

Updated as of April 27th, 2020

Central America:

Analysis of possible economic and fiscal risks of the Covid-19 crisis

Elements for discussion

Guatemala, Central America, April 28th, 2020

Image source: paho.org

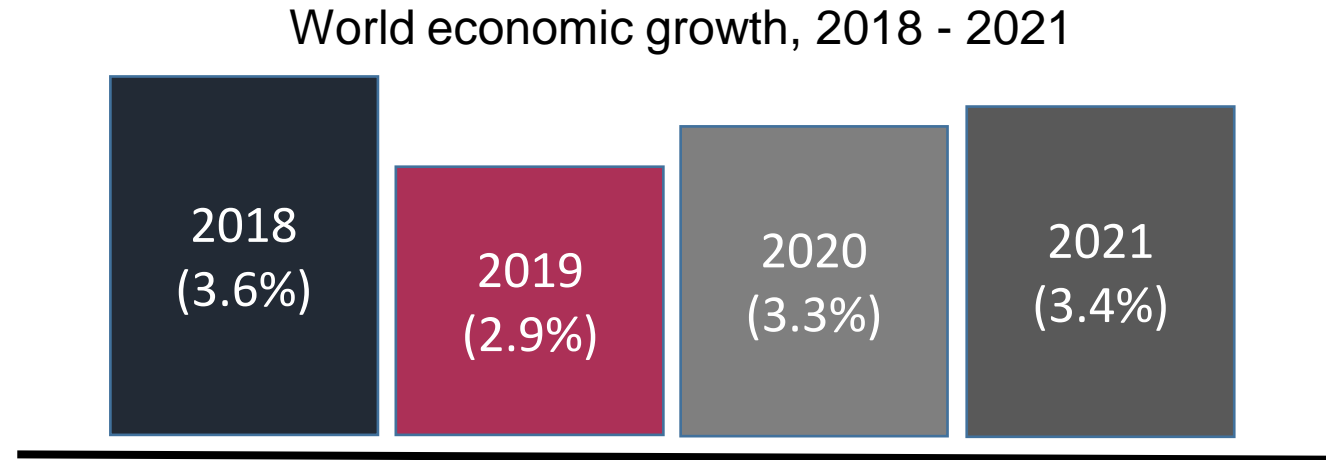
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- 2. Covid-19: expected impacts on the economic activity**
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1 Economy and fiscal policy in Central America at the beginning of 2020

