Coronavirus: macroeconomic implications for Latin America

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Adjunct Professor IE University
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The World
Historic surge in US unemployment benefits

More than 3 million people file claims as coronavirus hits

Car sales in China have fallen sharply

Source: China Passenger Car Association, 27 March 2020, 13:00 GMT
Satellite images show pollution clear amid lockdown

Nitrogen dioxide levels in the lower atmosphere

France

March 2019

14-25 March 2020

Italy

March 2019

14-25 March 2020

Spain

March 2019

14-25 March 2020

Source: ESA/Copernicus, 27 March 2020
The global economic outlook has been shifting at lightning speed.

Exhibit 1. Sharp contractions in the US and Euro zone,...

Exhibit 2. ... will open up large output gaps.
### Exhibit 3: IIF Global Growth Forecasts

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COVID-19 and Oil Price War Resulted In About 400 Negative Rating Actions (Downgrades, Outlook changes, CreditWatch Negative)

Percentage of total issuers with rating actions taken

- Aerospace & Defense
- Automotive
- Bank
- Building Materials
- Business and Consumer Services
- Capital Goods
- Chemicals
- Commercial & Professional Services
- Consumer Products
- Containers & Packaging
- Electric
- Energy
- Financial Institutions
- Gas
- Health Care
- Hotels & Gaming
- Information Technology
- Insurance
- Media & Entertainment
- Metals & Mining
- Property & Real Estate
- Retailing
- Sovereign
- Technology

The global economy

• Very difficult to forecast economic growth under these circumstances: it has become a moving target

• However, beyond the specific numbers, we are facing a global recession that hopefully will be short-lived

• The sectors more affected are automotive, commercial and professional services, hotels and gaming, media and entertainment, retailing, energy and aerospace and defense.

• Sectors that are performing well: gas, electricity, banks, insurance, information technology, container and packaging and health care
Latin America
Is Latin America prepared for COVID-19?

Sources: Worldometers.info, Global Health Security Index; and IMF staff calculations.
Note: Numbers in brackets represent the number of confirmed cases and number of deaths as of March 18, 2020.
Impact channels
Immediate economic impacts in Latin America include a tightening of financial conditions, a decline in commodity prices, and lower tourism.

(Sovereign spreads, emerging-market bond index; basis points)

Source: Bloomberg Finance L.P.
(Commodity exports, percent of GDP)

Source: World Bank. World Development Indicators database and IMF staff calculations.
Note: Latest available data. Includes food, fuel, and ores and metals exports. Country abbreviations refer to the International Organization for Standardization code.
(International tourism receipts, percent of GDP)

Source: World Bank. World Development Indicators database and IMF staff calculations.
Note: Latest available data. Country abbreviations refer to the International Organization for Standardization code.
<table>
<thead>
<tr>
<th>Country Name</th>
<th>Volume 2019 (US$)</th>
<th>Growth 2018</th>
<th>Growth 2019</th>
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<td>28.1%</td>
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Notes: * Estimates; ** Venezuela 2018, 2019 remittance data is Inter-American Dialogue estimate based on survey data; previous years are unavailable. For GDP growth and Remittances GDP, Inter-American Dialogue estimates based on World Bank figures for GDP and economic growth from the Economic Commission for Latin America and the Caribbean.
Figure 3.4 Shadow Economy by Region (average, percent of GDP)

Source: IMF
## Coronavirus Heat Map

<table>
<thead>
<tr>
<th>Country</th>
<th>Containment response</th>
<th>Health security</th>
<th>Disruption to domestic activity</th>
<th>Commodity dependence</th>
<th>Informality</th>
<th>Forecast fiscal stimulus</th>
<th>Public indebtedness</th>
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**Containment response:** A qualitative assessment by EIU analysts of the strictness of social distancing protocols, enforcement of border controls and measures taken to increase the testing rate.

**Health security:** Considers countries’ capabilities to respond to epidemics and pandemics, as measured by the Global Health Security Index.

**Disruption to domestic activity:** Uses the contribution of services to GDP to assess the extent to which quarantine measures affect aggregate output.

**Informality:** Uses proportion of informal employment to assess labour market vulnerability to economic shocks.

**Forecast fiscal stimulus:** Considers the magnitude of fiscal stimulus, as a percentage of GDP, deployed to minimise economic damage.

