Multilateral donors also provided support to the government during the early months: the World Bank approved $1 billion in funding to help the government meet the economic challenge. As with Pakistan, the IMF approved a $732 million disbursement for Bangladesh to "help finance the health, social protection, and macroeconomic stabilization measures" in the country, and the Asian Development Bank provided $500 million to "speed up the country's social and economic recovery." Despite these measures, the situation continued to look bleak: early assessments forecast that Bangladesh's poverty rate would double to around 40 percent.[49]

Following the end of the lockdown, the economy began to recover quickly. Beximco, Bangladesh's largest conglomerate, exported 6.5 million units of personal protective equipment to the United States, highlighting the resiliency and adaptability of the country's textiles industry. Contrary to the World Bank's prediction that remittances would fall precipitously, the economy experienced a record inflow in 2020, reaching $21.9 billion.[50] The sharp uptick in remittances, not just in Bangladesh but across South Asia and much of the world, suggest that earlier assessments had underestimated the breadth of informal money flows, particularly through international travel routes. Exports, which experienced huge drops in March and April, began to pick up in the summer, with the country's garment sector shipping over $1.5 billion in exports in the first three weeks of July.[51] Although exports remain below pre-pandemic levels, it is now expected that the vaccine rollout in the European Union and the United States will bolster demand for Bangladeshi exports in the second half of 2021.

PROSPECTS FOR 2021

According to the IMF, the Bangladeshi economy grew by 3.8 percent in 2020, making it one of the few major countries in the world to register a positive growth rate during the pandemic. Bangladesh's growth was largely the result of two decisions—reversing course on the lockdown after just two months, and government spending that spurred domestic demand, which proved vital when export orders dried up. Despite rising COVID-19 case counts, large infrastructure projects, including the Padma Bridge, are expected to be completed in the coming months, further bolstering growth prospects. The country also approved its eighth Five-Year Plan in December, committing to maintaining growth rates of over 8 percent in the coming years.[52]

For Bangladesh, the immediate economic concern is to recover the output lost during the early months of the pandemic. Bangladesh's poverty rate doubled as a result of the pandemic, rising from 21.6 percent in 2018 to 42 percent in 2020, and extreme poverty nearly tripled, climbing from 9.4 percent in 2018 to 28.5 percent in 2020.[53] To catalyze growth and create jobs in the near term and boost the long-term capacity required to sustain the high rates of economic growth envisioned by the government, Bangladesh will need to diversify its economy away from ready-made garment exports by prudently using its fiscal capacity to invest in next-generation infrastructure and industries. This shift is especially important as Bangladesh graduates from Least Developed

Country status and loses many preferential economic benefits. Seventy percent of Bangladeshi exports currently receive preferential market access, and according to the World Trade Organization, the change in status could lead to a 14 percent decline in exports.[54] The government has already started to move forward on export diversification plans, with companies like Samsung signaling a desire to expand its smartphone assembly operations there.[55] Sectors such as shipbuilding, in which the government has set a $4 billion export target, are also growing.[56]

The response to the pandemic will require a committed vaccination program from trusted sources. The government signed a deal to purchase thirty million doses of the AstraZeneca vaccine from India's Serum Institute (along with two million doses donated by India) and an additional sixty-eight million doses from the Gavi vaccine alliance, but rising cases in India in the first half of 2021 delayed their shipment, forcing the Hasina government to seek supplies from China.[57] Still another point of risk is the government's own credibility. During the early days of the pandemic, the Hasina government was embroiled in a scandal involving the sale of falsified COVID-19 testing certificates required for international travel. The government responded to this criticism by fining airlines that brought in passengers without COVID-19 clearances.[58] It also reshuffled the health department and adopted a tough approach against officials who undermined the COVID-19 response. Given concerns over corruption, it is important for the government to ensure an equal economic recovery that benefits citizens most severely impacted by the pandemic.

