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As in the rest of the world, Covid-19 has inflicted considerable pain in Latin America, both economically and socially. Prior to the pandemic, the region's gross domestic product (GDP) was expected to grow at a rate of 1.8 percent in 2020, a modest recovery from the 0.2 percent growth observed in 2019. Owing to the pandemic, however, the region's economy will instead contract by an estimated 8.1 percent this year, according to the International Monetary Fund's latest forecast. And while recovery is expected next year, its extent is likely to be limited, leaving economic output well below the pre-Covid level by the end of 2021. The potential for "scarring" and solvency concerns further weigh on the Latin American outlook, while upside potential exists from technological breakthroughs in treatments and vaccines, which would allow for stronger global growth and regional performance. Concerted government intervention will be required to assess the pandemic's impact on poverty and inequality in the region.

The Global Outlook post Covid-19: Are We out of the Woods?

The Covid-driven economic crisis that began in the first quarter of this year was an unprecedented global shock to both aggregate demand and aggregate supply. As countries imposed strict social distancing measures to flatten the contagion curve of the pandemic, global production, consumption, and investment came to a virtual stop, first in China and then in the rest of the world. Firms that were able to operate remotely continued to function, albeit less than optimally, while those that depended on in-person interactions had no choice but to shut down. In the first half of the year, real GDP in China and in the biggest advanced economies fell by 30 to 40 percent on an annualized basis from one quarter to the next, the timing of these downturns following the spread of the pandemic.

The decline in activity was larger in labor-intensive service industries than in capital-intensive primary and manufacturing ones, causing unemployment to jump in most countries. The United States witnessed its unemployment rates jump from a record-low of 3.7 percent before the pandemic to a record-high (since 1947) of 14.8 percent in April of this year. In Europe, the increase in unemployment was lower due to its social safety nets, but real GDP plummeted nonetheless as work hours decreased. The pandemic's effect on emerging markets was a mixed bag: some economies, like China, were able to control the spread of the virus early on, while others, like India, are still struggling with their health response. As a result, China saw its economy contract sharply in the first quarter and stabilize after that, in contrast to India and other less fortunate emerging markets, which are still facing harsher recessions.

Advanced economies are forecasted to contract by 6.1 percent in 2020, versus 1.1 percent in emerging markets and developing countries. However, excluding Asia, emerging market and developing economies are forecasted to contract more (4.0 percent), as emerging and developing Asia, including China, is the only region in the world forecasted to experience positive growth (1.0 percent) in the current year. Notwithstanding the pandemic's unprecedented shock to the global economy, outcomes would have been considerably worse had it not been for the massive monetary and fiscal support measures countries around the world implemented in response. For instance, central banks cut interest rates and intervened directly in financial markets to prevent a disruption in liquidity and credit flows. This swift and massive policy support not only helped to stabilize asset prices but was also instrumental in ending a brief, but unprecedented, sudden stop of capital inflows to emerging markets. Fiscal policy complemented monetary efforts through a battery of measures designed to support individual incomes and businesses hit by social distancing, as well as to support the public health response. Fiscal relief came in the form of direct payments to households and firms, along with tax breaks, deferments, and guarantees; according to some estimates, this came at a cost of $8 trillion worldwide.

Despite having considerably less monetary and fiscal space than the advanced economies, emerging markets also reacted forcefully, as did international financial institutions—including the International Monetary Fund (IMF), the World Bank, and many of the regional development banks—which acted promptly to support them.

Depending on the trajectory of the virus and the pace and distribution of technological advances, the biggest hit to the global economy may be behind us, with global recovery starting from the third quarter of this year and continuing into 2021. The IMF projects 5.2 percent real GDP growth in 2021 after a 4.4 percent contraction this year. Considering that, in 2019, global GDP was expected to grow by 3.4 percent in 2020 and 3.6 percent on average from 2021–2024. This would put post-pandemic levels 6 percent below the pre-pandemic trend by the end of 2021.

The output recovery underway in the United States has reduced unemployment from 14.8 percent in April to 7.9 percent in September. However, much of the recovery has been driven by consumer spending, which in turn was supported by income support under the CARES Act. Given the persistence and spread of the virus leading to continued and renewed restrictions, growth is once again at risk, especially if the next fiscal package is further delayed. For 2021, the IMF forecasts real GDP to grow by 3.1 percent in the United States, 5.2 percent in the Eurozone, and 8.2 percent in China (see Table 1). Numerous risks to these baseline projections exist, however, depending on both health and policy factors. Among the former is the likelihood of new waves of Covid-19 amid a lack of widely available effective treatments and delays in the availability and distribution of a vaccine. Among the latter, a premature withdrawal of policy support could derail recovery, while a deterioration in global financial conditions could trigger debt crises, especially in emerging and developing countries.

