



# INTERNATIONAL MONETARY AND FINANCIAL COMMITTEE

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**IMFC Statement by Martín Guzmán  
Minister of Economy  
Argentina**

On behalf of  
Argentina, Bolivia, Chile, Paraguay, Peru, and Uruguay

## **Statement by Governor Martín Guzmán, Minister of Economy of Argentina**

### **On behalf of the Southern Cone Constituency**

**(Argentina, Bolivia, Chile, Paraguay, Peru, and Uruguay)**

#### **Global Developments**

##### **The global outlook recovers amidst high uncertainty and risks tilted to the downside**

Global economic prospects for 2020 have improved due to a lower-than-anticipated but still severe contraction in the second quarter, mainly resulting from a pick-up in demand from China and a faster resumption of seasonal activities in advanced economies (AEs), but partly offset by weaker activity in some Asian countries.

The October 2020 World Economic Outlook (WEO) provides an invaluable analysis of the risks ahead. A modest improvement in the outlook may provide additional room to implement policies to foster a faster recovery, as analyzed in-depth in the report. The baseline assumption of a gradual expansion of vaccine coverage and the adoption of improved therapies appear reasonable at this stage. However, the unpredictable path of the pandemic, the undetermined nature of the adjustment costs to the economy, and the unknown effectiveness of policy responses create an uncertain environment. In these difficult circumstances, the Fund has risen to the immediate challenge, responding rapidly to requests of emergency financing and adapting its toolkit to the pandemic realities, including the delivery of capacity development, while widening its analytical coverage and disseminating its advice in friendly formats to guide policy decisions by its membership.

Global GDP growth in 2021 is expected to rise above 2019 levels slightly by 0.5 percent, impacting global progress achieved in reducing global poverty and lowering inequality. School closures and problems in the introduction of digital alternatives constrain access to quality education, nutrition, and a safe environment for children, resulting in a severe social problem that undermines the future of communities. The prospects for preventing human capital erosion are gloomy, particularly in an adverse scenario where the spread of the virus remains difficult to control, and fiscal and financial frictions are larger than envisaged in the baseline. In this scenario, global economic growth would be 3 percentage points lower than otherwise in 2021, and global GDP growth would remain 1.5 percent below the baseline scenario by 2025. The main challenge will be to ensure that this weaker growth does not also imply greater inequality within societies.

The materialization of such adverse scenario could create long-lasting damage to productive capacity, leading to a persistent rise in the rate of unemployment and weaker productivity growth, with a disastrous loss in the standard of living of vulnerable workers, including informal and domestic workers, and migrants. Specifically, structural adjustments in the workplace, lower participation in the labor market, and emerging financial dislocations are likely to give rise to scarring effects affecting output. Avoiding a dramatic setback in output is a collective responsibility that requires more than ever concerted efforts and cooperation between advanced, emerging, and developing economies alike, as well as multilateral organizations. A strategy to expand the health and social safety net is more urgent than ever to preserve employment and protect the vulnerable. Countries should adapt their policy frameworks to support the economy, keeping a focus on how to return to a path of stronger, equitable, and resilient growth, avoiding the premature withdrawal of supportive measures.

We agree with the WEO recommendation that policy makers should continue to support the economy. However, the precarious outlook for emerging market and developing economies (EMDEs) portrayed in the WEO is a cause for concern, especially for those still facing suboptimal healthcare services, high informality, and a decline in remittances. Estimates of potential GDP growth for the 10 largest emerging market economies (EMEs) already show a larger decline than for AEs relative to the January 2020 WEO. As the Fund resumes its regular surveillance work, it could help country authorities to monitor the emergence of macroeconomic imbalances and deviations from a sustainable growth path, as well as to identify the most suitable corrective policies.

However, in terms of fiscal policy, it is imperative to create additional room to meet the spending needs, namely health and education spending, as well as supporting firms and the most vulnerable sectors of society. Avoiding a premature withdrawal of stimulus will be particularly challenging for EMEs where fiscal space is rapidly narrowing. Public debt has significantly increased this year, reducing the room for maneuver, especially for countries with significant debt legacies. Rising private sector debt entails additional concerns, including the risk of migration of debt from the private to the public sector. Improving debt transparency should be a priority, including from debtors and creditors. Continuous assessment of fiscal instruments and policies by the Fund would contribute to timely decisions before fiscal sustainability is significantly compromised. Besides, we fully concur with the need for enhancing and building stronger institutions.

There is no alternative to maintaining an accommodative stance given the urgent need for stimulus during the recovery, as highlighted in the Global Financial Stability Report (GFSR). On the positive side, market stress has been contained thanks to central bank programs to support liquidity and Fund/Bank lending complemented by government guarantees, and the implementation for the first time of asset purchase programs by some EMEs. These measures have prevented the procyclical behavior of credit, and liquidity shortages, helping to contain the solvency risk, particularly in small and medium-sized enterprises (SMEs). However, private sector defaults are likely to increase, deteriorating the balance sheet of banks as non-performing loans materialize which, coupled with a reduction in bank capital buffers, pose a risk. Regulators should remain as flexible as possible, while maintaining the best standards in transparency and supervisory practices.

Medium-term policies should include sustainable and growth-supportive fiscal policy, raising public sector investment (and its efficiency), removing lingering trade policy, and ensuring the adequate multilateral support in critical areas. In this regard, fighting the health crisis should continue to be a priority. Efforts to manage debt sustainability in a cooperative environment, as currently under the Debt Service Suspension Initiative (DSSI), should continue, with the involvement of all relevant parties. We count on the Fund to continue to provide high-quality analysis to understand the gravity of the crisis as it evolves, making sensible and timely recommendations, including through capacity development, and providing the needed financial resources to countries that request them.

Latin America and the Caribbean (LAC) is the most unequal region of the world and was hit hard by the pandemic, provoking a dramatic health crisis. By the end of September, as presented in the Western Hemisphere Department's Regional Economic Outlook (WHD REO), this region, with no more than 8.2 percent of the global population, had 28 percent of the world's confirmed Covid cases and 34 percent of all Covid-related deaths. The number of new cases continues to rise in some countries, while it has stabilized in others. The answer to the pandemic in LAC poses an additional challenge for policymakers as they must establish measures adapted to the heterogeneity of their population.

