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COVID-19 in Latin America and the Caribbean: Regional socio-economic implications and policy priorities

17 April 2020

Most Latin American and Caribbean countries have been hit by the Covid-19 crisis in the context of low potential growth, high inequalities and rising social discontent. Policy reactions to the crisis have been bold, but further measures will be needed. In the immediate term, the priority must be to prevent contagion and support most vulnerable families, workers and firms. In the phasing out of the containment and lockdown measures, continued income support to stimulate consumption and support inclusiveness, as well as investment efforts to promote activity are fundamental to spur a swift economic recovery. In the medium term, the aftermath of this crisis must be turned into an opportunity to redefine the social pact, putting well-being at the centre, based on stronger social protection systems, better healthcare, more robust and inclusive public finances and implementing inclusive development strategies. Co-ordinating a global response to address the impact of the Covid-19 crisis in the region remains vital.

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The first cases of coronavirus in Latin America and the Caribbean (LAC) started end-February in Brazil, and since then, Covid-19 reported cases and deaths have continuously increased in the region.[1] The actual dimension of the pandemic in the region remains somewhat uncertain, as cases are underreported and accuracy for data collection varies considerably within the region. The digital transformation should provide new avenues to better detect and respond to Covid-19 in LAC.

Countries have gradually implemented social distancing and other mitigation measures to reduce the spread of the virus, starting with El Salvador's lockdown and travel ban on 11 March. Total and partial lockdowns include measures such as shutting down borders, prohibiting transit for non-essential reasons, cancelling events, closing non-essential business, and stopping or virtualising the classes in schools and universities, among others.

While the region confronts the crisis with a demographic structure where only 9% of the population is aged over 65 (vs. 17.2% in OECD countries), the limited capacity of health systems and the high levels of informality in most countries amplify the challenge of fighting this pandemic. The region spends four times less on healthcare than OECD countries. On average, there are 2.2 hospital beds (per 1 000 habitants), below the average of 4.7 hospital beds across OECD countries. In addition, there are almost 2 doctors and less than 3 nurses per 1 000 population, while the OECD averages are 3.5 and 9, respectively (OECD, 2020[1])). Finally, the share of population in Latin America satisfied with quality of healthcare services fell from 57% in 2006 to 42% in 2018, below the OECD average of around 70% (OECD et al., 2019[2]).

Pre-Covid-19 conditions and possible macroeconomic impact on growth and social conditions

The Covid-19 pandemic will have strong socio-economic consequences, accentuating the already complex scenario faced by LAC, characterised by significant structural *development traps* (OECD et al., 2019[2]). The region enters the Covid-19 crisis with the majority of countries presenting low potential growth and increasing social discontent. Between 2014 and 2019 the region experienced the weakest period of growth since the 1950s, consistently recording lower growth rates than the OECD average. In 2019, growth was practically nil and protests erupted in some countries, confirming that despite past improvements in reducing income poverty, vulnerability and exclusion remain a major concern in the region. Governments need to respond more effectively to the growing aspirations of a rising but vulnerable "middle-class" and continue to include segments of the population that are left behind. Several international organisations have estimated annual GDP growth for 2020 to be negative and these different projections are between -1.8% and -5.5% (ECLAC, 2020[3]; IMF, 2020[4]; Nuguer and Powell, 2020[5]; World Bank, 2020[6]). Uncertainty remains extremely high, and the size of the economic contraction will vary considerably across countries and will depend on (i) the depth and length of the confinements, (ii) the additional measures adopted by countries during the lockdown, both within and outside the region, and (iii) the path of the global economy in the aftermath of the crisis.

Beyond the direct effect of Covid-19 on human health, the socio-economic impact of the pandemic in LAC is – and will continue to occur – through different channels. First, the confinement measures adopted by governments induce a large immediate drop in economic activity, as workers are prevented to go to work and remain locked down at home. Households are also cutting sharply their consumption on most goods and services during confinement. Second, containment measures, restrictions to border crossing, and

[1] By the second week of April, reported cases in the whole region exceeded 65 000, while the death toll rose to more than 2 500. The countries with the highest number of deaths to date are Brazil, Ecuador and Mexico. For more details see OECD Coronavirus data in real-time http://oecd.org/coronavirus/en/ and the OECD note "COVID-19 in Latin America and the Caribbean: An overview of government responses to the crisis".

