



CREATIVE



About the Economic Impact of the COVID-19 Crisis on the Region

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Introduction

Economic growth in Latin America and the Caribbean will suffer a drastic negative decline of at least -5%. Some countries will be more affected than others due to the extent of their economic and political vulnerability, which is associated to the economic models they exhibit, and to the time they will take to recover. This memo offers an alternative calculation of the impact of Covid-19 in Latin America and the Caribbean by addressing shifting trends in the external sector and in the informal economy.

The countries more affected are those among with lowest per capita income and countries whose external dependence to exports, tourism and remittances are largest. These countries are also economies with large informal sectors, whose deterioration is not negligible.

The relevance of addressing this issue stems from the fact that the region was already registering a slow growth in 2019 with the possibility of entering a recession in 2020.

With the COVID-19 crisis, the pandemic's economic impact is far more severe that projected by international financial institutions.

ECONOMIC GROWTH 2020, LATIN AMERICA AND THE CARIBBEAN

Country	Growth 2020 (a)	WB Growth projection (b)	ECLAC growth projection (c)	IMF growth projection (d)	PC INCOME (e)
Bolivia	-11%	-3%	-3%		2,630.55
Brazil	-5%	-5%	-5%	-9%	8,397.12
Colombia	-8%	-2%	-3%		5,226.94
Costa Rica	-7%	-3%	-4%		10,326.78
Dominican Republic	-9%	0%	0%		6,457.62
Ecuador	-9%	-6%	-7%		5,021.30
El Salvador	-9%	-4%	-3%		3,240.72
Guatemala	-6%	-2%	-1%		3,785.25
Haiti	-5%	-4%	-3%		718.18
Honduras	-11%	-2%	-3%		2,095.79
Jamaica	-12%	-3%	-5%		4,438.77
Mexico	-9%	-6%	-7%	-10%	7,216.96
Nicaragua	-10%	-4%	-6%		1,832.37
Paraguay	-9%	-1%	-2%		4,821.33
Peru	-11%	-5%	-4%		5,419.92

Source: (a) author's methodology (section C); (b) World bank, THE ECONOMY IN THE TIME OF COVID-19; (c) ECLAC, Measuring the impact of COVID-19 with a view to reactivation (April 2020); d IMF. A Crisis Like No Other, An Uncertain Recovery (June 2020); (e) World Bank Development Indicators.

¹ Manuel Orozco. Creative Associates International, August 2020

A. The economic models in Latin America and the Caribbean

The problem of economic growth in Latin America and the Caribbean is a chronic or structural one.

Latin American countries' economies are split between two dysfunctional poles of growth, namely, a dense external dependence and economic informality, with a 'missing middle' (migration resulting from the two poles). Together they account for at least 70% of Gross Domestic Product, and with government consumption being 17% of GDP, these economies exhibit limited levels of complexity and competitiveness.

Any economic recovery approach requires addressing ways to focus on the economic opportunities of migration, re-engineering the obsolete model of growth and integrating the informal economies into more competitive agents.

Dependence on the external sector—Economic growth has been driven by a fragile dependence on the global economy, specifically on merchandise exports (predominantly agricultural exports, and “maquilas”) and tourism. In terms of merchandise exports, less than 30 products accounts for more than 50% of exports handled by few companies, which in turn employ only a fraction of the total labor force. This external dependence has an important effect on per capita income. The following table includes 15 countries that capture 85% of the region's GDP and illustrate the pattern.

External Dependence and Per Capita Income (2018)

Country	Key External factors (Exports of Goods and Services (tourism))	PC Income
Bolivia	26%	2,630.55
Brazil	15%	8,397.12
Colombia	16%	5,226.94
Costa Rica	34%	10,326.78
Dominican Republic	42%	6,457.62
Ecuador	23%	5,021.30
El Salvador	11%	3,240.72
Guatemala	17%	3,785.25
Haiti	15%	718.18
Honduras	40%	2,095.79
Jamaica	39%	4,438.77
Mexico	39%	7,216.96
Nicaragua	40%	1,832.37
Paraguay	37%	4,821.33
Peru	26%	5,419.92

Source: World Bank Development Indicators, 2020.