The adopted policies in LAC, as in the rest of the world, were directed to country lockdowns and the closure of borders, which provoked a downfall in economic activity and a reduction in trade, while

financial conditions remained stable as result of swift responses from the economic, monetary, and financial authorities. The growth rate projected for the region in 2020 shows one of the largest contractions in the world with high heterogeneity. The virus increased unemployment due to a high percentage of micro, and SMEs in total firms, informality, and the impossibility of working remotely in many activities. Those who suffered most were women, younger people, and low-skilled workers. Since May, recovery has been slow and unevenly buttressed on a strong fiscal support amounting to 8 percent of GDP on average.

Finally, countries should aim at preparing for a post-pandemic future of high-quality growth, promoting inclusion, enhancing employment opportunities, and encouraging green investments. We appreciate the staff's excellent and useful work embodied in the October 2020 WEO, GFSR, Fiscal Monitor (FM), and WHD REO reports.

### **Catalyzing a resilient recovery and the Managing Director's Global Policy Agenda**

We fully agree with the analysis and main recommendations posed in the Global Policy Agenda (GPA). In particular, the importance of accelerating universal access to vaccines and the Fund's commitment to support international cooperation in this area, as well as actions to reduce trade barriers on medical supplies and equipment. "In a pandemic, the global economy is only as strong as its weakest member" (GPA). Cooperation and solidarity are of the essence. In this regard, the Fund should also, on humanitarian grounds, support countries' requests for financing through the Rapid Financing Instrument or Rapid Credit Facility for medical supplies and equipment acquisition.

Challenges related to the pandemic are numerous and vast. Therefore, a strict prioritization is needed, trying first to concentrate on the immediate health effects of the crisis, and then on what will remain once the pandemic is over, which will eventually be related to fiscal and financial imbalances, poverty, inequality, gender disparities, and climate change activities. In this vein, we also support the IMF's work agenda and operations, especially regarding debt vulnerabilities.

It is critical to have the Fund's advice on the reopening of economies and the best ways to unwind exceptional policy measures. The resumption of bilateral surveillance activities and the Fund's work and advice on how to deal with sovereign debt, which for some members will be an unbearable burden, is essential.

We look forward to the further advances of policies to bolster aggregate demand and to promote structural change that support the recovery, as well as the development of tools to invest in structural transformation to increase productivity, create employment, leading to a greener and more inclusive economic growth. The pandemic has substantially accelerated processes related to digitalization, and it is vital to understand that its effects will materialize now and in the near future, in order to develop, among others, policies on fintech, financial inclusion, monetary policy, payment systems, and the international monetary system. We welcome the Fund's commitment to expand work on social and governance issues, as key levers in reducing inequality and strengthening social cohesion, including tax policies.

Facts and trends worldwide absolutely indicate the unavoidable necessity of addressing climate change and we are encouraged by the Fund's efforts to further strengthen its policy advice, which, of course, should include advancing its assessment. We are also pleased to see the Fund's commitment to EMDEs. While most of them lack ample monetary and fiscal space, and will conclude the pandemic with many more vulnerabilities.

The Fund's commitment to provide policy advice and financial assistance, as needed, is key to boost confidence. We welcome the intentions to adapt the Fund's lending toolkit, including by helping members

respond to uncertainties brought about by the pandemic and analyzing new lending alternatives. We also support the utilization of special drawing rights (SDRs) for low-income countries and the support of small developing states, a new generalized allocation of SDRs, and an extension of the G20 DSSI, while ensuring the involvement of private sector creditors in this initiative. On trade, we support the Fund in continuing to promote international cooperation and trade as an engine for restoring global growth. Overall, the Fund needs to secure resources so as to remain a quota-based institution. In this regard, we look forward to a swift discussion and implementation of the 16<sup>th</sup> General Review of Quotas.

Finally, we support the call to the international community to do all it can to support the most vulnerable.

## Argentina

### **Covid-19 poses a challenge to a delicate economic and financial situation**

The new administration has worked relentlessly to overcome a delicate economic and financial situation. The Covid-19 shock added pressure to what was already a critical scenario. Meanwhile, the government has also solved one of the most difficult problems it was facing: the restructuring of the foreign currency denominated debt under external and domestic law.

In recent years, the economic performance of our country has not been as satisfactory as expected. Well before the pandemic, GDP per capita was already lower than it was eight years earlier. The lack of dynamism of exports and the widespread propensity to save on foreign currency led to a repeated economic crisis due to a lack of foreign currency. After a brief opening to the international credit markets between 2016 and 2018, a sharp reversal of capital flows took place. The foreign exchange constraint and fiscal problems worsened, and Argentina faced a debt crisis with deleterious implications: a deep economic contraction, rising inflation, and growing poverty and unemployment rates. The Covid-19 shock aggravated all the economic problems.

In the context of this crisis, before the pandemic, Argentina 's policies were oriented to generate conditions to deal with the social and economic emergency, bring macroeconomic stability, and ensure public debt sustainability. Economic data reveals some improvement during February 2020, but the Covid-19 global pandemic declared by the WHO disrupted economic activity since March, when Argentina took early action to contain the virus by imposing a strict lockdown. Economic policy measures taken so far entail a fiscal stimulus, the amount of which will be conditional on the length and impact of the quarantine (as detailed in our chair's IMFC statement in April). Between February and June 2020 economic activity fell by 12.9 percent, with a slow recovery starting in June.

### **The immediate priorities of the government**

The completion of our recent debt restructuring deal puts an end to our recent cycle of unsustainable debt, lowering interest rates, and reducing the burden of debt repayment for several years. **This creates additional breathing space to manage the devastating impacts of the pandemic.**

To resume growth in the post-pandemic stage, the government has three main priorities, the fulfillment of which simultaneously become a *sine qua non* condition:

1. Take care of the lives and health of the population.
2. Protect the capacities and income of households and businesses.
3. Reactivate the productive system and boost employment.