social anxiety affect key sectors such as tourism and international travel. This will have particular incidence in highly dependent countries as some Caribbean economies, where tourism accounted for more than 20% of GDP in 2018 and where it could fall by around 25% (ECLAC, 2020[7]). Other sectors such as retail trade, wholesale trade and manufacturing sectors will also be heavily affected. Third, the global slowdown (OECD, 2020[8]) and the disruption of global and regional value chains will generate a sharp decline in LAC exports. Fourth, while the collapse in oil prices can be a relief to the oil-importing Caribbean and Central American economies, it affects fiscal and external accounts of several South American countries, as well as Mexico and Trinidad and Tobago. Similarly, Chile and Peru suffer from the decline in copper prices. Finally, financial volatility, the worsening of financial conditions and large capital outflows have brought a strong depreciation of LAC currencies and the reduction of financial assets in debt and equity markets, affecting the solvency of large LAC companies. In contrast to these negative effects, the adoption of digital technologies and the spread of the Internet have been critical to sustain certain continuity in business, jobs or studying from home, although the digital divide, notably the lack of high-speed broadband Internet has prevented from reaping the benefits to all. Going further, digital technologies can play an important role in the recovery, while addressing the persistent challenge of low productivity (OECD et al., 2020[9]).

The economic slowdown of previous years coupled with the drop in activity caused by this pandemic is already having negative effects on living standards and well-being. This is in particular true for poor and vulnerable workers, among which around 74% are informal. Regarding both current and future well-being of Latin Americans, the pandemic may touch every aspect of people's lives with several dimensions of well-being strongly affected, especially those related to material conditions (including income, job quality and housing), but also other aspects such as knowledge and skills. In particular, regarding the latter, as schools closed, home schooling may have different long-term impacts on children and youth, depending on their socio-economic background (OECD, 2020[10]) (see section below on impacts on households and firms).

Fiscal position and debt trajectory

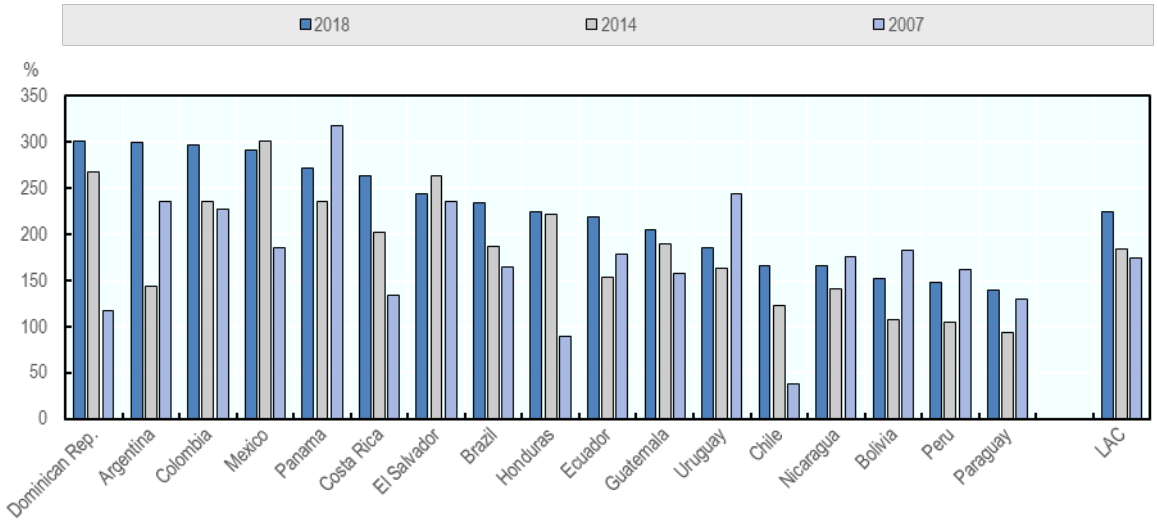
Fiscal policy is playing an essential role in mitigating the negative economic and social effects of the pandemic, and will continue to be pivotal in the subsequent recovery. Weak automatic stabilisers in the region (Espino and González Rozada, 2012[11]), with fragile or non-existent unemployment insurance, high levels of informality and low tax revenues, make discretionary fiscal responses to the crisis even more urgent than in European countries, for instance. At first, the aim of fiscal policy should be to stop the spread of the virus, through support for preventive programmes, detection and treatments, and to support businesses continuity and protect jobs. Most economies of the region have already started implementing such programmes. The measures aiming to mitigate the effects of the Covid-19 crisis should be designed as temporary, in order to not compromise fiscal stability in the future (Izquierdo and Ardanaz, 2020[12]).