An informal and vulnerable sector—The second pole of growth is a vast informal sector,² comprised of more than two thirds of the labor force and the business sector together. Most of these enterprises are one-person businesses that make less than two minimum wages in revenue but earn only one. In a typical regular household two people are working for the informal economy, in Latin America. These informal sectors are largely people that were not able to fit in to the first pole of growth.

² The informal sector is that segment of the economy that includes workers and businesses that are not registered as a legal entity before the state, municipal authorities, do not make social security contributions or pay income and business taxes.

Overall, however, the economic contribution of the vast size of the informal economy is only one fifth of national income at most. In turn, income among those working in the informal economy are one tenth of those in the formal sector. Moreover, this workforce and the households that host them are vulnerable in many ways, including lacking access to important social protection networks.

Informal Economic Sector: Size, National and Household Income

Country	Informal Economy Contribution to GDP	Size of Informal Economy %	Household income, informal	Household income, formal	Social Insurance coverage
Bolivia	62%	73%	13,447	11,028.26	8%
Brazil	17%	38%	17,846	37,028.79	31%
Colombia	31%	57%	15,105	30,952.05	9%
Costa Rica	5%	37%	6,596	58,734.52	16%
Dominican Republic	30%	54%	19,163	45,458.72	6%
Ecuador	30%	66%	11,574	51,925.27	11%
El Salvador	22%	63%	4,901	46,655.22	6%
Guatemala	22%	73%	4,907	77,084.65	4%
Haiti	80%	88%	4,315	1,951.19	0%
Honduras	23%	76%	3,162	18,532.41	3%
Jamaica	40%	70%	12,067	44,303.87	4%
Mexico	23%	61%	15,988	66,374.00	42%
Nicaragua	25%	75%	2,872	20,733.99	14%
Paraguay	25%	64%	10,917	37,422.03	14%
Peru	30%	59%	14,960	43,851.92	12%

Source: Author's calculations for income, and see source section at end.

Migration and Family remittances—Between these somewhat economically dysfunctional poles is labor migration.

This represent a segment of the labor force that opts out of the informal economy or low paid unskilled jobs in the formal sector. In eighty countries worldwide, migrant's economic engagement include sending remittances, consuming nostalgic trade commodities, diaspora tourism and other services, which represent which together over 10% of GDP (Orozco 2013). Remittances alone amounted to \$500 billion in 2019 and constituted half of household income among some 200 million households in the developing world. These households have large stocks of informal savings, which are largely uncaptured or unleveraged to build assets.

In Latin America and the Caribbean there are more than eight remittance dependent countries, some of which are listed below.

Country	Family remittances	As share of GDP
Haiti	3,346	34.9%
Honduras	5,424	22.0%
El Salvador	5,650	21.2%
Jamaica	2,376	14.9%
Nicaragua	1,700	13.7%
Guatemala	10,508	13.0%
Dominican Republic	7,087	7.9%
Bolivia	1,318	3.2%
Ecuador	3,250	3.0%
Mexico	36,046	3.0%
Colombia	6,773	2.0%
Peru	3,326	1.5%
Paraguay Q	568	1.4%
Costa Rica	518	0.8%

Brazil	2,962	0.2%
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Source: Orozco, Manuel 2020. *Remittances to Latin American and the Caribbean in 2019: Emerging Challenges*.

Therefore, the consequences of an obsolete growth model, accompanied by high rates of informal work, and unleveraged migration perpetuate the presence of unskilled, uneducated and underpaid labor force, and largely uncompetitive economies.

Within this context, economic crises, and particularly those with a systemic impact, will severally affect productivity but predominantly those more vulnerable in the informal sector.

B. The economic impact of COVID-19 in Latin America and the Caribbean

The contagion of COVID-19 has affected Latin America and the Caribbean in an unparalleled trend compared to the rest of the world.