Synchronization of these priorities is not an easy task given the uncertainty and instability of the situation, which is typical of internal and external conditions which are subject to unexpected fluctuations in the absence of a definitive solution to the pandemic.

### **1. Take care of the lives and health of the population**

Protecting the lives and health of the people has been the government's top priority; this became the organizing axis of the rest of public policies. Early on, the government diagnosed the severity of the pandemic phenomenon and acted accordingly, through strengthening the health system and the implementation of isolation and social distancing measures. This was supported by the inexhaustible efforts of health and safety workers and various essential areas with very high exposure to the virus. These measures jointly prevented a collapse of the health system and allowed Argentina to prevent thousands of deaths otherwise resulting from a lack of medical attention.

The construction of better health networks has been a priority in the management of the pandemic. Extraordinary articulation and coordination channels were generated through the promotion and strengthening of multiple vectors: political-health (provinces-municipalities), health services (public-private-social security), human resource planning, laboratories, scientific research, financing, and information and knowledge management. To guarantee universal care for the population, the Ministry of Health created the National Fund for Health Equity which finances the internment in public and private providers of around 18 million people (40 percent of the population) without health insurance.

*Transparency in the management of the health emergency has been another focal point.*

Finally, the government reinforced the containment of people in situations of gender violence and granted special traffic permits to victims of gender violence, among other actions aimed at ensuring that isolation and social distancing measures could be carried out with as little risk as possible.

### **2. Protect the capacities and income of households and businesses**

The early decision to protect the lives of all inhabitants was conceived hand in hand with economic and social assistance measures needed to mitigate the impact of the lockdown on the normal functioning of the economy and other essential aspects of community life. In this regard, the pandemic represented an unprecedented challenge for **education**. The suspension of in-person school activities across the country forced a rapid reorientation of the budget in order to address the consequences from such a situation, deploying actions to guarantee, within the restricted limits of reality, pedagogical continuity. Incidentally, several actions were deployed within the framework of the "We continue to educate" program. In parallel with these policies born and implemented in the framework of the health emergency, more than 42 million educational booklets were printed and distributed, which allowed pupils and students without internet connection, and those in rural and isolated areas or in a situation of socio-educational vulnerability to continue the learning process.

Regarding the economic implications, this year the government is deploying an assistance and containment package composed of fiscal resources, amounting to an equivalent of 4.9 percent of GDP. The measures to stimulate credit for companies and families will amount to almost 1.9 percent of GDP. The public sector will have invested direct and indirect resources into the economy for an equivalent of 6.6 percent of GDP in 2020. Among the actions and programs implemented in the framework of the health and economic crisis caused by the Covid-19 pandemic, two programs stand out, given their size and innovative nature and that they are unprecedented in Argentine history: the Emergency Assistance Program at Work and Production (ATP) and Emergency Household Income (IFE).

The ATP finances 50 percent of workers' salaries whose companies were affected by the pandemic. It was implemented to protect the productive capacities of the economy and the income of workers in the private and independent sector. It has benefited 236,000 firms, which represents 43 percent of all firms registered in the country, 99.5 percent of which are SMEs that employ 2.5 million workers.

The IFE, a monetary transfer that benefited almost 9 million people and targeted informal and unemployed workers, was a key tool to contain the effects of the pandemic on the most vulnerable population. This program is one of the largest and most far-reaching transfer measures in the history of Argentina. According to a joint estimate by the Ministries of Economy, Productive Development and Labor, Employment and Social Security, the IFE prevented between 2.7 and 4.6 million people from falling into poverty. This is because it maintained a minimum income floor in sectors that were not reached by other social security tools. While the Universal Child Allowance (AUH) reaches 60 percent of the households in the poorest decile, with the IFE it was possible to benefit 90 percent of those households (the difference is explained by those households where there are no children). The IFE had a widespread reach in all provinces of Argentina, following the federal criteria of the government throughout the development of the pandemic. Among those who received the IFE, 55.7 percent are women, while 61 percent are young people under the age of 35. These are the two population groups that exhibit the worst working conditions and are overrepresented in poverty and extreme poverty.

Simultaneously, a set of measures were deployed with the aim of boosting credit towards the productive sector, as a form of assistance, both to cover expenses during the period without activity because of the lockdown, as for adjustments in production, establishment of sanitary protocols, and recovery of activity for the reopening period.

### **3. Reactivate the productive system and boost employment**

During this first stage of the crisis, the government has worked to improve the initial conditions of the Argentine economy. As stated previously, a good part of the efforts of the public sector were aimed at sustaining the capacities of companies and workers through direct public spending and soft loans.

These initial conditions for economic recovery will be determined by (i) the level of idle installed capacity of the productive sector, (ii) the financing capacity of the public sector, and (iii) the capacity to generate confidence in order to encourage the demand for investment by companies and household consumption in a context currently marked by instability and the possible persistent effects of the pandemic on the global and domestic economy.

Regarding public investment, the objective is to promote a substantive recovery of capital spending in the public sector as a dynamic factor for economic activity and employment, with a federal perspective and with priorities focused on the extension of access to basic needs and rights. Even in a far-from-ideal fiscal context, the action plan for 2021 includes significant efforts in terms of public investment with the aim of gradually recovering levels in relation to GDP consistent with a growth trajectory.

#### ***Challenges ahead – preparing for the future***

##### **A framework for structural change and the IMF program**

The government is focused on the construction of a framework of general stability that reassures the economy and allows the country to strive towards the dynamic, inclusive, stable, federal, and sovereign development model proposed. The normalization of Argentina's debt situation with the private sector in both local and foreign currency has been a fundamental contribution to the sustainability of the economy.

However, such normalization is a process that has not been completed. The government finds the need to redefine the commitments assumed with the IMF in the framework of the Stand-By Agreement signed in 2018, which implied disbursements of around USD 44,000 million. Considering the current global and domestic juncture, renegotiating the terms of the agreement with the Fund should incorporate new macroeconomic prospects and a common understanding of the specific needs of the local economy. Argentina is committed to meet the repayment of this debt in a socially, economically, and politically sustainable way.