Countries' ability to react with fiscal policy to the pandemic will depend on the starting fiscal position and their access to international markets. Before the Covid-19 crisis, fiscal space in the majority of countries in the region was already limited as many economies were undergoing fiscal adjustments. Fiscal deficits are the norm in most countries of the region, but a large group of countries have implemented fiscal rules, including Chile, Colombia, Mexico and Peru that should allow for some countercyclical policies. Despite high heterogeneity, tax revenues remain scarce at close to 23% of GDP, more than 10 percentage points lower than the OECD average (OECD/ECLAC/CIAT/IDB, 2019[13]). Moreover, fiscal policy has not been sufficiently effective in reducing inequalities and promoting entrepreneurship (OECD et al., 2019[2]; Izquierdo, Pessino and Vuletin, 2018[39]).

Debt levels have been on the rise since 2014 in almost all countries. Public debt-to-tax ratios increased in most countries, leaving them in a weaker position to face the Covid-19 crisis than in 2007, before the 2008

financial crisis (Figure 1). While on-going international discussions on the outstanding public debt obligations, in countries such as Argentina or Ecuador, should affect access to international capital markets, this process of debt restructuring should contribute to restore fiscal space later on. Caribbean countries are highly indebted and may face constraints to borrow. In 2018, 3 out of the 25 most highly indebted countries in the world (measured by gross general government debt levels relative to GDP) were in the Caribbean: Antigua and Barbuda, Barbados and Jamaica (IMF, 2019[36]; OECD et al., 2019[2]). Going forward, tax measures to address the Covid-19 crisis and the consequent economic slowdown are likely to take a toll on tax revenues. Similarly, and despite the limited space for increasing debt, governments will have to access financial markets. Rising interest rates, due to growing risk aversion and sovereign bond spreads (see section below), should make multilateral loans a priority (see section on policy priorities).

Figure 1. Debt-to-tax ratio (gross public debt) in Latin American countries



Note: Simple average of the countries included in the figure.
Source: Own calculations based on (OECD/ECLAC/CIAT/IDB, 2019[13]) and CEPALSTAT.

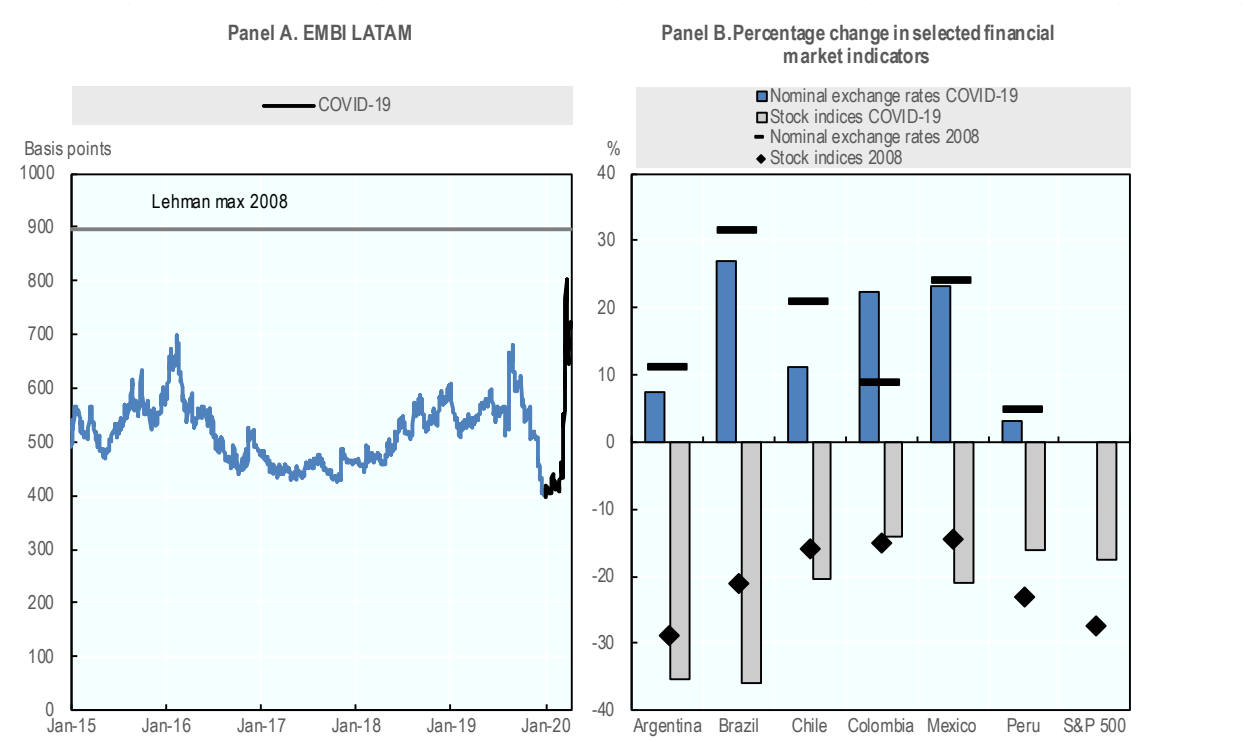
Balance of payments and global integration