Moreover, the economic impact will have drastic effects due to the systemic nature of its manifestation, that is, the partial stoppage of economic activity both in the three sources of economic dynamism (external, informal and migration) in the region have severely disrupted economic well being and heightened the vulnerability of weaker economic players.

Drop of trade

The consensus among economists, and UNCTAD in particular is of a meaningful drop in exports of at least 20%. The World Trade Organization estimates a drop between 13%-32% for example.³ Commodity prices in key agricultural areas of importance in Latin America and the Caribbean, such as coffee, cocoa, for example, point to drastic declines which further exacerbate an impact on growth.⁴ Preliminary US bilateral trade data points to an already significant decline in textiles.

Similarly, projections on the drop of tourism show a bleaker picture with declines of over -30% relative to 2019. Tourism in several Latin American and Caribbean countries, like Costa Rica, represents at least 3% of GDP.

Economic activity

Many reports have stressed that the most affected sectors by COVID-19 are those working in the informal economy because they must earn an income regardless of the circumstances they are faced with. In every part of the region people have responded differently, however. The critical issue with people working in the informal economy is that the majority are self-employed entrepreneurs, and the issue to them is not losing a job but not working and earning from their sales.

Therefore, this memo utilized a method to measure the impact of losses of income by using the Global Mobility Reports from Google to determine the number of days loss and estimate the drop in revenue controlling for savings. The memo calculated the retail sector's activity as a proxy for informal sector activity.⁵

³ https://www.wto.org/english/news_e/pres20_e/pr855_e.htm

⁴ <https://markets.businessinsider.com/commodities/coffee-price>

⁵ This method is useful proxy in so far as it captures a user's geographic location activity. The calculation employed used the average retail activity percent change between February 7th and June 27th, relative to the baseline period Google uses, Jan 5-February, 6. For July to December it calculates an assumed an activity that is 30% less of what

Day's Losses among key Latin American and Caribbean Countries during the COVID-19 crisis

Country	Day's losses
<i>Bolivia</i>	21%
<i>Brazil</i>	10%
<i>Colombia</i>	17%
<i>Costa Rica</i>	8%
<i>Dominican Republic</i>	11%
<i>Ecuador</i>	15%
<i>El Salvador</i>	17%
<i>Guatemala</i>	11%
<i>Haiti</i>	1%
<i>Honduras</i>	18%
<i>Jamaica</i>	5%
<i>Mexico</i>	8%
<i>Nicaragua</i>	2%
<i>Paraguay</i>	7%
<i>Peru</i>	22%

Source: Google, Global Mobility Report.

Remittances

Research by the author (Orozco 2020) has pointed that remittance transfers are likely to decline between -7 and -16%, and the World Bank -20%. Looking at trends in previous crisis, the 2009, and money transfer data, the likely drop in remittances ranges outside those bounds. For example, As of April, an increase in unemployment of at least 18% among migrants already indicated the effect on remitting. But then in June 2020 unemployment was 13.5% and 12.9% in July.⁶

Unemployment rates among immigrants and US-born adults over 16 years old

	Immigrants	US born
Leisure and hospitality	39.1%	37.6%
Personal and other services	26.0%	21.1%
Transportation and utilities	20.8%	10.2%
Retail trade	19.8%	17.9%
Construction	16.8%	15.1%
Education and social assistance services	15.7%	14.3%
Manufacturing	13.0%	13.1%
Wholesale trade	12.5%	8.8%
Information	11.7%	12.1%
Agriculture	11.6%	5.5%
Professional and business services	10.5%	9.4%
Health services	8.1%	8.1%
Mining, quarrying, and oil and gas extraction	7.9%	10.2%
Financial activities	6.0%	5.3%

was reported in previous period. The percent for the year represents a given number of days losses, which are subtracted from 60 (the stock of disposable income and savings available to cope in a crisis).