The dialogue with the IMF is underway. Although the characteristics of this agreement will be a result of the negotiations that will take place over the next few months, the government will be consistent with its initial vision about the direction that Argentina should take: no course of action that postpones production, jobs, education, health, or science and technology, or that reinforces structural inequality gaps, will be validated. It will be a program made by and for Argentina to solve long-standing problems. Furthermore, to ensure ownership, the program to be agreed with the Fund will be sent to Congress for its approval.

### **Stabilization, recovery, and reconstruction**

Against the background of the pandemic, the government is defining a stabilization, recovery, and reconstruction path. On this path, macroeconomic policy has a key role to deal with this situation of economic emergency aggravated by the pandemic, in which two principles are essential.

The first principle is that **macroeconomic stabilization is only possible if economic activity recovers first**. In a context of a deep recession, the state plays a central role in promoting economic recovery. In a context of multiple constraints, including a limited financing capacity by the state, an expansionary fiscal policy scheme is proposed to recover the level of activity. Argentina must undergo profound structural changes to generate a sustainable economy that guarantees each worker the possibility of having a decent formal job and allowing each company access to credit, investment, to boost production, exports, and added employment.

The second principle is that **fiscal sustainability will require consistent efforts toward a fiscal balance compatible with an inclusive growth path**. At the same time, fiscal policy aims to guarantee the protection of the most vulnerable social segments in the current economic situation. In this way, conditions will be established for the development of productive sectors with the potential to generate growth in levels of income, employment, productivity, and exports.

To this end, it is necessary to turn towards a sustainable development model in economic, social, and political terms that simultaneously meets five structural conditions: inclusion, dynamism, stability, federalism, and sovereignty.

The government is working intensively on the revenue side to include the five structural conditions mentioned above harmonizing the Argentine tax structure in such a way as to:

- i) Consolidate a more progressive income distribution.
- ii) Aligning the incentives that the tax system gives the private sector with a focus on domestic production, exports, and the generation of decent formal employment.

### **Macroeconomic forecast**

For the macroeconomic scenarios presented, it should be considered that crisis contexts such as the current one affect the ability to make reliable economic forecasts in a medium-term perspective, due to the volatility that crises impose on the main macroeconomic variables. Hence, the figures present are



guidelines; they show an average scenario in which a gradual recovery in economic activity and a progressive reduction in the inflation rate are observed. Likewise, the recovery scenario for the coming years will be fundamentally based on an increase in investment and consumption.

### **Foreign exchange market**

On the foreign exchange market front, the gradual reconstruction of the local sovereign debt market and the lower level of the primary fiscal deficit will allow for a sustained reduction in the needs of financing that the Treasury covers with Central Bank resources, a process that will collaborate with the decompression of a part of the current tensions that are verified in the exchange market. This normalization process is also essential to create greater incentives to stimulate savings in domestic currency. However, the transition to a situation of greater stability in the exchange market is a process that will require time and properly aligned signals. With a not very flexible supply of dollars in the short term, the financing of a growing volume of imports must be guaranteed to increase productive investment and the incorporation of technology.

The government will have at its disposal all the needed tools to guarantee an exchange rate path compatible with progressive disinflation and a high level of external competitiveness. The Central Bank of Argentina has a sufficient level of international reserves and the possibility of expanding them through contingent support agreements with various monetary authorities to intervene in the exchange market. For its part, the public sector debt-restructuring process has meant a recapitalization for many state agencies, which could eventually be translated into a powerful new instrument for managing the exchange rate.

### **Monetary policy**

Monetary policy will continue to pursue the double objective of promoting the leverage of productive investment and channeling private sector savings towards instruments in local currency. In practice, the recovery of acceptable levels of monetary sovereignty will require an interest rate that preserves the purchasing power of savers. Intra-governmental coordination is of the essence, which through instruments of rate subsidy and guarantees ensures the financing of production and consumption, in particular SMEs and families. The compatibility of high interest rates for stability and soft credit for production, is a challenge for the production policy.

### **Inflation**

On another level, high inertial inflation could cause tensions in macroeconomic dynamics once the economy starts to grow. **Income policy** is a powerful tool to coordinate a gradual decline in inflation while prudently boosting aggregate demand. Consequently, in 2021 work will be carried out to generate multipartite economic and social agreements in which the state, the business community, and the entire range of workers' representatives converge. It will not only be an opportunity to manage the distributive conflict with a medium and long-term perspective, but will also be relevant to design, implement, and consolidate state policies that transcend government cycles and allow Argentina to shore up the systemic competitiveness of the economy.

This coordination framework to achieve stability will allow the country to undertake a sustainable economic recovery which, at the same time, does not create conditions for a future crisis, as has recurrently happened in past decades. Likewise, the greater tranquility to be reached will enable the implementation of a new structural transformation agenda for the Argentine economy in which the state and the private sector must converge organically. This agenda will have the following general guidelines: production and development financing, export promotion, knowledge of economy and technological

development, sustainable green growth, regional development, and social inclusion with a gender perspective.

Regarding the last point, it is worth noting that this is the first time in the country's history that the national budget has a gender perspective. That means the budget was made under a methodology that allows us to focus on the government's effort to close gender inequality gaps while expressing concrete initiatives of an inclusive and diverse political definition.

**Finally**, an average GDP growth scenario is expected to go from -12.1 percent year-on-year in 2020 to 5.5 percent year-on-year in 2021, to 4.5 percent in 2022, and to 3.5 percent in 2023, with a deviation of 0.5 percentage points higher or downward between 2021 and 2023. Inflation is expected to gradually decrease from 32.0 percent year-on-year in December 2020, to 29.0 percent in 2021, to 24.0 percent in 2022, and to 20.0 percent in 2023, with a deviation of 4 percentage points up or down between 2021 and 2023.