IMF, January 2020

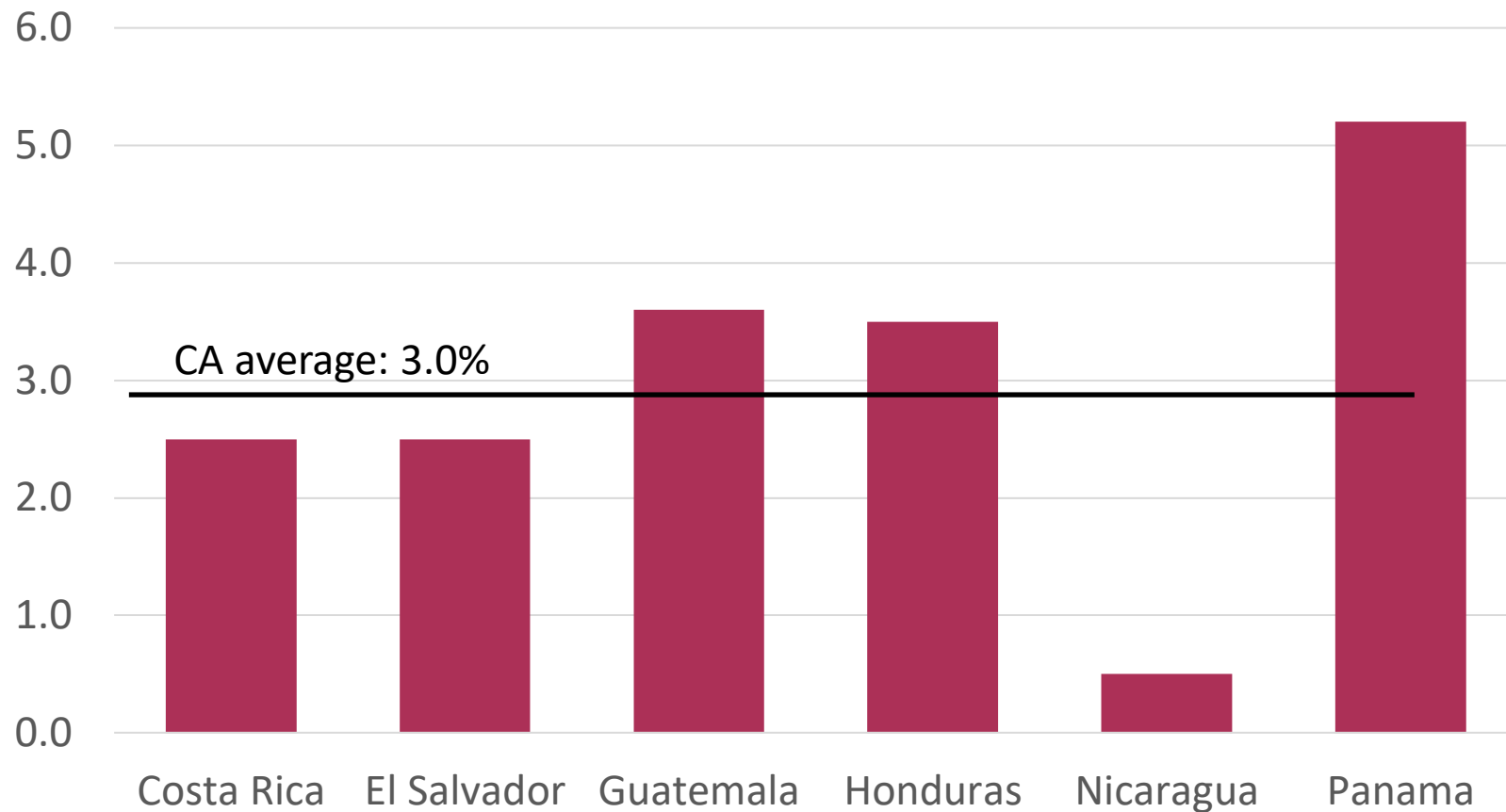
“Tentative Stabilization, Sluggish Recovery?”



“These outcomes depend to an important extent on avoiding further escalation in the US-China trade tensions [...], averting a no-deal Brexit, and the economic ramifications of social unrest and geopolitical tensions remaining contained.”

Governments projections, January 2020

Central America: real economic growth estimations



Source: Icefi based on official statistics.

January, 2020

Central America: overview of the expected fiscal situation for 2020 (% of GDP)

Macro-fiscal variables	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua	Panama
Tax burden	13.4%	18.2%	10.5%	16.8%	17.2%	7.7%
Public expenditure	22.1%	22.1%	13.8%	18.4%	18.9%	15.5%
Fiscal deficit	-7.9%	-1.9%	-2.6%	-2.0%	0.0%	-3.1%
Public debt stock	63.3%	71.3%	25.6%	49.4%	38.0%	46.8%

Source: Icefi based on official data.

Note: public debt stock estimates are based on the annual national budget for each country; public expenditure does not include budgetary extensions derived from Covid-19; and, economic growth are the original estimates of the monetary authorities. Tax revenues forecasts for Costa Rica and Guatemala consider a normal collection path.