⁶ <https://www.pewresearch.org/hispanic/2020/08/04/coronavirus-economic-downturn-has-hit-latinos-especially-hard/>

Public administration	3.8%	4.8%
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Source: Author's own based on Migration Policy Institute, June 2020, "Covid-19 and Unemployment. Assessing the Early Fallout for Immigrants and Other U.S. Workers", which uses data from the US Census Bureau's January 2020 and April 2020 monthly Community Population Survey (CPS).

In fact, data between January to June pointed an average -6.6% drop in remittances so far. Money transfer companies for example, registered drops in their transactions of at least -30% in March and April then recovering positively between May and July.

Remittances to Latin America and the Caribbean, 2020 (first six months growth relative to 2019)

Country	YoY Growth (first six months 2020)	Migrts.US	Europe	Rest (mostly LAC)
Brazil	-28%	26%	70%	4%
Colombia	-5%	28%	38%	33%
Dominican Republic (July)	1%	70%	24%	6%
El Salvador	-8%	89%	7%	4%
Guatemala (July)	1%	90%	5%	5%
Haiti* reported from companies	5%	46%	11%	42%
Honduras	-4%	90%	6%	4%
Jamaica	-1%	68%	30%	2%
Mexico	10%	96%	2%	2%
Nicaragua*	3%	44%	10%	46%
Paraguay	-20%	4%	18%	78%
Peru	-15%	35%	51%	14%
Selected countries	-6.6%			

Source: Central Banks; *reported from companies; UNDESA 2019.

The table below presents an estimated (and revised) drop of -3% for 2020 in family remittances. It also identifies the number of migrant remitters, who typically send to 1.2 households back home. Research also points that 60% of recipients are working in formal headed households, and 40% are recipients with people in the informal economy.

The estimated preliminary migrant survey data points that 34% of the unemployed will not be able to send money back home, and 41% of those who didn't lose their jobs will remit 13% less.

In total, Year on Year growth is estimated at -9.3%.

Remittance transfers to Latin America and the Caribbean

<i>Indicators</i>	<i>Migrant remitters</i>	<i>Net remitters in 2020</i>	<i>Expected volume in 2020</i>	<i>YoY growth</i>	<i>Households not receiving</i>
Bolivia	570,837	541,610	\$ 1,269,786,594	-3.67%	34,935
Brazil	1,134,250	1,083,889	\$ 6,926,233,452	-13.01%	61,703
Colombia	2,869,032	2,722,138	\$ 6,692,990,438	-1.17%	175,585
Costa Rica	125,000	121,150	\$ 493,954,120	-4.68%	5,100
Dom. Rep	897,793	857,931	\$ 7,138,066,862	0.49%	48,840
Ecuador	681,803	646,894	\$ 3,130,830,963	-3.67%	41,726
El Salvador	1,040,673	1,022,773	\$ 5,553,776,836	-1.71%	56,613
Guatemala	1,500,000	1,474,200	\$ 10,603,083,926	0.90%	81,600
Haiti	1,585,681	1,493,712	\$ 3,334,911,756	-0.34%	107,826
Honduras	850,000	835,380	\$ 5,337,357,443	-1.60%	46,240
Jamaica	913,896	873,319	\$ 2,387,799,792	0.49%	49,716
Mexico	7,399,547	7,071,008	\$ 38,205,056,760	5.99%	402,535
Nicaragua	750,000	735,825	\$ 1,707,191,680	0.42%	43,350
Paraguay	697,310	666,350	\$ 517,220,858	-9.01%	37,934
Peru	1,210,336	1,156,597	\$ 3,109,440,058	-6.51%	65,842
Venezuela	2,835,000	2,670,570	\$ 2,623,702,444	-15.80%	192,780
Other nationalities	5,149,281	4,920,653	4,492,088,102	-39.14%	280,121
All Latin American migrant remitters	30,210,439	28,780,097	103,523,492,084	-2.67%	1,732,447

Source: Orozco, Manuel. Migrants and the Impact of the COVID-19 Pandemic on Remittances, 2020, and Migrant workers and Remittances to Latin America and the Caribbean in 2020.