Pakistan

As Prime Minister Imran Khan's government took over in August 2018, Pakistan's economy was in dire straits. With both a budget shortfall and a massive trade imbalance, the country faced a twin-deficit crisis. Yet in the early days of the Khan administration, many Pakistani policymakers believed that bilateral inflows from China, Saudi Arabia, and the United Arab Emirates would help the country weather the storm and allow it to avoid going to the IMF for yet another bailout. All three countries pledged support, with Saudi Arabia providing a total of $6 billion in financial assistance.[59] Pakistan's "all-weather ally," China, also stepped in, providing a critical $2 billion loan to boost its foreign exchange reserves.[60] At the same time, the State Bank of Pakistan ended its policy of propping up the rupee, allowing the currency to devalue sharply and providing a boost to exports.

Hopes of avoiding the IMF soon fizzled as the severity of the economic crisis became clear in Islamabad. On July 3, 2019, the IMF approved a $6 billion bailout to put "Pakistan's economy on the path of sustainable and balanced growth."[61] To control inflation (a key precondition of the IMF bailout) and to attract vital foreign currency flows, the central bank raised interest rates to 13.25 percent—a policy decision that was widely criticized by the opposition as well as independent economists, who argued that inflation in Pakistan, a cash-dependent economy, could not be tamed by higher interest rates.

The economic crisis and the subsequent bailout led to a sharp decline in growth and rapid uptick in inflation, which hit 11.4 percent in September. The inflationary pressures were a direct result of the sharp devaluation of the currency, which led to an increase in the prices of essential commodities and energy inputs. The State Bank maintained interest rates at 13.25 percent, however; and the stabilization policies quickly led to an improvement in Pakistan's current account deficit, which fell by almost 75 percent in the July–September quarter of the 2019 fiscal year to $1.5 billion.[62]

EARLY IMPACT OF THE PANDEMIC

On February 26, 2020, Pakistan confirmed its first two cases of COVID-19.[63] The pandemic could not have come at a worse time: the economy was growing at a tepid rate, jobs were hard to come by, and high inflation continued to erode the purchasing power of millions of households. As the case count grew, fear that the virus would spread rapidly across the country led to a vociferous "lockdown versus livelihoods" debate. Khan made a public case for protecting livelihoods and argued against a countrywide lockdown.[64] Nevertheless, provincial governments began to issue their own lockdown orders, shutting down all nonessential businesses. The enforcement of these orders brought Pakistan's economy to a standstill by the end of March.[65]

Early estimates predicted that the economy would lose between 12 and 18 million jobs during the lockdown.[66] The World Bank predicted that the country would enter its first recession in decades.[67] Consequently, on March 24, 2020, Khan announced a stimulus package to prop up the economy and pave the way for a quick recovery. Totaling Rs. 1.2 trillion (about 3 percent of GDP), the stimulus included a Rs. 200 billion fund to protect laborers, Rs. 150 billion to expand the country's existing cash transfer program to poor families, and another Rs. 100 billion for pandemic-related emergencies.[68]

The biggest success of the stimulus was the rapid expansion of the country's cash transfer mechanism. More than 15 million families received funds through the program, ensuring that millions of citizens did not fall into extreme poverty.[69] The State Bank also played a key role in supporting the economy, extending credit to small- and medium-sized businesses and protecting millions of jobs in the formal economy. The cumulative support provided by the central bank reached Rs. 1.3 trillion by October 2020.[70] It also sharply cut interest rates from 13.25 percent to 9 percent in April 2020, and pushed them down to 7 percent by the end of June.[71]

As its domestic economy struggled, Pakistan had to pause its $6 billion fiscal stabilization program (which had started in 2019) and seek emergency relief from the IMF. By mid-April, the IMF also approved a $1.39 billion loan to alleviate the economic pain from the pandemic.[72] In the following months, the World Bank provided $505 million in low-interest, soft loans; the Asian Development Bank approved a $500 million emergency loan; and the Asian Infrastructure Investment Bank approved a $250 million loan. Nevertheless, by December 2020, debt relief program talks with the IMF stalled as the Khan government resisted the demands and restrictions posed by the IMF. These included demands to increase energy tariffs and to sustainably reduce debt in the power sector, among others.