The sharp decline in global and regional economic activity in 2020 will have an impact on LAC's external accounts. Current account balances in Latin America had slightly deteriorated in 2019, following the slowdown in international trade and the correction in commodity prices. However, with few exceptions, current account deficits were financed by foreign direct investment (FDI). The expected slowdown in global and regional economies caused by the Covid-19 crisis will worsen these dynamics. Demand from the rest of the world, due to a fall in consumption, has dropped. Trading partners are postponing investment decisions while the decline in international demand is triggering a dramatic fall in exports from the region. As of early April 2020, oil prices have fallen by 60% since the beginning of the year; copper, iron, soybeans, sugar and coffee prices have also sharply declined. With containment measures expected to remain in place for some time, LAC exports are expected to contract even further (IDB, 2020[14]). For the case of South and Central America, merchandise trade could decline in 2020 between 12% and 31% compared to 2019 (WTO, 2020[15]). On the other hand, strong currency depreciations will make foreign goods more expensive, pushing imports to fall but increasing the competitiveness of the regions' exports. It remains to be seen which effect will prevail, what seems undisputed is that FDI will deteriorate. On a global scale, FDI is expected to fall between 30% to 40%, decreasing the most in economies that are most severely hit by

the pandemic (UNCTAD, 2020[16]). The fall in remittances will also further weaken trade balances, with a likely stronger impact on Central America and Mexico. Conservative estimates show that remittances originating from the United States will fall by 3% in 2020 (Inter-American Dialogue, 2020[17]); this could decrease further due to border-crossing restrictions that will cut back sharply migration flows, such as seasonal workers to the United States (see section below on the impacts on households and firms).

LAC economies will be highly affected by the slow-down in their trade partners, notably the People's Republic of China (hereafter "China") and the United States. China has become the main trading partner for many South-American economies (OECD/CAF/UN ECLAC, 2015[18]). China is not only a major importer of raw materials, but also a direct investor and a credit provider to LAC economies, mainly to Argentina, Brazil, Ecuador and Venezuela (Inter-American Dialogue, 2020[19]). On the other hand, the contraction in the United States will mainly affect Mexico, Central America, Colombia and the Caribbean.

Figure 2. Latin American financial markets



Note: Panel A: the EMBI is a benchmark index for measuring the total return performance of international bonds issued by emerging market economies. EMBI LATAM measures the average spread that is defined as the differentials between the performance of sovereign bonds denominated in US dollars and US Treasury bonds, as calculated by JP Morgan Chase. Panel B: the indices shown are BOVESPA (Brazil), IPSA (Chile), IGBC (Colombia), IPC (Mexico) and IGBVL (Peru), and the S&P 500 composite index (United States) to compare with global markets. Panel B is the percentage change from 01/01/2020 to 06/04/2020 for Covid-19 crisis. For 2008 financial crisis, it is between 15/09/2008 (fall of Lehman Brothers) to 15/12/2008.
Source: Own calculations based on Thomson Reuters, Datastream.

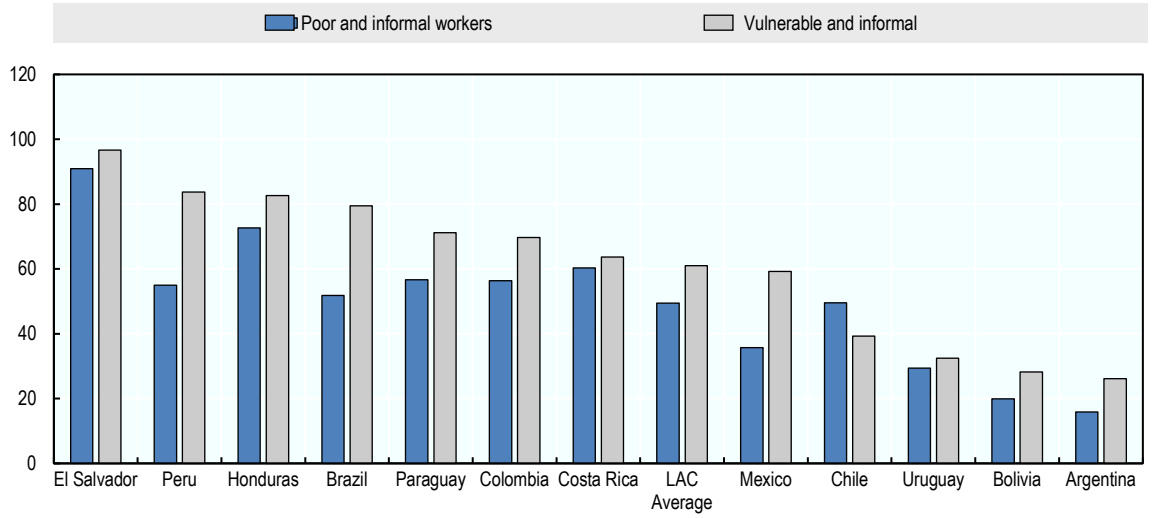
Since late January 2020 the region is experiencing substantial capital outflows (especially portfolio investment), surpassing the levels reached in the aftermath of the 2008 financial crisis (IIF, 2020[35]; IDB, 2020[14]). Covid-19 has affected financial markets and created high volatility at similar levels to the 2008 international financial crisis. In mid-march 2020 global financial volatility, measured by the VIX, surpassed temporarily the maximum level seen in the 2008 crisis. For LAC, sovereign bond spreads, measured by the emerging markets bond index (EMBI), have almost doubled since the beginning of 2020 (Figure 2, Panel A) (Izquierdo and Ardanaz, 2020[12]). Although EMBI spreads remain lower than in the 2008 financial crisis, they are above the levels observed in the past five years. Large capital outflows have also resulted in strong stock market falls since the beginning of the year. Similarly, currencies have strongly depreciated in the region since the beginning of the year (Figure 2, Panel B). Strong currency depreciations will pose an additional problem to governments and companies that are highly indebted in foreign currency and that have not hedged their foreign currency exposure.