Table 1: Real GDP Growth and Unemployment in the United States, Eurozone, and China

Baseline Forecasts for 2020–2023.

	2019	2020	2021	2022	2023
USA					
Real GDP Growth	2.2	(4.3)	3.1	2.9	2.3
Unemployment %	3.7	8.9	7.3	5.7	5.1
Eurozone					
Real GDP Growth	1.3	(8.3)	5.2	3.1	2.2
Unemployment%	7.6	8.9	9.1	8.4	7.9
China					
Real GDP Growth	6.1	1.9	8.2	5.8	5.7
Unemployment %	3.6	3.8	3.6	3.6	3.5

Source: International Monetary Fund, World Economic Outlook: A Long and Difficult Ascent (Washington, D.C.: IMF, October 2020), https://www.imf.org/en/Publications/WEO/Issues/2020/09/30/world-economic-outlook-october-2020.

The Regional Outlook: How Will Latin America Fare?

It is no secret that economic growth in Latin America has underperformed for many years, when compared to other emerging market regions. From 1980 to 2020, the only period of significant expansion in real GDP per capita took place between 2003 and 2013 and was largely fueled by the China-led commodity boom rather than by improvements in physical and human capital investment or total factor productivity. Before the pandemic hit at the beginning of this year, the region's GDP was already poised to grow at only 2 percent per year in 2020 and 2021. The IMF forecasts that real GDP for the region will contract by 8.1 percent in 2020 followed by a 3.6 percent expansion in 2021, leaving the region 8.7 percent below the projected pre-pandemic trend (or in per-capita terms, more than 10 percent below projections). Among the region's six largest economies (hereinafter the Latam-6), those most severely hit by the pandemic were Peru, Argentina, and Mexico. These are forecasted to experience real GDP contractions of 13.9 percent, 11.8 percent, and 9.0 percent, respectively, followed by Colombia (8.2 percent), Chile (6.0 percent), and Brazil (5.8 percent).

Latin America's expected economic performance in response to the pandemic compares unfavorably with that of other emerging market regions (see Table 2). Not only will this year's economic contraction be deeper than in emerging regions of Asia, Eastern Europe, the Middle East, and Africa, but next year's recovery will be relatively weak, further widening the income gaps across regions. Weak recovery—coming after years of low growth—has implications for poverty rates and living standards, which in turn are amplified by historically high levels of inequality in the region.

Table 2: Growth Outlook in Latin America vs. Other Emerging Market Regions

% Change in Real GDP Relative to Previous Year; Baseline Forecasts for 2020 and 2021.

	2019	2020	2021	2022	2023
Latin America	0.2	(8.1)	3.6	2.7	2.7
EM-Asia	5.5	(1.7)	8.0	6.3	6.1
EM-Europe	2.1	(4.6)	3.9	3.4	3.0
EM-Middle East	1.4	(4.1)	3.0	4.0	3.6
Sub-Saharan Africa	3.2	(3.0)	3.1	4.0	4.4

Source: International Monetary Fund, World Economic Outlook: A Long and Difficult Ascent (Washington, D.C.: IMF, October 2020), https://www.imf.org/en/Publications/WEO/Issues/2020/09/30/world-economic-outlook-october-2020.

Latam-6 Country Outlooks[1]

ARGENTINA

Argentina's seasonally-adjusted quarterly real GDP fell by 50 percent in the second quarter, on an annualized basis. This dramatic drop of economic activity took place after a difficult 2019 in which GDP fell by 2.1 percent year-on-year and inflation reached 54 percent—up from 48 percent the year before. Against the backdrop of this health and economic crisis, 2020 saw Argentina complete its ninth sovereign debt restructuring with private creditors, and its government is now preparing to start negotiations with the IMF on a new IMF-supported program. The IMF predicts Argentina's GDP will shrink by an additional 11.8 percent this year and expand by 4.9 percent in 2021 (see Table 3), hence accumulating a permanent loss of 8.0 percent; this adds to the malaise of the past seven years, during which the country's real GDP did not grow at all. Going forward, Argentina's growth prospects will be challenged by persistently high inflation, a high fiscal deficit (10 percent of GDP) significantly increased by the pandemic, and high exchange rate volatility due to a very low level of foreign reserves.