Although Pakistan's domestic politics were intensely polarized during this period (for example, in September 2020 several opposition parties came together to form the Pakistan Democratic Movement [PDM], which vowed to overthrow the government), provincial governments continued to cooperate with the federal government to respond to the pandemic. This coordination occurred through the National Command Operation Center (NCOC). The effectiveness of the NCOC (together with other factors, such as the young age structure of Pakistan's population) meant that the virus did not spread as quickly as anticipated, allowing provincial governments to end their lockdowns relatively early. Primed by the government's and central bank's timely and targeted fiscal and monetary support, post-lockdown economic activity had gained momentum by the end of 2020. Although the country saw a decline in export earnings in the early months of the pandemic, a quick end to the lockdowns allowed exporters to fill new orders from international suppliers dealing with supply-chain shocks.[73]

Government employees wait to receive the Convidecia COVID-19 vaccine at Nishtar Hall, an entertainment venue, in Peshawar, Pakistan, on June 11, 2021. (Photo by Muhammad Sajjad/AP)

PROSPECTS FOR 2021

There is clear evidence that economic momentum is building in Pakistan, with the economy projected to have grown by almost 4 percent for the 2020–21 fiscal year.[74] The challenge going forward will be to ensure that a robust, nationwide vaccination drive is rolled out and that the new cases are kept under control.

The Khan government must also ensure that the recovery is equitable. Households were already struggling prior to the onset of the pandemic, with economic insecurity growing as a result of job losses and high inflation (particularly food). According to early survey data, unemployment rose by 34.1 percent and incomes fell by over 40 percent during the first wave of the pandemic.[75] Even though the nascent recovery has led to a rally in the stock market, jobs and wages have not yet regained their pre-pandemic levels.[76] Still, Khan's government finds itself in a relatively secure position as of mid-2021—the PDM opposition alliance imploded in the spring—and the newly appointed finance minister has suggested that the government will spend upward of $6 billion in the 2021–22 fiscal year to catalyze growth.[77] However, sustained increases in food inflation could spur political and social instability, creating an opening for opposition political voices to confront the government in Islamabad.

In early 2021, the State Bank of Pakistan painted a rosier picture of the country's growth prospects, noting that manufacturing "is also becoming more broad-based."[78] As the economy has rebounded, tax revenues have also inched up: the Federal Board of Revenue exceeded its collection targets for the first eleven months of the fiscal year, with revenues growing by over 17 percent compared to the same period last year.[79] Remittances, which were expected to decline globally, have also grown at a brisk pace, bringing stability to the country's balance of payments. As of March, Pakistan had received over $2 billion in monthly remittances for ten straight months.[80]

The underlying structural issues that have plagued Pakistan's economy remain in place, however. Loss-making state-owned enterprises continue to burn scarce fiscal resources; for instance, a Pakistan International Airlines plane was stopped in Kuala Lumpur, Malaysia, for failure to pay lease payments.[81] Mounting debt in the energy sector also poses a continuing risk to the overall economy.[82] A sustained gap between the cost of energy produced and the revenues earned by distribution companies caused debt in the sector to top Rs. 2.6 trillion in 2021.[83] The crisis in the power sector has further burdened millions of Pakistani households through

While India has its own vaccine manufacturing capacity, it is reliant on critical raw materials from the United States. Pakistan and Bangladesh . . . have sought to import vaccines from both Russia and China.

frequent hikes in energy bills, which are required as part of its agreement with the IMF.

Pakistan also trails the region in terms of human development indicators. India and Bangladesh have both achieved youth literacy rates greater than 90 percent, according to UNESCO data, yet Pakistan's continues to hover around 75 percent. The situation is even worse for Pakistani women, who have higher levels of illiteracy and lower levels of labor force participation than women in peer economies. Pakistan will need to sustain a high rate of economic growth for several years to fully take advantage of its youth dividend, which will require the country's ruling elite to agree on a common agenda focused on economic and human development. Structural economic issues—such as a low tax base, mounting circular debt in the energy sector, and cumbersome regulations that stunt innovation while empowering rent-seeking economic actors—also need to be addressed.