Impacts on households and firms

The socio-economic impact of the Covid-19 crisis can be severe across individuals, households and firms in the absence of ambitious public policy responses (see section below on policy responses). Social conditions are already worsening as a result of the slowdown. In the absence of a strong response, the pandemic could leave between 14 to 22 million more Latin Americans in extreme poverty by the end of 2020 (ECLAC, 2020[7]). If the worsening of the pandemic were to cause a fall of 5% in the average income of the active population, the number of citizens in extreme poverty would go from 67.5 million to 82 million. If the decrease in income for the economically active population were 10%, that figure would reach 90 million people.

The social impact of the Covid-19 crisis could be particularly difficult for the 38% of workers who do not have access to any form of social protection. The crisis is likely to increase informal employment, which already accounts for 58% of workers (OECD/ILO, 2019[20]). While the region's social insurance and major social assistance programmes cover two thirds of workers (62%) and their families, including most of the poor households, 65% of informal workers do not benefit from any form of social protection. They do not benefit from sick leave or unemployment benefits, and have poor access to health insurance and national health services. This especially affects the large share of informal vulnerable workers, those living with between USD 5.5 and USD 13 (PPP 2011) a day. Many of them are own-account workers, work in the subsistence economy, and live day-by-day. Very few of them can work remotely. Among informal workers who face economic vulnerability, 61% are not part of a household covered by a major social assistance programme (direct transfers from the largest transfer programmes or non-contributory pensions) (Figure 3). The risk for them of slipping back into poverty is considerable. Here lies one of the main challenges of this crisis: protecting these group of informal vulnerable workers with no access to social protection and avoiding a widespread expansion of poverty, which already affects 25% of the population.

Figure 3. Poor and vulnerable informal workers not covered by a major social assistance programme, selected Latin American countries (%)



Note: Regional average is a simple average. Informal workers by definition are those who do not contribute to the social security system and therefore do not have access to contributory health and unemployment insurance. Major social assistance programmes include poverty targeted cash transfers in the form of conditional cash transfers, unconditional cash transfers and social/non-contributory pensions. They do not include disability benefits or in-kind transfers. Labour informality is estimated using the methodology developed by (ILO, 2018[21]) and implemented by (OECD/ILO, 2019[20]).
Source: Own calculations based on each country's latest available Household Surveys (preliminary estimations).

The immediate effects of an economic downturn will be quickly felt by migrants living in LAC countries and their households, as many have irregular migrant statuses or work informally. More than 11 million migrants reside in LAC countries. Figures have dramatically increased since 2015 with the humanitarian and economic crisis in Venezuela pushing around 4.9 million people to leave the country, with close to 4 million who have settled in countries of the region. Migrants in LAC are overrepresented among the poorest segments of the population. Less than 15% of households in the lowest income quintile have savings to cover emergency expenses (Messina, 2020[22]).

Given the expected decrease in remittances (see section above on balance of payments and global integration), the immediate effects of Covid-19 crisis will also be felt by migrants' families in their countries of origin. Remittances are a major source of income in several LAC countries, having steadily risen since 1990 from USD 5.7 billion to more than USD 90 billion in 2018. Remittances are estimated at 1.5% of the region's GDP; yet, in some countries, they represent a high proportion of national income. For instance, in most Central American and Caribbean countries they account between 10% and 30% of GDP (World Bank, 2020[23]).