## **Bolivia**

### **1. A vulnerable situation before the pandemic**

Since the beginning of 2020, Bolivia has been facing four weaknesses, which are still currently present:

- A fragile democracy, which is a result, in great part, of the previous Administration's illegitimate attempts to continue in office, especially since 2016, when it refused to accept the result of a national referendum. This prevented the reelection of the former President for a fourth term and a fraudulent attempt to alter the results of the general election of October of 2019.
- Economic weakness deepened due to the slowdown of GDP growth from 6.8 percent in 2013 to 2.2 percent in 2019, as well as an average fiscal deficit of 7 percent of GDP, mainly due to inefficient management of public investment.
- Social fragility is apparent because of the stagnation in the rate of poverty reduction. Currently, one third of the population remains below the poverty line, while the middle class presents serious vulnerabilities due to the high degree of informality in the labor market.
- A lack of facilities in the Bolivian health system as reported by Johns Hopkins University.

These four issues set up a complex scenario. In fact, the well-known consulting firm Oxford Economics rated Bolivia as the most vulnerable country to Covid-19 in terms of health and economics in April of this year.

### **2. The economic impact of Covid-19**

As in the rest of the world, Covid-19 changed the evolution of the Bolivian economy. Indeed, in the face of the outbreak of the pandemic, economic activity declined rapidly and deeply, with an expected annual fall of around 6 percent of GDP in 2020.

Lockdown measures adopted to face the pandemic distressed the labor market increased unemployment and inactivity by seven percentage points of the economically active population above the natural rate of unemployment. Furthermore, households' income fell by up to two thirds due to the lockdown in April, although it recovered to 70 percent in July. Lower income would have resulted in an expected rise in poverty, which was mitigated by the government's direct cash transfers to the population.

The fall in economic activity mixed with measures to limit the impact of the pandemic on the population have had fiscal impacts which will exacerbate previous imbalances. In fact, the projected fiscal deficit will rise to 12 percent of GDP in 2020, far above the expected 6.6 percent at the beginning of the year.

### **3. Policies to face the pandemic**

Covid-19 reached Bolivia on March 10. Due to the low capability of healthcare system, some immediate interventions were enacted such as quarantines, school closures, and bans on international and national flights to limit the transmission of the disease.

International studies indicate that, without these measures, most of the population would have been infected with a projection of 50,000 deaths, according to the Imperial College of London. Consistent with this, economic conditions deteriorated deeply.

In fact, this disruption could imply a reversal of at least five years in the average standard of living in Bolivia, measured by per capita GDP. For these very reasons, the Bolivian government enacted several measures to face this crisis, taking care of lives and livelihoods.

Regarding monetary policy, the extent of liquidity injections made by the Central Bank of Bolivia is higher than 15 percent of GDP through new lines to support the liquidity of the financial system and deferral of loan payments. Furthermore, it has the potential to reach 22 percent of GDP this year.

Concerning fiscal policy, direct transfers to vulnerable households, tax payment deferrals, and new credit lines for firms have involved a stimulus of 7 percent of GDP.

It should be noted that these measures have been taken and developed with only domestic resources, given the blockade of Congress, for political reasons, against the entry of foreign aid and international credits to face the pandemic.

### **4. Challenges after the pandemic**

A global and national worsening of economic conditions since April revealed the need for new policies. Faced with more adverse conditions, the National Employment Reactivation Plan (NERP) has been formulated with three axes: i) funds for working capital; ii) assistance to the most affected sectors; and, iii) public efforts to create temporary employment. Due to domestic political restrictions to access external financing, this plan is in its initial stage.

A new government will be elected through a democratic general election on October 18, 2020. The next administration will oversee the implementation of the NERP to mitigate second-round effects of the pandemic in several economic sectors.

The enactment of this whole plan requires financial resources to preserve employment. Furthermore, budget support will be required for the continuity of the basic functions of the public sector, mainly in social areas.

The delay in the execution of the NERP could imply serious and irreversible systemic problems in the economy. Therefore, assistance from international organizations will be needed. Thus, external financing will be crucial to maintain stability and resume growth of the Bolivian economy. Consequently, the country will be able to move towards a successful path to sustained development and strong democracy.

## 1. Overview

The evolution of the macroeconomic scenario in Chile and elsewhere continues to be closely determined by the evolution of the Covid-19 pandemic and the applied containment measures. After a sharp drop at the beginning of the second quarter, in recent months the Chilean economy has shown signs of stabilization, combining improvements in some sectors badly hit by the pandemic, with further deterioration in others. This has shadowed contagion dynamics, which dropped significantly since mid-July, to stabilize at 1,000-2,000 cases a day and some 14,000 active cases in the last two and a half months. This has eased pressure on the health system, which has further developed its capacity to test, trace, and isolate as well as to treat difficult cases.

Given these improvements, authorities have set in motion a gradual and evidence-based process to lift lock-down restrictions. The Government plan is structured in five steps that are applied selectively at the geographical level. Territories can move back to more constrained stages if indicators were to worsen. The total population in confinement dropped from 54 percent at the peak in July, to 21 percent by end-September.

Despite mentioned signs of stabilization, the economic impact of the pandemic has been very deep, reflected not only in a dramatic contraction of sales and output but also in a major shock to household earnings. In the second quarter, the economy posted a contraction of 14.1 percent year-on-year, the worst record in several decades. In the labor market, 1.8 million jobs have been compromised, out of a labor force close to 10 million.

The major economic blow from Covid-19 prompted an equally strong policy response at the fiscal, monetary, and financial level. A number of measures have been aimed at preventing liquidity constraints turning into widespread solvency problems for firms, as well as to cushion the impact on household disposable incomes and private consumption. Special liquidity measures, government loan guarantees, and regulatory forbearance, combined with the solvency of the banking system, have pushed bank lending to firms to grow at more than 10 percent in real terms, contrasting with its pro-cyclical behavior in previous crises. Close to a quarter million loans have been channeled to SMEs, combined with 1.5 million rollover operations for commercial, consumption and mortgage loans. There is evidence that this access to credit has sustained the operational continuity of businesses and helped mitigate the drop in investment. In turn, government cash transfers for households picked up since June, reaching more than 3 million households currently. Thus, the net effect of the variation in labor earnings and Government transfers would move from -22 percent in the second quarter to -3 percent in the third quarter.