2 Covid-19: expected impacts on the economic activity

Updated as of April 27th, 2020

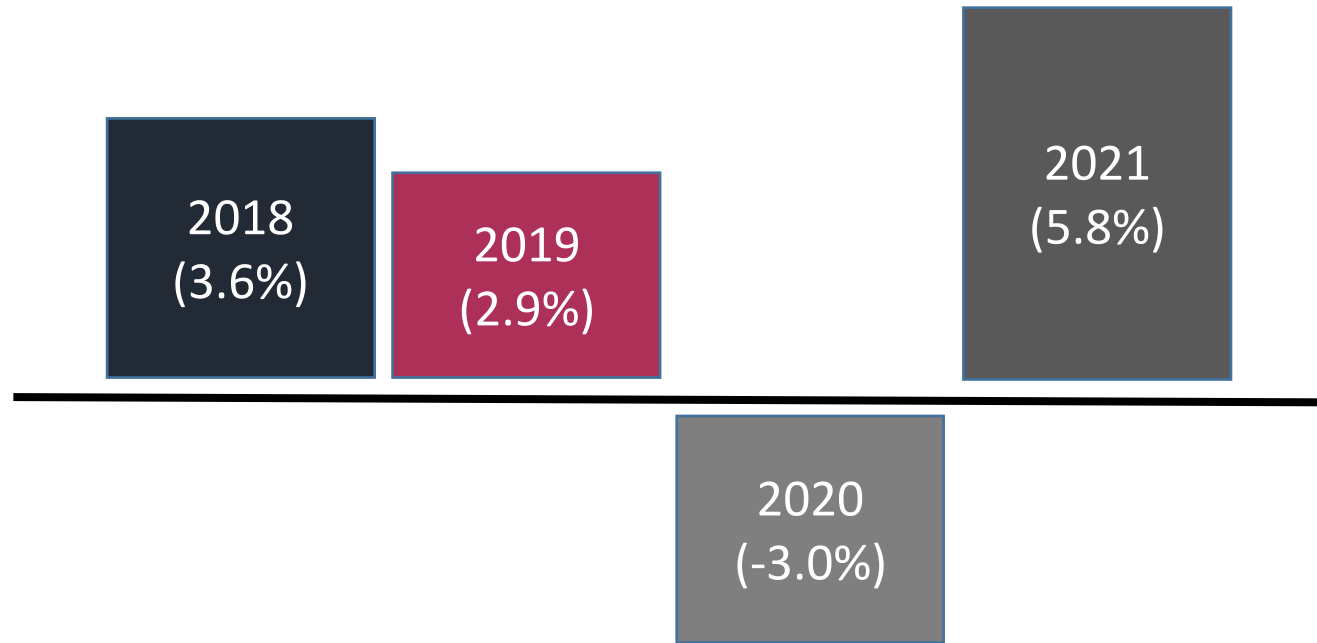
Covid-19: pandemic advance

Country	Confirmed cases	Deaths
World total	2,883,603	198,842
Central America	7,642	250
Costa Rica	693	6
El Salvador	298	8
Guatemala	473	15
Honduras	627	59
Nicaragua	13	3
Panama	5,538	159

IMF, April 14th, 2020

“The great lockdown”

World economic growth, 2018 - 2021



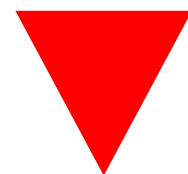
“[...] It is very likely that this year the global economy will experience its worst recession since the Great Depression [...] A partial recovery is projected for 2021, with above trend growth rates, but the level of GDP will remain below the pre-virus trend, with considerable uncertainty about the strength of the rebound”

Economic impacts caused by Covid-19

- It is complicated to predict the total impact of the emergency in economic activity. However, different sources identify the greatest impacts on: **tourists flows, foreign remittances, exports and employment.**
- Each impact has isolated effects and interconnected effects with the rest of the economic activity
 - That's why is too early to try to estimate a total effect.
- Icefi estimated the isolated effect of each impact.
 - It's important to note that the results represent the maximum effect in each scenario, without the interconnected effects with the rest of the economic activity
 - However this data is useful to outline the impact of the emergency.
- Icefi considered the following 4 scenarios:
 - Reduction by 1/3 in tourism revenues
 - 20% drop in family remittances, and hence a related drop in consumption
 - 20% decline in exports
 - Economic activity shutdown during 4 weeks

Four direct impacts on the Central American economy

Tourism

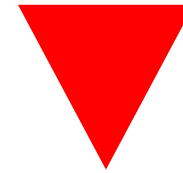


20.0% - 30.0%

(Updated as of March 27th, 2020) The World Tourism Organization (UNWTO) released its updated assessment of the likely impact of the COVID-19 on international tourism. Taking into account the unparalleled introduction of travel restrictions across the world, the United Nations specialized agency for tourism expects that international tourist arrivals will be down by 20% to 30% in 2020 when compared with 2019 figures [...] this could translate into a decline in international tourism receipts (exports) of between USD 300-450 billion almost one third of the USD 1.5 trillion generated in 2019. Taking into account past market trends, this would mean that between five and seven years' worth of growth will be lost to COVID-19.