In the absence of strong policy responses, the Covid-19 crisis could deepen disparities between regions and cities within LAC countries. Measures as basic as washing hands or avoiding physical contact are difficult to follow for 21% of the LAC urban population living in slums, informal settlements or inadequate housing where basic services are not affordable. Many houses do not have access to safe water and, on average, up to 3 people share each room (Oxfam, 2020[24]). In these areas, the potential positive impact of containment measures would be limited. Territorial differences are important also when considering health and social conditions, which could lead to a heterogeneous impact of the pandemic. For instance, in Colombia, the infant mortality – regarded as a sensitive (proxy) measure of population health – of Vichada is almost three times that of Antioquia; and in Peru the infant mortality of Tumbes is over three times higher than that observed in Puno (OECD et al., 2019[2]).

Women might be disproportionally affected by the Covid-19 crisis. First, given the traditional and gendered division of roles in LAC, women are likely to bear a higher physical and emotional burden than men during the pandemic. Women are the primary care providers and the daily time they dedicate to unpaid domestic and care work is on average three times higher than men in LAC (OECD, 2019[25]). Secondly, in some countries women may be particularly affected by the reduction in economic activity as they are more likely to hold an informal job. For example, in Mexico 58% of women are part of informal employment against 50% of men, and in Costa Rica 39% of women are informal compared with 35.5% of men in 2018. Finally, women are more likely to be exposed to domestic violence as a result of quarantine and lockdown measures. For instance, recent data show that in Argentina emergency calls for domestic violence cases have increased by 25% since the lockdown on March 20. A fall in their income may further create barriers for them to leave a violent domestic situation (UN Women, 2020[26]).

Many companies may go bankrupt, particularly micro, small and medium enterprises (MSMEs) that represent 99% of all companies in the region and generate more than half of jobs (ILO, 2015[27]; Dini and Stumpo, 2019[28]). MSMEs, especially those relying on self-employment and microenterprises, could be largely affected by the economic consequences of containment measures as they have less liquidity and buffers. Preliminary surveys suggest that only 15% of firms with sales lower than USD 5 000 per month will survive after 2 months of lockdown in the region (Nauta and SistemaB, 2020[29]). Furthermore, SMEs employ 76.5% of workers in the trade sector and 86.1% in hotels and restaurants (OECD/CAF, 2019[30]). Both sectors are highly affected by this crisis. Indeed, by end-March 2020, mobility trends for places like restaurants, cafes, or shopping centres fell by more than 80% compared to normal periods in countries like Colombia, Ecuador, El Salvador, the Dominican Republic, Panama and Peru (Google, 2020[31]). Finally, the productivity gap of LAC MSMEs makes them particularly vulnerable to demand shocks. Microenterprise productivity reaches only 6% of the productivity of large firms (vs. 42% for European Union firms) (Dini and Stumpo, 2019[28]). With lower productivity and potentially facing rigid cost structures, MSMEs are more likely to face bankruptcy or losses.

With the Covid-19 crisis, the digital divide becomes an ever greater concern since it can further amplify existing inequalities. Only workers, students or consumers with the proper infrastructure and skills can benefit from the advantages of technological tools. Although access to ICTs has significantly improved, gaps persist and new ones may emerge (OECD et al., 2020[9]). More than 6 in 10 households with per capita income in the lower quintile of the income distribution do not have access to high-speed fixed broadband connection needed to support working and studying, whereas nearly 8 in 10 households with per capita income in the highest quintile of the income distribution do so. A striking gap also remains in the way people with low and high levels of education use the Internet, with over 20 percentage points' difference in the case of on-line banking (OECD et al., 2020[9]).

At the same time, the Covid-19 crisis might further amplify existing inequalities in access to and quality of education. As schools closed in almost all LAC countries, online learning became suddenly critical for the education of 154 million students (around 95% of all students in LAC) (UNICEF, 2020[32]). Yet, education systems in LAC are not sufficiently prepared for the world of digital learning. In fact, 51% of the region's 15-year-old students in advantaged schools have access to an effective online learning support platform, while only 21% of the students in disadvantaged schools do so. Additionally, 88% of the region's 15-year-old students from advantaged schools have access to a computer to work at home, while only 45% of students in disadvantaged schools do. Technology is only as good as its use. PISA 2018 asked school principals about school's capacity to enhance teaching and learning using digital devices. On average across LAC countries, 58% of 15-year-olds are enrolled in schools whose school principal considers that their teachers have the necessary technical and pedagogical skills to integrate digital devices in instruction. This highlights the enormous training needs that lie ahead for educators to catch up with technology opportunities. Again, this contrasts significantly between socio-economically advantaged and disadvantaged. In Colombia, for example, this percentage is 73% in advantaged schools but just 50% in

disadvantaged schools. These numbers signal that schools may reinforce rather than moderate the disadvantage that comes from individual home backgrounds (OECD, 2020[33]).