Although internal differences caused the PDM to fracture barely six months after its formation, the country's leading opposition parties are unlikely to work for a consensus with the Khan government to enact meaningful reforms. Furthermore, the resumption of the IMF's stabilization program will likely force the government to pursue deficit-reducing policy measures that could create economic headwinds and inflict additional pain on Pakistani households. The Khan government's thin majority in parliament (even after gaining seats in the senate elections and winning a vote of confidence in parliament in March) means that expending political capital to disrupt the status quo is an inherent risky option. Yet this is exactly the tough choice Khan—who appears likely to become the first Pakistani prime minister to complete a full five-year term—must make to sustain the country's economic momentum. If he fails to make these choices, it is likely that Pakistan will face another economic crisis and find itself hat in hand at the doors of the IMF and its strategic allies.

Impact on Relations with the United States

The near-term focus of the Biden administration must be on ensuring that the United States continues to provide the support needed to accelerate each country's vaccination program. While India has its own vaccine manufacturing capacity, it is reliant on critical raw materials from the United States. Pakistan and Bangladesh, on the other hand, have sought to import vaccines from both Russia and China. In May, Dhaka received a gift of five hundred thousand doses of China's Sinopharm vaccine after shipments of the India-made AstraZeneca vaccine were delayed.

In addition to its focus on vaccine distribution, the United States must also continue to engage with each country as they seek to build economic momentum and deliver sustainable and equitable growth for their citizens.

US-INDIA RELATIONS

Since the signing of the US-India nuclear deal in 2005, relations between the two countries have thrived. India is a key pillar in the United States' Indo-Pacific strategy, particularly as both countries seek sustainable, equitable growth in India as a counterbalance to a rising China. In recent years, the United States, India, Australia, and Japan—known as "The Quad"—have acted more forcefully to counter China's growing assertiveness in the region.

Increased investment from US companies in India's economy, ranging from the technology sector to e-commerce and pharmaceuticals, is a major opportunity. For US investors, India remains an attractive market and a potential destination for relocating global supply chains. Other opportunities for collaboration include 5G technologies and clean energy. To counter China's growing economic influence, the United States and India, along with Australia and Japan, can work together to leverage India's manufacturing base to build capacity in these sectors. The Quad governments' mobilization of resources and equipment to aid India is evidence of the country's strategic importance.[84]

At the same time, reports about changes to e-commerce and retail policies have raised concerns in Washington about India's commitment to providing a level playing field for foreign companies and investors.[85] Recently leaked policy drafts on these issues suggest that the Modi government's desire to create a self-reliant digital ecosystem could create challenges for US-India economic ties and undermine the Quad's strategic ambitions.

Domestic developments in India may force the White House to urge the Modi government to do more to protect human and minority rights, especially if another event similar to the 2020 Delhi riots were to occur. Mounting criticism in the international press may force the Biden administration to publicly comment on events in India, creating tensions in the US-India relationship. Although the United States will likely exercise strategic restraint in any potential commentary on increasing intolerance and radicalization, this restraint will be tested by the Modi government's attitude toward India's minorities. There is also the risk of the Modi government becoming more insular on defense-related issues. India's decision in January 2021 to purchase the Russian S-400 anti-aircraft missile system could potentially lead to US sanctions under the Countering America's Adversaries Through Sanctions Act.[86]

To meet the full potential of the US-India relationship, India will have to continue to push through reforms, open up its economy, and mitigate its long-standing tendency to distrust foreign companies and investors. A US-India trade deal would be a positive development for the relationship, but it is unlikely that such a deal will be signed any time soon. At the same time, India can expect the United States to continue pressuring Pakistan on counterterrorism issues, particularly in the public domain. Although the Financial Action Task Force and other multilateral forums will be used to force action in Pakistan, it is likely that the pressure will ease as the United States disengages from Afghanistan.

For the US-India relationship to deepen, investment and trade flows need to grow further. This growth is only possible if India resists the temptation to be more insular. Policymakers in Washington and Delhi agree on the importance of the US-India relationship, but a slow post-pandemic recovery in India and increasing radicalization may create headwinds and challenges for the relationship in the coming months and years.