Four direct impacts on the Central American economy

Family remittances



20.0%

(Published on March 20th, 2020) Investmaster warns that Guatemala may suffer quarterly decreases in family remittances of 1.0%, 30.0%, 25.0% and 23.0%, respectively.

Icefi's evaluation exercise assumes a 20% fall in the remittances flow compared to 2019.

Four direct impacts on the Central American economy

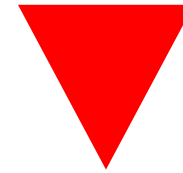


(Published on March 26th, 2020) According to Capital Economics Consulting, worldwide exports are expected to drop 20.0% in 2020.

In 2009, GDP contracted 0.6% and trade volumes collapsed by 13.0%. By 2020, a greater economic contraction is expected, around 2.5%. This suggests that this year trade volumes may even decrease in 25.0%.

Four direct impacts on the Central American economy

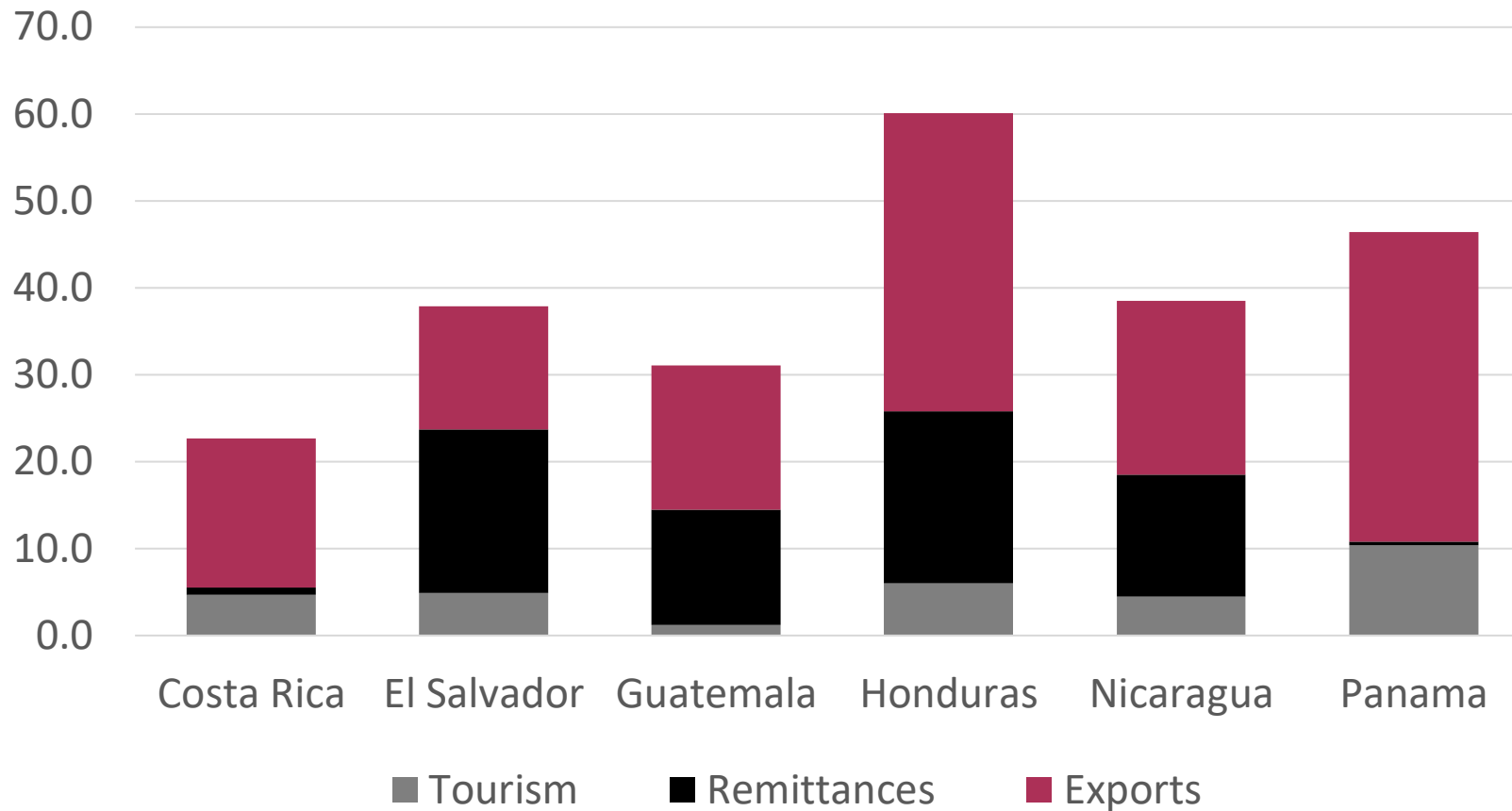
Economic shutdown during one month
(fall in aggregated demand)