**Public indebtedness:** Uses the public debt/GDP ratio as a proxy for available fiscal space.

**Commodity dependence:** Uses the commodity exports/GDP ratio to assess countries’ exposure to external demand shocks.
Sovereign Ratings: Americas

Canada AAA/AAA
U.S. AA+/AA+
Bermuda A+/A+
Chile A+/AA-
Aruba BBB+/BBB+
Panama BBB+/BBB+
Peru BBB+/A-
Turks and Caicos BBB+/BBB+
Uruguay BBB/BBB
Curacao BBB/BBB
Mexico BBB/BBB+
Colombia BBB-/BBB
Trinidad & Tobago BBB-/BBB-
Montserrat BBB-/BBB-

Bahamas BB+/BB+
Paraguay BB/BB
Brazil BB-/BB-
Bolivia BB-/BB-
Dominican Republic BB-/BB-
Guatemala BB-/BB
Honduras BB-/BB-
Costa Rica B+/B+
Jamaica B+/B+
Suriname B/B
Belize B-/B-
El Salvador B-/B-
Nicaragua B-/B-
Barbados B-/B-
Ecuador CCC-/C / CW NEG
Argentina CCC-/SD
Venezuela SD/CCC-

Outlook/CreditWatch: Stable, Positive, Negative

Source: Ratings as of March 9th, 2020 as published on S&P Global’s Global Credit Portal.
South America

• Reduced export revenues, both from the fall in commodity prices and reduction in export volumes

• The drop in oil prices will hit the oil exporters hard especially Ecuador, Colombia Brazil and Venezuela

• Capital outflows due to global financial conditions will impact negatively the large and financially integrated countries (Brazil, Mexico, Colombia) and those with underlying vulnerabilities (Argentina, Ecuador).

• Containment measures in several economies will reduce economic activity in service and manufacturing sectors
The recession in the United States will cause a reduction in trade, foreign direct investment, tourism, and remittances.

Key agricultural exports (coffee, sugar, banana) as well as trade flows will be adversely affected by lower global demand.

Local outbreaks will put pressure on economic activity in the next quarter and aggravate already uncertain business conditions (especially in Mexico).

In the Caribbean, commodity exporters will also be strongly impacted and a reduction in remittances and tourism is likely to add to the economic stress.
We are we now?
Where are we?

- Uncharted waters

- Governments are making decisions at a very fast pace, without much time to think or plan

- There are difficult moral trade-offs

- The connection between public health and macroeconomics is not clear

- Macroeconomic policy discussions are focused on advanced countries
The trolley problem

Covid-19

Government

People

Economy
The three shocks
Three simultaneous shocks

- **Health Shock:** Coronavirus COVID-19
- **External Income Shock:** Commodity prices, Tourism, Remittances
- **Capital Markets Shock**
Commodity prices have taken a large hit

Aggregate commodity index

Copper
Oil hits record lows

US dollars per barrel

Source: Bloomberg, 27 March 2020, 13:00 GMT
Far fewer commercial flights
Number of daily flights in March

Source: Flightradar24, 27 March 2020, 13:00 GMT
The impact of coronavirus on stock markets since the start of the outbreak

Nikkei: -16.4%
Dow Jones: -21.9%
FTSE 100: -26.6%

Source: Bloomberg, 27 March 2020, 13:00 GMT
This time is different

• It is a supply shock.

• It expands through both supply and demand channels.

• Traditional Keynesian fiscal policies have limited impact: there is demand, but many activities are shut down.

• Layoffs and bankruptcies will make the recuperation much slower.

• Fiscal policy can help, but not through the standard channels: it should focus on people and firms.
Macroeconomic Policies Responses
Macroeconomic policies responses

- Coronavirus is a short-term situation, it is not a permanent shock

- There is the need to create all the short-term fiscal space possible

- Tax revenues are going down because of the measures to fight COVID-19

- This is no the time to worry about prudential norms: credit rating, debt/GDP, fiscal deficit, etc.

- The objective is to mobilize the maximum amount of fiscal resources by borrowing all that is possible
Creating maximum fiscal space

- Short-term situation: borrow all that is possible with a maturity of around two years
  - Domestic markets: monetary easing and central bank support
  - International capital markets
  - IMF and other International Financial Institutions (IFIs)

- Postpone all non-essential expenditures

- Oil importers should take advantage of lower prices: split the gains between government and consumers

- International Reserves are for emergencies: they should be used to support fiscal efforts such as loans to firms and credit lines to banks
Using the fiscal space

- Most important: support health system
- Provide short-term assistance to people and firms
- Help banks if needed through central banks
- There is not time to design new programs, governments should use what it is in place i.e. cash transfers schemes
- Focus on the informal sector
- Use the banking system to support firms, i.e. provide partial guarantees for banks to lend for the payroll
The International Community
What should the international financial community do?

- Recirculate the flight-to-safety money that is flowing to the US
- Quantitative Easing: buy IFIs and EM bonds
- Increase the number of countries with access to FED swap lines
- Expand the use of existing credit facilities, i.e. IMF Rapid Financing Instrument (RFI)
- Create an international fund to pay for testing, equipment and eventually vaccines