US-BANGLADESH RELATIONS

The Bangladeshi government is eager to deepen its relationship with the United States in the coming months. It has consistently signaled a desire to seek investment and maintain good relations with India, China, and the United States. For the United States, an increased role in promoting infrastructure and technology investments in Bangladesh should be of strategic interest. Prime Minister Hasina has continued to solidify ties with India, despite domestic opposition and concerns over the treatment of India's Muslim minority population by the BJP-led government. Bangladesh has sought increased Chinese investments into its economy (for example, Chinese companies are building the $3.65 billion Padma Multipurpose Bridge).[87] At the same time, it has signed agreements to develop strategic infrastructure assets such as the Matarbari deep-sea port and the Dhaka Metro Rail project through a public-private partnership with Japan.[88]

Dhaka is also likely to showcase its appetite for partnering with Washington on strategic projects that improve Bangladesh's economic competitiveness, diversify its economy, and accelerate its digitization efforts. Dhaka has expressed a desire to purchase strategic weapons from the United States in a bid to diversify its military purchases away from China.[89] Its strategic engagement with the United States on the Indo-Pacific strategy is likely to continue during the Biden administration. Dhaka's engagement with New Delhi, particularly through the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation, will also generate further momentum for growing Bangladesh's role in the Indo-Pacific strategy. The Biden administration's climate change agenda is also likely to resonate with Bangladesh—where increasingly extreme weather events pose a grave national security threat to its people and infrastructure—and could open doors for increased collaboration between the two countries.

Bangladesh's authoritarian turn, however, could create tensions in the US-Bangladesh relationship. Prime Minister Hasina has consolidated power in recent years by virtually eliminating her opposition in the country. The space for dissent in Bangladesh is severely constrained, and international human rights organizations have expressed concerns over the government's authoritarian tendencies. The vacuum left by mainstream opposition parties could be filled by Islamist groups, some of whom have become increasingly radicalized.[90]

In recent decades, Bangladesh has made significant investments to boost its economic and human development capacity. These investments have helped it maintain its rising economic trajectory, making the country an attractive destination for US and global investors. It has also deepened its relationship with India and other Asian countries. On January 26, 2021, the Bangladeshi military marched in New Delhi to mark India's Republic Day, and Prime Minister Modi visited Dhaka in March to mark fifty years of Bangladesh's independence.[91] Even as Dhaka has maintained close ties with Beijing, it has made efforts to craft its foreign and economic policy to avoid outright dependence. Bangladesh will continue to balance its relations with both the United States and China, seeking market access and foreign investment to build its economic capacity. The ongoing crisis in Myanmar, however, could create strains between Dhaka and Beijing, as an authoritarian junta in Myanmar could create additional refugees flows into Bangladesh. Given the economic and locational importance of the country, it is important for the Biden administration to broaden and deepen its strategic ties with Bangladesh in the coming months.

US-PAKISTAN RELATIONS

The US-China rivalry will be the dominant feature of geopolitics for years to come. In Washington, Pakistan's relations with the United States will be viewed within this context. Pakistan's strategic relations with China, however, should not prevent the United States from pursuing a narrower, but deeper, relationship with Pakistan in the coming months. Though the priority areas will remain the same—notably, stability in Afghanistan and counterterrorism—other areas of mutual interest are likely to shape US-Pakistan relations. Some of these are climate change, energy security, and technology.

Pakistan faces immense risks from climate change. Water security, a major risk, is already wreaking havoc on the country.[92] The change of administration in Washington means that combating climate change is again a top priority for the United States. Pakistan will need global support to finance needed investments to build resilience and adapt to climate change. This is an area where Pakistan, China, the United States, and other regional countries including India ought to cooperate.

Another important area is energy security. For the third consecutive winter, Pakistan faced gas shortages that curtailed economic activity.[93] Islamabad has invested billions of dollars in building power capacity, yet it requires billions of dollars in additional investments to ensure its energy security. This includes investments in gas infrastructure, renewable energy (including wind and solar power), and electricity transmission. The United States has historically played a vital role in Pakistan's energy sector—from providing financing and technical expertise in the 1960s and 1970s for the massive hydroelectric Tarbela Dam to, more recently, helping create the legal framework for the development of infrastructure for the importation of liquefied natural gas. There are opportunities for bilateral and private-sector cooperation in this space.