8.3%

Government policies of social distancing has been associated with the declining or shutdown of non-essential activities.

Central America: percentage of economic activity at direct risk due to tourism, exports and remittances fall



Source: Icefi

Central America: impact on real economic growth

Country / Region	Base scenario of economic growth	Scenario 1. Reduction by 33.3% in tourism revenues	Scenario 2. A 20% drop in family remittances from USA	Scenario 3. A 20% decline in exports	Scenario 4. Economic activity shutdown during one month
CA average	3.0	0.8	1.7	-1.9	-4.8
Costa Rica	2.5	0.3	2.3	-2.2	-6.1
El Salvador	2.5	-0.8	-0.4	-3.4	-6.4
Guatemala	3.6	3.1	2.2	-0.9	-4.7
Honduras	3.5	1.8	2.0	-2.7	-4.8
Nicaragua	0.5	-1.3	-1.0	-1.0	-3.2
Panama	5.2	1.6	5.1	-0.9	-3.3

Central America: impact on employment

Country / Region	Scenario 1. Reduction by 33.3% in tourism revenues	Scenario 2. A 20% drop in family remittances from USA	Scenario 3. A 20% decline in exports	Scenario 4. Economic activity shutdown during one month
CA average	-367,314	-452,148	-1,166,691	-1,869,964
Costa Rica	-31,026	-3,583	-63,912	-145,497
El Salvador	-74,578	-71,377	-133,124	-216,165
Guatemala	-36,043	-96,535	-376,160	-555,060
Honduras	-84,025	-46,599	-194,079	-261,328
Nicaragua	-103,065	-233,206	-359,011	-585,879
Panama	-38,576	-849	-40,405	-106,035

To simplify fiscal analysis, Icefi summarizes 4 aggregate scenarios for economic growth:

Scenario 1: original official real GDP growth estimates are reduced by 50.0%; 2.0% fall in tax productivity due to increase in tax evasion, exceptions and moratoriums exceeding the fiscal period; fall in international fuel prices and consumption inelasticity due to lockdown; and, loss in tax control.

*Nicaragua is a different case because it has a preexisting recession, thus similar productivity is assumed.

Scenario 2: no variation in GDP and 4.0% decline in tax productivity

Scenario 3: decreases of 2.0% GDP and 6.0% in tax productivity

Scenario 4: decreases of 4.0% GDP and 8.0% in tax productivity

Updated as of April, 2020

Central America: economic growth scenarios for 2020

Country	Base scenario	Icefi				IMF	WB
		Scenario 1 (most optimistic)	Scenario 2 (intermediate optimistic)	Scenario 3 (intermediate pessimistic)	Scenario 4 (most pessimistic)		
Release date	January 2020	April 2020				April 2020	
Costa Rica	2.5	1.3	0.0	-2.0	-4.0	-3.3	-3.3
El Salvador	2.5	1.3	0.0	-2.0	-4.0	-5.4	-4.3
Guatemala	3.6	1.8	0.0	-2.0	-4.0	-2.0	-1.8
Honduras	3.5	1.8	0.0	-2.0	-4.0	-2.4	-2.3
Nicaragua	0.5	0.3	0.0	-2.0	-4.0	-6.0	-4.3
Panama	5.2	2.6	0.0	-2.0	-4.0	-2.0	-2.0
Central America	3.0	1.5	0.0	-2.0	-4.0	-3.5	-3.0

Source: Icefi based on official data, World Bank and International Monetary Fund.