C. Measuring and Assessing the economic impact of COVID-19

The economic impact of the COVID-19 needs to consider as framework the two poles of growth and its missing middle. With at least a 20% drop in external factors such as exports of goods and services (tourism included), a drop in migrant remittances of -16%, and a loss of economic activity equivalent to an average of 30 days losses after controlling for the informal sector's economic resilience, the severity of the crisis is dramatic.

The following is a model employed to measure the economic impact of the pandemic by controlling external and domestic factor behavior. Specifically, the model looks at economic changes within sectors of the informal and formal economy controlling for changes in exports of goods and services and family remittances. The model does not account for changes in other external factors such as foreign direct investment and hold government expenditure constant.

$$GDP\ Growth_{2020} = Informal\ economy + Formal\ economy + Government\ Expenditure + (X+R_{formal\ \&\ informal})$$

Where,

Informal economy: Informal activity + (X[20%]+R[40%]) * Coefficient of day loss

(Although the majority of trade is conducted by formally established businesses with a transnational operation, within the context of the value chain there are informal workers and entrepreneurs associated to businesses in the formal sector. That link may be small and is calculated at 20% of all trade. Among remittance recipients, research shows that 60% of remittance recipients are people with a professional job or are spouses of people in the formal economy. Those directly linked to the informal sector are calculated at 40%). The day loss coefficient is only calculated in the informal sector because they lack any formal support network that can shelter them against external shocks.

Formal economy: Formal Activity + (X[80%]+ R [60%])

In turn, the analysis produces independent impact results on the formal and informal sectors.

The relevance of conducting this analysis controlling for the informal economy stems on the fact that because the informal sector is large and more economically weak, it will be more vulnerable to external shocks. Therefore, as the table shows below, the effect on income loss will also be higher among the informal sector than those in the formal sector. Because of their income capacity is much lower, given cost of living expenses, their recovery will take much longer, despite any recovery from the effect of the pandemic itself.

For example, when the average annual household income among the Latin American and Caribbean sector is US\$10,000, for a family of four, the costs of managing that household in times of crisis within a context of deprivation, income loss, and risk of falling ill, are much higher than a household earning four times higher that is already protected by a social safety net.