## 2. Macroeconomic forecasts

Real GDP growth is projected to fall between 5.5 to 4.5 percent in 2020, improving on the June outlook, in line with the global signs of bottoming out reflected in the October 2020 *World Economic Outlook*. In the specific case of Chile, this combines a less drastic decline in the second quarter with a recovery during the second half of the year, on the back of stable terms of trade, growing exports, a gradual rolling back of sanitary constraints, a recovery of consumption, a resumption of suspended investment projects, and sustained impulse from fiscal and monetary policy. In 2021 real GDP growth will return to positive territory estimated within 4 and 5 percent. Thus, while Chile's GDP contraction in 2020 will be about half that of the rest of Latin America, the output gap opened in the first half of the year may take until 2022 to close, while per capita income would return to its pre-crisis levels only by 2023. Even by then, the gap with respect to projections in September 2019 would remain close to 10 percent, reflecting the lasting economic loss caused by the social crisis at the end-2019 and the Covid-19 pandemic.

While the relaxation of confinement measures and increased mobility will help activity to recover, some sectors will still face substantial challenges due to lasting social distancing standards and practices. Similarly, employment recovery may not be symmetrical nor balanced across sectors. Precautionary household savings may increase, and firm investments may be held back by uncertainty, either from the evolution of the pandemic, social tensions or by the Constitutional process agreed last November. So substantial policy support will remain necessary to support recovery, adaptation of most affected sectors, preserve financial stability, and contain uncertainty.

### **3. Inflation, Central Bank measures, and monetary policy**

Inflation—total and core—will converge to the 3 percent target by 2022, and its level will not fall below 2 percent annually. Although in the short-term this trend runs somewhat above previous forecast, largely due to the recovery in private consumption, into the medium term, its main determinant continues to be the lower accumulated activity. Two-year inflation expectations remain anchored around the target.

To cope with the Covid-19 crisis, the CBC adopted or expanded a variety of measures in four areas: (i) on conventional monetary policy, a policy rate cut by 125 basis points to its estimated effective lower bound of 0.5 percent back in March—a highly expansionary rate measured in real terms; (ii) on lending promotion, two programs that amount to USD 44 billion, equivalent to nearly 20 percent of GDP: (a) a bank lending enhancement program (FCIC), providing 4-year loans at the policy rate to commercial banks, conditional on them lending forward to firms, and (b) an asset purchase program, including repurchasing longer-term CBC bonds and purchasing bank bonds at market prices; (iii) on market stabilization, a number of measures to facilitate portfolio adjustment at a time of changing market perceptions, and (iv) strengthened its external liquidity position and broadened its policy toolbox by signing an agreement for a precautionary *Flexible Credit Line* (FCL) with the IMF, equivalent to nearly USD 24.0 billion, a figure close to 60 percent of the International Reserves, for two years. Also, at the end of June, the New York Federal Reserve accepted the registration of the CBC in the FIMA REPO Facility. Finally, the CBC agreed with the People's Bank of China to increase the *Bilateral Agreement on Swap of Renminbi/Peso Currencies* (RMB/CLP) signed in 2015 for facilitating the settlement of trade operations in RMB/CLP, to RMB 220 billion (more than USD 7 billion) for three years.

In August, a Constitutional Reform was approved to allow the CBC to purchase government bonds in the secondary market, on a temporary and exceptional basis, and for financial stability purposes only. As a result, the future potential for bond purchases in dealing with stress episodes in financial markets, doubles. Based on the toolkit deployed, and potentially available, and the economic outlook, the communication of the CBC is that the monetary policy will remain highly expansionary, maintaining the policy rate at its 0.5 percent minimum for most of the two-year policy horizon. In addition, unconventional measures will be renewed or expanded as needed.

### **4. Fiscal policy**

Since the beginning of the pandemic, the Government has taken bold actions to, first of all, protect lives and contain the spread of the virus, and then safeguard jobs and the economy. It has responded by delivering an unprecedented level of fiscal stimulus amounting to more than 7.5 percent of GDP, targeted to support families, businesses and public services, including providing direct income support to more than 3 million families. In addition, has helped over half a million businesses through tax deferrals and state-guaranteed loans, and protected jobs through amended short-time work and temporary lay-off schemes.

The Government remains committed to easing short-term economic strains and to revitalizing the economy going forward. As lockdown measures become less stringent, fiscal actions will be increasingly

redirected towards supporting the economic recovery. In August, new fiscal measures were announced, including a temporary income tax reduction for SMEs from 25 to 10 percent and an extension of instantaneous depreciation of 100 percent of capital expenditure, both during 2020-22. In September, to encourage temporarily laid off employees' return to work and also incentivize new hires, the Government started a transitory subsidy to employment. The state-guaranteed loan scheme remains in force to support the credit channel during the economic recovery. Also, public investment will increase 15 percent in 2021 compared to 2020.

Finally, it is worth highlighting that the fiscal policy response is based on an agreement reached between the Government and the opposition parties in Congress, set to frame the Covid-19 emergency plan within a sustainable medium-term fiscal path. This agreement established a *Covid-19 Emergency Fund* to finance all fiscal relief and stimulus measures for an amount of up to USD 12 billion, equivalent to almost 5 percent of GDP. The Government has flexibility to use these resources during the 2020-22 period. At the same time, the agreement establishes a sunset clause to ensure that these extraordinary policies phase out after this period, and the fiscal budget returns to a consolidation path to stabilize the public gross debt burden below 45 percent of GDP.

## **5. Challenges ahead**

Several challenges emerge in transitioning towards recovery. First, recovery of the labor market, severely affected, is of utmost importance to support the well-being of the population. The upturn of employment needs to be approached with urgency, determination and realism, and with the active participation of firms of all sizes and sectors. Second, smoothing the transition of households and firms from a phase of emergency support to a phase of reactivation, while incorporating the new challenges arising from social distancing, will require a careful calibration of the timing to terminate the support programs. Third, the need to recover, restructure and/or reconvert the sectors most affected by the pandemic and all those permanently affected by the new patterns of interaction with users, customers, and suppliers. This will require investments in infrastructure, adaptation of the logistics chain, and incorporation of technology which will hardly occur based only on to the operation of market forces. Fourth, the materialization of investments, productive adjustments and increases in activity levels will require adequate financing. The mere dynamism of income will not be enough, so it will be essential to ensure a sustained flow of credit, under affordable conditions, by a financial system capable of performing its intermediation and risk distribution functions efficiently. Fifth, it will be necessary to significantly reduce uncertainty, which is about to complete a year well above its historical levels. These degrees of uncertainty have different causes, but we must be clear that the Chilean economy and society will hardly be able to withstand its protraction or intensification without more permanent damage to entrepreneurship, investment and employment.