Evaluation of impacts in well-being and economic development remain to be done:

Social inequality in access to health system, social care and protection, and support for MSMEs and other businesses

Death, unemployment and poverty

Business bankruptcies

Loss in production capacity for domestic and external consumption

Democratic ungovernability

... but these depend, in great measure, to the implemented public policies and their effectiveness

Covid-19 impacts exacerbate structural problems

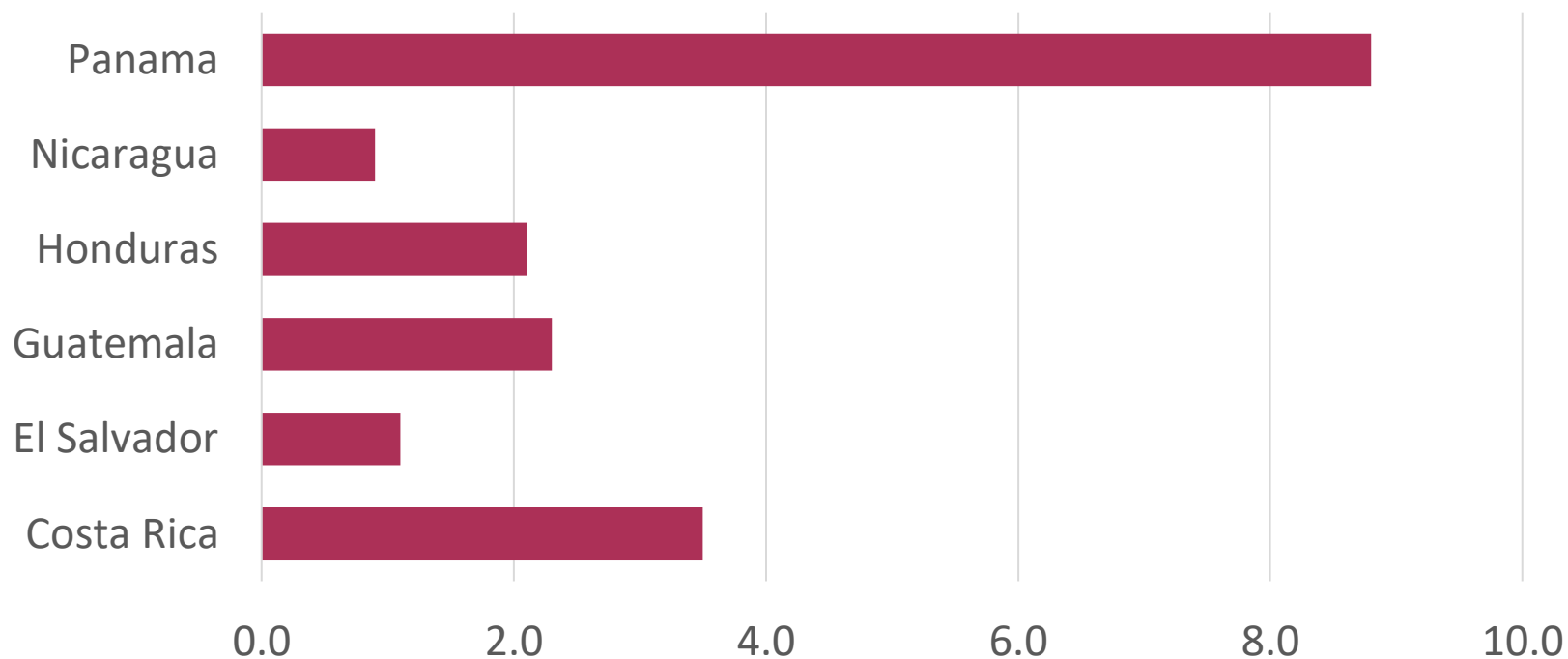
A health system fragmented and run as a private business

Type of health system	Low per capita income (< USD 3,895)	Middle per capita income (USD 3,895 - USD 12,055)	High per capita income (> USD 12,055)
Mainly public (more than 66% of national health expenditure is public)	Bolivia	Belize, Colombia, Costa Rica and Cuba	Argentina, Canada and Uruguay
Mixed (between 50% - 66% of the national health expenditure is public)	El Salvador and Nicaragua	Ecuador, Jamaica, Mexico, Peru and Surinam	Chile, Panama , Trinidad and Tobago and USA
Market oriented (Less than 50% of the national health expenditure is public)	Honduras and Haiti	Brazil, Dominican Republic, Guatemala , Paraguay and Venezuela	