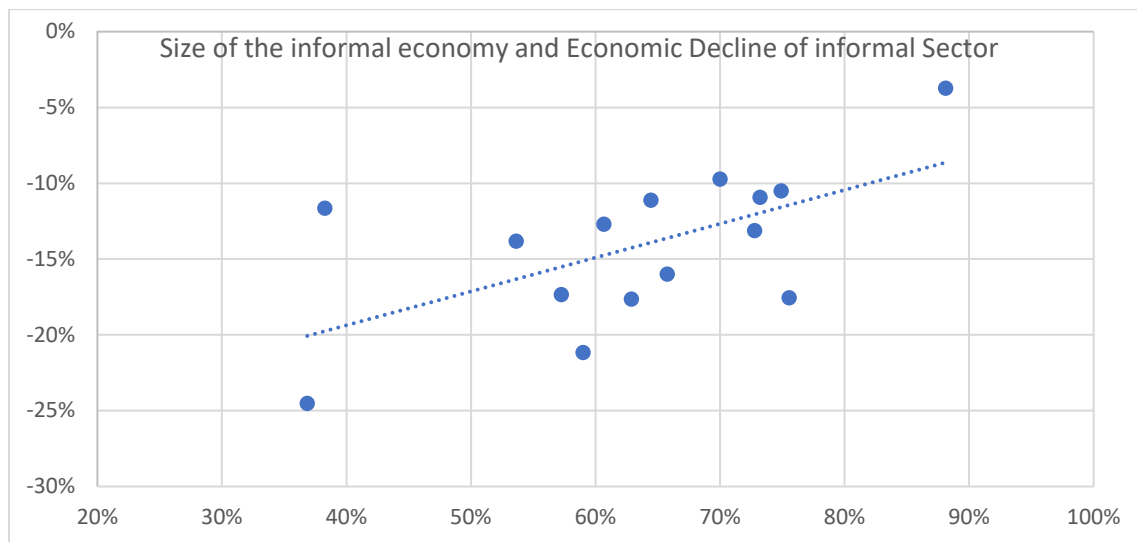
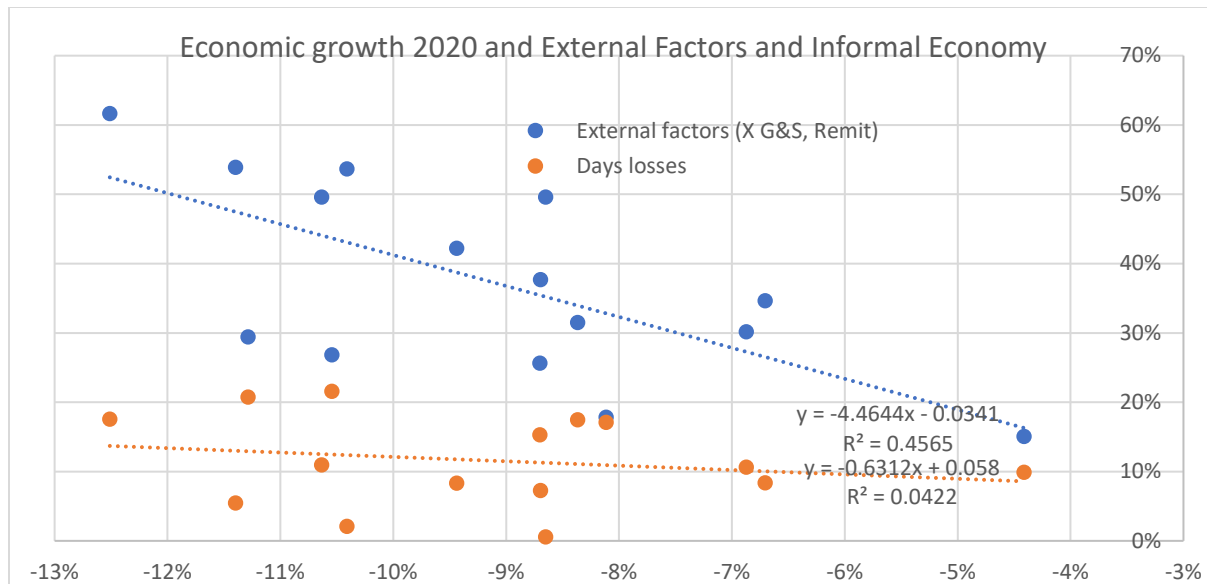
Projected decline of economic growth within sectors of the economy, 2020

Country	Growth 2020	<i>Growth Informal sector</i>	Growth Formal Sector
Bolivia	-11%	-11%	-12%
Brazil	-5%	-12%	-3%
Colombia	-8%	-17%	-4%
Costa Rica	-7%	-25%	-6%
Dominican Republic	-9%	-12%	-7%
Ecuador	-9%	-16%	-6%
El Salvador	-9%	-15%	-7%
Guatemala	-6%	-11%	-5%
Haiti	-5%	-2%	-18%
Honduras	-11%	-15%	-10%
Jamaica	-12%	-10%	-13%
Mexico	-9%	-12%	-9%
Nicaragua	-10%	-9%	-11%
Paraguay	-9%	-11%	-8%
Peru	-11%	-21%	-6%

On a macroeconomic level, the economic impact of the pandemic is greatest due to the decline from external forces than to the days loss from quarantine mitigation procedures. In that sense, the impact on the informal economy and households is more pronounced yet lowest among those countries whose labor in the informal economies are largest. Part of the reason stems from the fact that the lockdowns associated with quarantine and social distancing were affecting sectors whose purchasing power is lower in the Latin American and Caribbean region than other parts of the world. Relative to each country's cost of living conditions, the severity of the income loss is more durable and heaviest in countries with higher informal economies.