BRAZIL

Compared to the rest of the region, Brazil's second quarter contraction (33.5 percent when seasonally adjusted and annualized) was relatively mild. Various factors contributed to this outcome, including looser quarantine measures than those implemented by neighbors such as Argentina and Peru, increased exports to China (particularly of soybeans), and a spectacular increase in fiscal transfers. This last measure raised the budget deficit by 10 percent of GDP—from around 6 percent in 2019 to an expected 16 percent in 2020. In addition, the Central Bank reduced the monetary policy interest rate to a record-low 2 percent, aided by low inflation. Brazil's GDP is forecast to contract by 5.8 percent this year and expand by 2.8 percent next year, as fiscal stimulus unwinds to comply with the constitutional mandate of keeping primary spending constant in real terms over the medium term. It is also worth noting that, along with Mexico, Brazil is one of two countries in Latin America with access to a dollar swap line with the U.S. Federal Reserve.

CHILE

Second quarter GDP contraction (seasonally adjusted and annualized) was 43 percent, higher than in Brazil but lower than in the other Latam-6 countries. An improvement in external terms of trade, due to

1. Data for this section, unless otherwise noted, comes from the IMF World Economic Outlook Database, part of the October 2020 report. International Monetary Fund, *World Economic Outlook: A Long and Difficult Ascent* (Washington, D.C.: IMF, October 2020), https://www.imf.org/en/Publications/WEO/Issues/2020/09/30/world-economic-outlook-october-2020.

sustained copper prices and low oil prices, prevented a stronger collapse in real income. Even so, Chile's GDP is expected to fall by 6.0 percent this year, due to a decrease in export volumes and a strict lockdown—notwithstanding the strong expansionary fiscal and monetary policies adopted by its government and Central Bank. On the monetary side, the Central Bank kept the policy rate at 0.5 percent, but it introduced unconventional liquidity measures to prop up credit supply. On the fiscal side, Chile's budget deficit rose to an expected 12 percent of GDP. This was complemented by a resolution authorizing younger workers to withdraw money from their individual pension accounts. The economy is expected to recover next year, growing by 4.5 percent, but an impending referendum on a new constitution clouds the long-term horizon. As of May 2020, Chile has a Flexible Credit Line (FCL) with the IMF providing access to roughly $24 billion to meet its balance of payments needs.

COLOMBIA

The Andean country has been struggling to control the pandemic, intermittently shutting and re-opening its economy as the health system has become stressed in some major cities. A sharp decline in domestic demand, combined with the decrease in the price of oil and an overall reduction in exports, provoked a sharp increase in unemployment: it jumped from 10.5 percent in January to almost 20 percent in August, although it is expected to fall to 17.3 percent by the end of this year (see Table 4). Second-quarter contraction was in-line with the region, but third-quarter recovery was slow because of this unemployment increase. Colombia's economy is posed to contract by 8.2 percent this year and grow by 4.0 percent next year. Weaker public finances (as compared with Chile and Peru) and a lack of monetary maneuvering space prevent the government from engineering a large stimulus program; furthermore, as in Brazil, Colombia's public sector budget is subject to the strictures of a multi-year fiscal responsibility rule that calls for a fiscal contraction next year. Colombia has an expanded Flexible Credit Line with the IMF, which was further increased on September 25, 2020, providing total access to roughly $17.2 billion for balance of payments needs.

MEXICO

Mexico's economy was already in poor shape last year when a mild recession took place; it contracted again in the first quarter of this year. The pandemic accelerated the reduction in Mexico's real GDP as lower demand from the United States restricted manufacturing production and exports. Despite having more fiscal space than Argentina, Brazil, and Colombia, the stimulus plan implemented by Mexico's federal government was weak—and, for the most part, consisted of handouts to households rather than programs to protect employment in business activities, particularly in the large (both formal and informal) service sector and among small and medium enterprises. The IMF expects a sharp contraction in 2020 (by 9.0 percent) followed by a mild recovery in 2021 (by 3.5 percent). Like Brazil, Mexico has access to a dollar swap line with the U.S. Federal Reserve; it also has access to an FCL with the IMF, which provides an additional $61 billion.

PERU

The Peruvian economy contracted by a record 72 percent in the second quarter (annualized and seasonally adjusted). The strict nationwide lockdown needed to fight a stubbornly high Covid-19 infection rate caused domestic consumption and investment to plummet; at the same time, the drop in metal demand—especially from China—drove exports down, resulting in a projected 13.9 percent contraction this year, after a meager 2.2 percent growth rate in 2019. However, the government is using the fiscal space it enjoys thanks to prudent budgetary policies implemented in the past to stimulate domestic demand amid a sharp increase in unemployment. Along with the resumption of exports to China, this will make it possible for

Peru to experience a recovery next year, when GDP is expected to grow by 7.3 percent. Peru also has an FCL with the IMF which was approved in May 2020 and which provides up to $11 billion in balance of payments financing.