Policy priorities: from the immediate response to the broader rethinking of the social pact

Profound uncertainties remain around the evolution of the crisis for Latin America and the Caribbean, making the policy response more complex to design. The sequencing of policy priorities will be critical and should be structured to address different policy objectives in the immediate, short and medium-term.

In the immediate term, preventing the contagion and supporting the most vulnerable

To contain the spread of Covid-19, many LAC countries have already reacted swiftly by adopting social distancing and lockdown measures. As these measures have a strong socio-economic impact, several countries in the region have adopted fiscal and monetary policies to protect the most vulnerable and to preserve human, productive and financial capacities to help reduce the negative impact of the crisis (for more details of these policy measures see the OECD Country Policy Tracker at http://oecd.org/coronavirus/en/#country-policy-tracker and the OECD note on "Covid-19 in Latin America and the Caribbean : An overview of government responses to the crisis").

On the monetary front, some central banks, under their inflation targeting regimes, have lowered interest rates, but have also announced a reduction of reserve requirements and an injection of liquidity into the economy.

In addition to this, specific measures have been adopted to shield the most vulnerable families, workers and MSMEs:

- Financial intermediaries, including national development banks, have adopted facility conditions on loan repayments (e.g. mortgages or consumption credits) to households and have promoted guarantees for new credits or deferral on loan repayments to vulnerable firms.
- Government measures in support to the most vulnerable families include non-conditional cash transfers, tax deferrals and reductions, food baskets or suspension of payments of basic utilities. Similarly, measures to support workers include exemptions from social security contributions, right to withdraw funds from individual saving accounts (i.e., unemployment, pensions), direct cash transfers to self-employed and subsidies to temporary employment. Finally, to minimise bankruptcies, tax deferrals have been allowed for firms as well as payroll support or deferral on payment of utilities.

It is essential to constantly evaluate the implementation and effectiveness of these measures and to re-adjust them if necessary, especially those aimed at the poorest and vulnerable population. This is in particular relevant to support informal vulnerable workers who are not covered by any form of social assistance programme; innovative policy actions are needed, as already announced in some countries, such as Argentina, Brazil, Colombia and Peru (see the OECD Country Policy Tracker at http://oecd.org/coronavirus/en/#country-policy-tracker) and the OECD note on "Covid-19 in Latin America and the Caribbean : An overview of government responses to the crisis").

In the short term, adopting bold measures to spur a swift economic recovery

The phasing out of the containment and lockdown measures should consider healthcare system capacity and be informed, as much as possible, by data on infections. Testing more people to identify who are infected, tracking them to make sure they do not spread the disease further, and tracing who they have been in contact with, will be essential to supress the resurgence of local outbreaks.

On the economic front, while the previous measures aimed to avoid further increases in poverty or in firms' bankruptcy, this stage must be aimed at bringing the economy back to its full activity. The main measures must support effective demand stimulus, in particular from the consumption side. Specific support measures for most affected sectors and investment plans should also contribute to reactivate the economy.

Social policies will need to continue to support those affected by the inevitable impact of the crisis, particularly the most vulnerable and those who may have fallen into poverty during the pandemic.

These actions will involve the mobilisation of vast financial and human resources. Domestically, it will certainly lead to higher public deficits and rising levels of public debt, which in countries with a weaker fiscal position will represent a challenge. In this context, co-ordinated support from the international community will be vital given the magnitude of the effort and the difficulties that LAC countries will face to finance themselves in international markets.

Finally, Covid-19 could continue to strike in future waves, either directly or indirectly through the effect on other economies, so governments must prepare upfront for managing such a scenario and not just react to a new crisis.

In the medium term, laying the foundations of a new social contract

This crisis has impacted LAC at a time when levels of trust and citizen satisfaction are particularly low (OECD et al., 2019[2]). A wave of protests in late-2019 highlighted the rise in social discontent and growing aspirations for better quality public services, and greater well-being for all. While the Covid-19 crisis may further deepen social discontent, it may also present an opportunity to create consensus among citizens around major pending reforms, and to recover common values around the importance of having strong public services and the relevance of belonging to the formal sector. Indeed, approval ratings for some LAC presidents have increased in the context of the crisis, thus expanding political capital to undergo structural reforms.