Country	Economy	Annual Income among Households in the informal sector		Annual Income among Households in the formal sector		PC Income 2019
	Size of Informal Economy %	2019	2020	2019	2020	
Nicaragua	75%	2,872	2,570	20,734	18,583	1,832
Honduras	76%	3,162	2,607	18,532	16,494	2,096
El Salvador	63%	4,901	4,037	46,655	43,973	3,241
Haiti	88%	4,315	4,154	1,951	1,399	718
Guatemala	73%	4,907	4,262	77,085	73,150	3,785
Costa Rica	37%	6,596	4,977	58,735	55,347	10,327
Paraguay	64%	10,917	9,702	37,422	34,472	4,821
Ecuador	66%	11,574	9,722	51,925	49,030	5,021
Jamaica	70%	12,067	10,893	44,304	38,761	4,439
Peru	59%	14,960	11,792	43,852	41,226	5,420
Bolivia	73%	13,447	11,975	11,028	9,721	2,631
Colombia	57%	15,105	12,485	30,952	29,730	5,227
Mexico	61%	15,988	13,955	66,374	60,750	7,217
Brazil	38%	17,846	15,765	37,029	35,956	8,397
Dominican Republic	54%	19,163	16,514	45,459	41,246	6,458

Moreover economic recovery will take longer than in other regions partly because the policy measures adopted are largely associated to limited relief rather than recovery, and that the lockdowns measures do not come with the economic precision to mitigate the crisis and reduce the size of the pandemic.



Final observations as mode of conclusion

The severity of the economic impact of COVID19 is getting stronger in so far as the duration of the pandemic last longer. Overall, across all groups, and particularly those where income dependence from external sectors is over 5% of Gross Domestic Product, is important to implement financial inclusion and income retention and management methods in times of economic crisis. The strategy should consist of three specific prongs:

- a) money management tools for financial resilience.
- b) differentiated approaches to main social sectors, including remittance recipient, women head of households, students, and entrepreneurs;
- c) financial access in the digital economy.

The strategy consists of providing financial advice to those in countries whose participation in the economy is at least 10% of the economy. Remittance recipients are a group with a strong purchasing power, and financial advice can have the purpose to stretch the durability of their income using economic resilience tools, budget re-evaluation, savings administration, and use of mobile wallets as efficient budgeting vehicles.

The differentiated approach to women headed households, which typically represent half of all recipient households is particularly important because they face uncertainty in terms of the durability of the income, further economic losses and diminished social capital. Financial tools that can help smooth some of their economic obligations, while exploring alternative modes of economic activity.

With a labor force that is over 60% informal, and at least two in ten people are entrepreneurs, the majority also informal, who work as entrepreneurs, vendors, traders in both formal and informal sectors. Providing them with tools to integrate their business into the digital economy is essential.

Moreover, one in ten remittance recipients are youth under 30 who are studying and their income dependence in remittances is greater. Therefore, while their financial budget is less complex than with female heads of households or entrepreneurs, they need to have particular tools to cope with future expenditures in education, adapting to new technologies, and future employment prospects.

Finally, financial access is not only central but necessary to confront the recession and enabling recipients with digital financial vehicles will contribute to budget, save, but also reduce the risk of contagion.

Sources:

GDP: ECLAC.

Size of labor force in informal economy: The World Bank, Informal employment (% of total non-agricultural employment); International Labour Organization, ILOSTAT database. Data retrieved in March 1, 2020.

<https://data.worldbank.org/indicator/sl.isv.ifrm.zs>

Contribution of informal sector to GDP: <https://financiatribune.com/articles/world-economy/81033/imf-bolivia-has-world-s-largest-informal-economy>";

<https://g1.globo.com/economia/noticia/2019/12/18/economia-informal-cresce-pelo-5o-ano-seguido-no-pais-e-corresponde-a-173percent-do-pib-aponta-estudo.ghtml>;

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