Table 3: Growth Outlook in Latam-6 Countries

% Change in Real GDP Relative to Previous Year; Baseline Forecasts for 2020–2023.

	2019	2020	2021	2022	2023
Argentina	(2.1)	(11.8)	4.9	2.5	2.3
Brazil	1.1	(5.8)	2.8	2.3	2.2
Chile	1.1	(6.0)	4.5	3.2	2.9
Colombia	3.3	(8.2)	4.0	3.7	3.8
Mexico	(0.3)	(9.0)	3.5	2.3	2.2
Peru	2.2	(13.9)	7.3	5.0	4.9

Source: International Monetary Fund, World Economic Outlook: A Long and Difficult Ascent (Washington, D.C.: IMF, October 2020), https://www.imf.org/en/Publications/WEO/Issues/2020/09/30/world-economic-outlook-october-2020.

Table 4: Unemployment Outlook in Latam-6 Countries

Unemployment As % of Labor Force; Baseline Forecasts for 2020–2023.

	2019	2020	2021	2022	2023
Argentina	9.8	11.0	10.1	9.7	9.4
Brazil	11.9	13.4	14.1	13.3	12.5
Chile	7.2	11.4	10.2	9.1	8.2
Colombia	10.5	17.3	15.8	14.6	13.5
Mexico	3.5	5.2	5.8	4.7	4.4
Peru	6.6	12.5	8.9	6.8	6.5

Source: International Monetary Fund, World Economic Outlook: A Long and Difficult Ascent (Washington, D.C.: IMF, October 2020), https://www.imf.org/en/Publications/WEO/Issues/2020/09/30/world-economic-outlook-october-2020.

Risks to Baseline Forecasts

The above forecasts correspond to a baseline scenario, but there are upside and downside risks affecting individual countries and the region as a whole. These risks stem mainly from changes in health conditions, global trade, and domestic policies.

On the health front, the baseline scenario assumes that the pandemic will be controlled by mid-2021—if perhaps not globally, at least in advanced countries. Vaccine availability and effective disease treatments will allow consumer and business confidence to return, causing global and individual economies to normalize. In the meantime, Covid-19 will continue to be a threat, especially in emerging and developing countries, particularly if new contagion waves occur calling for fresh new lockdowns. In this sense, the rapid deployment of a vaccine, targeting universal access, should increase the speed and strength of global economic recovery.

Regarding trade, the World Trade Organization forecasts that global trading volumes will decline by 9.2 percent in 2020, followed by a partial recovery in 2021. However, economic effects so far have differed widely across regions and by country. In Latin America, Brazil benefitted from higher exports to China, but Colombia and Peru did not. Mexico's manufacturing exports suffered because they are linked to industrial production in the United States, and they are still depressed. Sustained copper prices helped Chile to keep export revenues high, but soybean exports in Argentina did not increase as they did in Brazil, because of export taxes and a less competitive exchange rate. Going forward, all countries in the region are likely to benefit from the renewed increase in world trade and the recovery of commodity prices. However, unlike during the Global Financial Crisis, China's relatively more restrained policy response means that China is unlikely to be as significant a source of export demand as before, potentially weighing on the outlook for many Latin American economies.

Lastly, on the issue of domestic policy, there is a question of how much fiscal and monetary space the Latam-6 countries have—the unfortunate answer is not very much, and certainly less than advanced economies. Moreover, fiscal policy will need to weigh debt-sustainability as well as price-stability concerns. Unless modified, Brazil and Colombia will soon have to start unwinding the fiscal expansions introduced this year in order to comply with their own fiscal responsibility rules, while Argentina faces an even more complicated situation because the increase in its budget deficit was financed almost exclusively by issuing money. As the local economy reopens, Argentina will likely see inflation accelerate from its already high level. On the other hand, the need to reverse fiscal expansion is less urgent in Chile and Peru, thanks to the greater space afforded by past fiscal restraint in these countries, and in Mexico, because its initial fiscal expansion was not as large in response to the first wave of the pandemic.

On the positive side, global financial conditions remain supportive. Along with the fact that all Latam-6 countries (except Argentina) have low inflation, this gives their central banks room to keep interest rates low for longer—and, in certain circumstances, even to resort to unconventional monetary easing if needed without their jeopardizing currency and financial stability.