Lastly, a more structural challenge will be to raise—or at least maintain—long-term growth capacity. The trend growth estimates for our economy have not been updated yet, factors have appeared in recent months that add risks to the downside. Higher costs associated with security and social distancing in the provision of services, as well as higher transaction costs reduce productivity, while higher hiring costs, low investment and business bankruptcy may negatively affect the availability of work and capital. These are not irreversible phenomena, and in fact innovation and technological development could have a compensatory effect. Nevertheless, the challenge today is surely greater than it was a year ago.

At the beginning of 2020, the different short-term indicators of economic activity in Paraguay displayed good dynamics, in line with the GDP growth estimate of 4.1 percent from December 2019. However, as of March, with the confirmation of the first cases of Covid-19 and the implementation of the necessary containment measures, the dynamism of the economy suddenly slowed. The greatest negative impact was observed in the services sector, especially in tourism-related activities and those that involve social interaction (hotels, restaurants, border trade, services to households, etc.). In this context, growth forecasts were revised downwards to a rate of -2.5 percent in April of this year and to -3.5 percent in July. However, it should be noted although economic activity had a sharp fall in April, it has recovered at a higher rate than expected, driven by the greater expansion of the primary sector and construction, and the lower fall of manufacturing and services, with respect to the forecasts at the beginning of the pandemic. With this, the Indicator of Economic Activity of Paraguay (IMAEP)<sup>1</sup> accumulates a slight decrease as of July (-0.3 percent), significantly lower than the retractions observed in other countries in the region. On the demand side, the Large Companies Sales Indicator (ECN) has also recovered, due to the improvement in the sales of supermarkets, construction materials, and durable goods (vehicles and home equipment), and accumulates a variation of -1.6 percent as of July.

The weakening of domestic demand in the second quarter, mainly of consumption, has also been reflected in prices. Headline inflation and its core measures registered lower rates during this period, mainly due to the reduction in food and energy (fuels) prices. At the beginning of the year, the annual variation of the Consumer Price Index (CPI) was 2.8 percent, then decreased to stand at 0.5 percent in June, and rebounded to 1.1 percent in July, and to 1.6 percent in August. Nevertheless, inflation has remained below the lower zone of the tolerance range of 4.0 percent +/- 2 percentage points (between 2 percent and 6 percent). The cumulative rate of headline inflation as of August is 0.2 percent, while the average year-on-year inflation was 1.7 percent. As for the underlying inflation and underlying X1 annual rates, so far, they averaged 1.9 percent and 2.5 percent, respectively.

Given the lower inflationary pressures, as well as the evolution of economic activity and domestic demand indicators throughout 2020, the Central Bank of Paraguay (BCP) considered there was enough room to ease the monetary policy stance, lowering the reference rate by 325 basis points in the meetings of, March, April, and June. Thus, the reference rate went down from 4.00 percent to 0.75 percent annually, remaining at that level as of September.

The nominal exchange rate of Paraguay exhibited a similar behavior to the dynamics observed at the regional level so far in 2020. As of September 21st, the Paraguayan Guaraní depreciated by 9.2 percent in annual terms vis-à-vis the United States dollar and registered a cumulative rate of depreciation of 7.9 percent. The participation of the BCP in the exchange market has been limited to the attenuation of sharp volatilities of the exchange rate, without shifting the trend in market fundamentals. On the other hand, net international reserves (NIR) stand at consistent liquidity levels to face any sudden fluctuations in the exchange rate. As of September 18, 2020, the NIR reached around 8.9 billion US dollars, which represents around 25 percent of the GDP estimate for this year.

As for public finances, the negative consequences of the pandemic and the necessary containment measures of COVID-19 contagion affected the performance of economic activity and domestic demand in 2020, thus lowering tax revenues, including those from imports. As of August, cumulative tax revenues registered a decrease of 11.7 percent compared to the same period of 2019, while expenditures

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<sup>1</sup>The acronyms in this document correspond to the nomenclatures in Spanish for specific local indicators.

increased 11.3 percent. The fiscal deficit up to August is around 3.4 percent of GDP, and the annualized deficit is 5.1 percent of GDP. This result is also explained, in part, by a significant increase in public investment.

Despite the adverse economic context, the financial system has remained stable, solvent, with adequate levels of liquidity and weaker indicators of credit quality and profitability, but in line with the economic and financial situation of recent months. The favorable macroeconomic and financial conditions of the country at the beginning of the spread of Covid-19 have allowed the BCP and other public financial institutions to act proactively, which has been reflected in the multiple measures adopted to meet the financing needs of people and companies. In this regard, the implementation of financial measures of easing credit conditions has been promoted both to maintain the customer's credit quality in the financial system and to facilitate the granting of new loans, mainly to micro, small, and medium-sized enterprises (MSMEs), and independent workers. In addition, the terms for the sale of assets awarded or received in payments by financial entities were extended so that they can carry out transactions under more favorable conditions and maintain the value of the assets, among other measures.

Regarding financial regulation, Law No. 6,588/2020 was recently enacted, which regulates the commissions charged for commercial operations through electronic means of payments. In this regard, this regulation has the purpose of facilitating trade, protecting consumer rights, and promoting competition.

Regarding the credit situation, since May 2019, the annual growth rate of total credit slowed down and continued with this dynamic until April 2020. However, in recent months, such behavior has been attenuated by the performance of credit in national currency, which has shown some signs of recovery, in line with the financial measures implemented in the context of Covid-19. In August 2020, total credit expanded 3.2 percent year-on-year, driven by loans in local currency, which increased 12.2 percent year-on-year, and was partially moderated by the annual change of -7.0 percent of loans in foreign currency.