Technology is a third key area of concern in US-Pakistan relations. Even though Pakistan has a lower youth literacy rate than peer economies, it is one of the largest freelance technology markets in the world. As a result, the country's information technology exports have increased by more than 175 percent in recent years. Despite Pakistan's strategic bilateral ties with China, American technology brands from Netflix to Facebook and YouTube are by far the more popular in the country. These tech companies, however, face a difficult operating environment in Pakistan as a result of authorities frequently restricting citizen's access to their platforms. The country also recently launched a digital payments system, which, it is hoped, will catalyze the growth of fintech start-ups and promote financial inclusion. Given the 5G rivalry between the United States and China, it is important for American technology companies and investors to have a stake in Pakistan's growing information technology market. Onerous regulations remain a risk, and yet bilateral engagement and an increased level of investment flowing from the United States into Pakistan's start-up ecosystem, particularly through the diaspora, can help develop a competitive and open technology sector.

China will continue to be a strategic ally that plays an outsized role in Pakistan. However, there is space for the Biden administration to engage with Pakistan and improve bilateral relations, allowing the United States to play a balancing role to China's growing influence in the region while pursuing mutually beneficial strategic objectives. Pakistan has significant agency in determining how this relationship evolves. To strengthen this relationship, its policymakers must pursue a reforms agenda that makes Pakistan an important country not just for Washington, but for New York, Silicon Valley, and beyond.

Conclusion

The COVID-19 pandemic has caused one of the most serious public health and economic crises faced by India, Bangladesh, and Pakistan in recent years, creating mass unemployment and pushing millions of households below the poverty line. Although the expansion of cash and food support programs by all three countries has been a critical lifeline for the millions of households hovering around the poverty line, the breadth and depth of the economic crisis means that, even under the most optimistic scenarios, it will take months if not years for the majority of households to recover from the economic havoc.

Rising number of cases during the first half of 2021 inflicted additional pain and misery on the subcontinent, jeopardizing the region's nascent recovery. The risk is especially high in India, which experienced exponential growth in new cases during its second wave in April and May 2021, overwhelming the country's health-care system, leading to another series of lockdowns from Delhi to Karnataka, and inflicting unimaginable socioeconomic trauma on millions of citizens. As a result, India's economic outlook has substantially worsened, creating serious challenges for the government in Delhi. While Prime Minister Modi's government has used the pandemic as an opportunity to push through some vital reforms to deal with the economy's structural issues, it now has to focus on dealing with the nation's most serious crisis since partition in 1947.

Despite losing billions of dollars in export earnings, Bangladesh managed to maintain positive economic growth during the first fifteen months of the pandemic—the only country among the three to do so. Prime Minister Hasina's government adopted a forward-looking strategy in order to build economic capacity and diversify the economy away from ready-made garments. Despite the reimposition of lockdowns in April and May 2021, it is possible that Bangladesh's economy will emerge from the pandemic in a stronger position, provided that cases do not rise dramatically and that its mass vaccination program continues to build momentum.

Pakistan has managed to control the spread of the coronavirus during both the initial and the subsequent waves of the pandemic. However, its political system remains fractured, leaving little to no room for Prime Minister Khan's government to pursue the politically costly structural reforms necessary to change the economy's long-term trajectory. While the Khan government has focused on catalyzing growth in the budget announced in June 2021, structural weaknesses in Pakistan's political economy will continue to create near-term headwinds for a sustainable, broad-based economic recovery.

The subcontinent has continued to see an erosion of democratic norms, growing authoritarianism, and a severe crackdown on dissent. An inequitable post-pandemic recovery could lead to both economic and social instability, leading to heavy-handed responses from any or all of these governments that could in turn fuel violence and systemic instability. Such instability could create a vicious cycle, where growing instability erodes confidence in the economy, which slows down investment, which jeopardizes growth, which leads to further instability. To prevent such an outcome and to pave the path for a sustainable economic recovery, governments across the subcontinent will have to remain focused on proactively curtailing the spread of the virus, rapidly expand their vaccination programs, and mobilize economic resources in a way that allows a broad-based, equitable, and sustainable economic recovery to take hold.

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