The Covid-19 crisis may trigger pending structural reforms in the region. Following the lessons learned from past reforms adopted in crises periods, there are various possible mechanisms through which this crisis may favour reforms. For instance, this crisis may increase further the costs (for example at the fiscal or social fronts) of delaying reform. In this sense, a crisis may result in a "window of opportunity" that enables to undergo reforms that seemed hitherto impossible (Tommasi and Velasco, 1995[37]; Dayton-Johnson, Londoño and Nieto Parra, 2011[38]). Therefore, moving forward, in the context of the Covid-19 crisis, governments must use the momentum to rethink the social pact, addressing structural vulnerabilities – the development traps of low productivity, social vulnerability, institutional weaknesses and environmental sustainability – and responding to citizens' rising aspirations. This would mean moving from today's fragmented status quo to a new equilibrium grounded on equality of opportunities in the longer term, which is the basis of a social pact (Larrain, 2020[34]). Three dimensions should be considered to re-design the social pact in the region:

- **Putting well-being at the centre of public policies and moving towards stronger social protection systems**. This crisis exposes underlying vulnerabilities that simple income metrics, while important, fail to identify and address. Citizens' frustrations with the quality of public services and the multi-dimensional aspects of poverty reinforce the idea that development is much more than GDP. Governments in the region have taken important steps to mainstream well-being in public policies, with a stronger alignment of National Development Strategies to the SDGs. These efforts should not be reversed by the response to the Covid-19 crisis. Furthermore, the crisis has revealed that current mechanisms for social protection may be insufficient; many citizens are left outside the existing channels. The response to the crisis should promote innovative options to reduce social coverage gaps, protect the most vulnerable population, promote quality jobs, improve

the quality and universality of healthcare, and design crisis response mechanisms in the absence of strong automatic stabilisers.

- **Mobilising resources to build resilience and finance inclusive development**: The crisis highlights the need for more financing for public services, social protection and competitiveness. Tax and expenditure systems need to be reformed. In terms of taxes, options include increasing direct personal income taxes, property taxes, environment-related taxes, and eliminating inefficient tax expenditures. These measures should contribute to increasing progressivity and tax collection, while also contributing to the imperative transition to a low-carbon economy. In terms of expenditures, governments should support income security for the most vulnerable, enabling them to plan, cope with risks and transition to the formal economy. They should also strengthen investment to promote financially and environmentally sustainable MSMEs with better insertion in local and global value chains to overcome the regional productivity trap.
- **Defining a sustainable development strategy where all actors are involved**. More than ever the Covid-19 crisis highlights the need for effective co-ordination and coherence across different actors to deliver the most effective and sustainable responses. Latin American and the Caribbean countries need strategies that empower citizens at all stages of the policy-making process. National strategies should involve a broad range of actors and draw on a variety of knowledge and viewpoints to define policies towards higher levels of productivity and formal job creation in the region. The response to the crisis is an opportunity to transform the development model of LAC by embracing the opportunities and addressing the challenges of two major global trends. First, climate change, which should be turned into an opportunity to direct the economic stimulus towards building a development model grounded on environmental sustainability. Second, the digital transformation, which throughout this crisis is proving to be a tool to preserve certain economic activities and to save jobs in the region, while it exposes the negative consequences of the digital divide. The need to embrace a digital transformation that works for all is another lesson of this crisis.

The role of international co-operation

The relevance of co-ordinating a global response to address the immediate, short and medium-term impacts of the Covid-19 crisis cannot be overemphasised. There are at least three critical areas for co-ordinated action at the international level:

- **Financial support is essential**, working together and involving multilateral banks, bilateral public and private actors and international organisations. Non-negligible financial support is already underway, and the available financial capacity of multilateral institutions can be mobilised. Yet, this may need to be expanded to sustain the support in the medium term. In addition, different official debt-relief alternatives could be considered. In this context, an ambition similar to the Marshall Plan but at the global level in which Latin America and the Caribbean has a voice is fundamental. To support sustainable global recovery, developed and developing countries, including Latin American countries, should join forces and establish a dedicated global investment fund.
- **International co-operation is critical**, and the role of the G20 must be central to co-ordinate the response to the health emergency but also to the mobilisation of financial resources at a global level. Beyond this, mechanisms for knowledge-sharing, policy dialogues and technological transfers are needed to spur a lasting, sustainable recovery and a reinvigorated multilateral system where the region should play an active role.
- **Regional co-operation and integration** appear as a pending, yet highly desirable objective, both to address the urgent consequences of the crisis and also to drive the recovery and prepare for future setbacks. Though still limited in size, immediate co-operation is already taking place through existing sub-regional agreements, such as Mercosur with the Emergency Fund for Covid-19.

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