## Peru

### Economic Performance

The strict containment measures and the prolonged and almost generalized closure of economic activities in Peru (a national lockdown was declared from March 16 to June 30) caused a GDP contraction of 17.4 percent in the first half of 2020. This was mainly due to negative growth in non-primary industries (construction, manufacturing, commerce, and services), especially in activities with a high degree of personal interaction. During the same period, domestic demand fell by 15.1 percent, in line with the negative effects of the compulsory lockdown and the increase in uncertainty; while net exports fell mainly due to lower local production and, to a lesser extent, global demand contraction. As the COVID-19 shock gradually unwinds with the reopening of the economy, annual growth is expected to contract 12.7 percent in 2020 and increase 11.0 percent in 2021.

Inflation in Peru has been one of the lowest and less volatile in LAC since 2001 (2.6 percent in 2001-2019). In September, inflation was 1.8 percent and is expected to be slightly below the target range (1 percent-3 percent) of the Central Reserve Bank of Peru (BCRP) during some months over the forecasting horizon (the remainder of 2020 and 2021).

Credit to the private sector increased 14.4 percent year-on-year as of August 2020, mainly due to higher loans to businesses, in line with the expansionary monetary policy stance, liquidity injection operations, and a Government Loan Guarantee Program (GLGP) known as *Reactiva Peru*.



The fiscal deficit is expected to increase from 1.6 percent in 2019 to 9.2 percent in 2020, mainly due to lower government revenues and higher expenditure related to expansionary fiscal policy measures to cope with the Covid-19 shock. Public debt as of end-2020 is expected to reach 34.3 percent of GDP. Going forward, the deficit is expected to decrease as the economy gradually recovers from the negative Covid-19 shock.

The current account deficit (forecasted at 0.1 percent of GDP in 2020 and 1.6 percent in 2021) is below the previous 10-year average (2.8 percent of GDP) and will continue to be sustainable and financed by long-term capital inflows. The trade balance surplus will continue to be positive in 2020 (3.7 percent of GDP), despite domestic and global demand contractions; and is expected to increase in 2021 (4.3 percent of GDP).

The BCRP has taken measures to reduce the cost of financing and prevent the disruption of the payments system: lowering the monetary policy rate by 200 bps to 0.25 percent (its historical minimum) in March and April; providing liquidity to the financial system (through longer-maturity repo operations, which are significantly larger than under the Global Financial Crisis); and easing reserve requirements. These measures include a loan program with government guarantees (8.4 percent of GDP) and liquidity provided by the BCRP through repo operations to support working capital financing. FX intervention, using mainly swaps and BCRP certificates of deposit (CDRBCRP), has reduced exchange rate volatility. The BCRP maintains a significant expansionary stance in a context of anchored inflation expectations and growth below potential, and will continue to take the necessary steps to support the payments system and the credit channel.

Additionally, the BCRP maintains an FX buffer of around six times the country's short-term obligations and 30 percent of GDP thanks to a precautionary accumulation of international reserves. Additionally, Peru has access to contingent funds like the USD 11-billion Flexible Credit Line agreed with the International Monetary Fund. With sound fundamentals and high FX reserves, Peru's external position is one of the strongest among emerging market economies. This enables the authorities to considerably limit the risks from exogenous financial shocks.

Peru's strong and coordinated fiscal and monetary policy response was possible as a result of solid macroeconomic fundamentals, including low debt ratios, one of the largest fiscal spaces in Latin America, and significant external buffers. In a context of unprecedented challenges, the country's solid policy management over the past three decades is being validated.

## Uruguay

With a population of almost 3.5 million people, the first case of coronavirus in Uruguay was detected in mid-March. So far, there have been around 2,100 confirmed cases and 48 deaths. Currently, there are 3 ICU patients, and 250 people still recovering outside hospitals, mainly in their homes. These numbers result from a current rate of testing of more than 600 people per million, and, more importantly, eight positive results in every thousand tests. Whereas it is always possible to improve the detection of new cases, the analysis of the whole group of indicators allows the authorities to declare that the pandemic, so far, is under control in Uruguay.

Since the beginning of the pandemic, the Government decided not to enforce a countrywide lockdown or mandatory stay-at-home order; rather, it trusted citizens to adhere to voluntary social distancing and follow hygiene protocols, by appealing to "*individual freedom with social responsibility*". In parallel, the Government took early and decisive action and sealed-off land borders, closed air traffic—except for

chartered repatriation flights—, suspended all public events and in-person school classes, limited visits to nursing homes, and encouraged citizens to stay home and telework.

There has been an effective coordinated response between the public and private sector and scientific community. The health care system and facilities have been strengthened with increased access to medical equipment, and extensive randomized testing has been carried out. Community tracing has also been key in outbreak areas, such as the border with Brazil and nursing homes. The government developed a roadmap for re-opening various activities, in consultation with scientific experts and private sector representatives.

Uruguay has established a strategy that has been successful in combining freedom with responsibility, scientific knowledge with political leadership, and a powerful combination of health, social, and economic measures based on our traditional strengths.

However, the impact of the pandemic is significant and should not be underestimated. The downfall in GDP in the second quarter of the year was 10.6 percent in year-on-year terms, and the Uruguayan authorities project a decrease of 3.5 percent in 2020. The authorities expect a positive dynamic thereafter, starting with a GDP growth of 4.3 percent in 2021. Once the effects of the pandemic have been overcome, Uruguay will begin a process of improving its public accounts, significantly reducing the projected fiscal deficit of 6.5 percent of GDP this year, to 2.5 percent of GDP in 2024.

Despite the pandemic, the government has continued to work on a series of structural reforms aimed at improving its economic institutions and competitiveness. These changes will include the implementation of a fiscal rule—recently approved in Parliament—, a reform of the social security system, a more proactive international insertion strategy, changes in the way of setting public rates, and a general improvement in the business climate facilitating and encouraging investment.

In summary, Uruguay has been successfully facing the challenges of the situation in relative terms, without losing sight of the long-term structural aspects. The authorities are confident that these policies will allow Uruguay to begin a sustainable development process with a direct and positive impact on the quality of life for the whole population, particularly the most vulnerable.