The Role of International Financial Institutions and Foreign Donors during the Pandemic

Given the unprecedented nature of the Covid-19 crisis, the force with which multilateral and bilateral organizations responded to it is not surprising. Efforts were made to mobilize resources in large quantities to support emerging and developing economies. Several Latin American countries requested and obtained emergency loans from the IMF, while others have been granted precautionary credit since March. Emergency loans from the IMF, in the shape of the Rapid Credit Facility (RCF) and the Rapid Financing Instrument (RFI), allow the IMF to "provide emergency assistance without the need to have a full-fledged program in place," and are better suited to the needs of the smaller and poorer countries in the region. Ecuador received an RFI and an Extended Fund Facility (EFF), the latter in the amount of $6.5 billion. Honduras and Barbados augmented their existing EFF and Stand-By Arrangement (SBA).

In addition to lending money in concessional terms to these countries, the IMF can alleviate existing official debt service for low income countries that qualify through its Catastrophe Containment and Relief Trust (CCRT). The CCRT—which grew out of efforts to eliminate Haiti's entire outstanding debt to the IMF after the 2010 earthquake—provides grants to the Fund's poorest and most vulnerable members in order to cover IMF debt service obligations. A separate initiative, the Debt Service Suspension Initiative (DSSI), was proposed by the heads of the IMF and the World Bank in March, and agreed to by G20 Finance Ministers and Central Bank Governors in April. This measure will "allow official bilateral donors to suspend debt service payments from the poorest countries and, in this way, free up scarce resources that can be used to safeguard lives and livelihoods in those countries." The Fund, the World Bank, and the G20 have also called for private sector creditors to participate in similar debt relief on comparable voluntary terms, which could add a further $7 billion of relief.

For the larger countries that are the focus of this report, emergency credit assistance has not been necessary during the pandemic, because all of them, with the exception of Argentina, have access to voluntary lending from domestic and external private sources. This access is available at relatively low interest rates thanks to supportive international and local capital market conditions. Rather than emergency measures, a number of these larger Latin American economies have accessed precautionary financial assistance from the IMF in the form of Flexible Credit Lines (FCLs). This form of assistance is available to countries with "very strong policy frameworks and track records" that don't have a current balance of payments need but could have one in the future. Since the start of the crisis, the IMF has approved FCLs for Chile, Colombia, and Peru in the amounts of $23.9 billion, $16.9 billion, and $11 billion, respectively. Mexico also has an FCL, which was most recently re-approved in November 2019. While there is no official eligibility list for the FCL, Argentina is almost certainly ineligible; in addition, Argentina already owes $44 billion to the Fund. This money was disbursed before the pandemic as part of an SBA designed to cope with a currency crisis that afflicted the economy in 2018 and 2019. Even though Argentina cannot expect fresh resources from the Fund, conversations to extend the maturity of the country's massive existing debt are scheduled to begin soon between the Argentine Government and the IMF.

Conclusion

The Covid-driven economic crisis that began in January of this year was an unprecedented global shock to both aggregate demand and aggregate supply. Outcomes would have been considerably worse had it not been for the equally unprecedented monetary and fiscal support measures countries put forth in response to the pandemic. While the largest policy packages have come from advanced economies, emerging markets also reacted forcefully despite having considerably less monetary and fiscal space, as did international financial institutions.

Leading economic indicators available in most countries suggest that the worse of the crisis may be behind us and that the world economy is set to recover beginning in the fourth quarter of this year. Unfortunately, Latin America's economy took an especially hard hit from the pandemic when compared to the world or to other emerging markets. Not only will this year's economic contraction be deeper in Latin America than in emerging regions of Asia, Eastern Europe, the Middle East, and Africa, but next year's recovery will be relatively weak, further widening the income gaps across regions.

Among the Latin American region's top six economies, those most severely hit by the pandemic are Peru, Argentina, and Mexico. Brazil, Chile, and Colombia are also forecast to incur economic contractions in excess of 5 percent this year. Recovery is expected to be slow in all of these countries except Peru, and even in the latter, it will not amount to a full-fledged V-shaped recovery. Risks to the baseline scenarios stem mainly from changes in health conditions, global trade, and domestic policies, as well as from the potential for solvency concerns to slow economic recovery. On the positive side, global financial conditions remain supportive. This, and the fact that all Latam-6 countries (except Argentina) have low inflation, provides sufficient room for central banks to keep interest rates low for longer, and even to try unconventional monetary easing in certain circumstances, without jeopardizing currency and financial stability. ■

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