Covid-19 impacts exacerbate structural problems

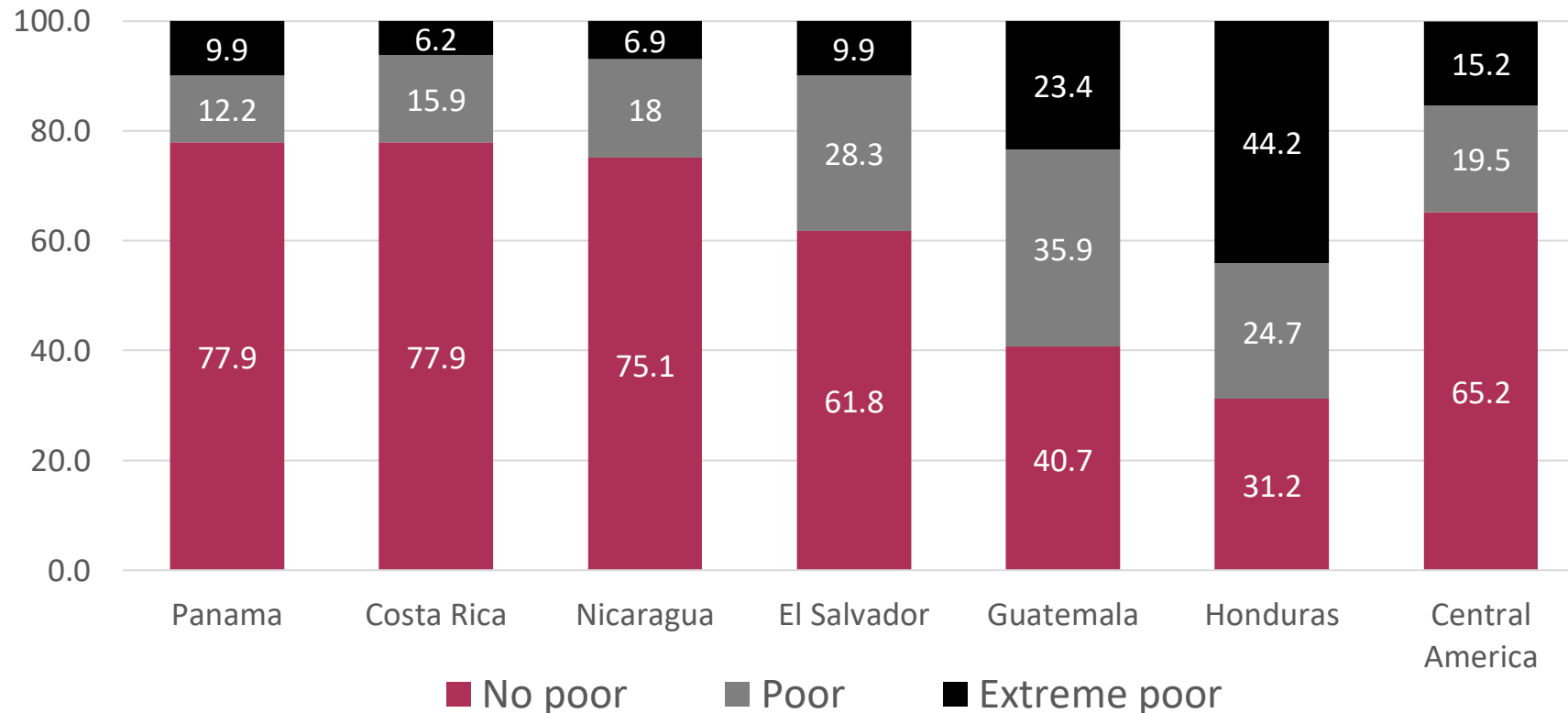
An exhausted economic model with low productive transformation and incapacity to absorb the working-age population

Central America: GDP growth rate and variation in the number of inhabitants per country (1960-2017)



Covid-19 impacts exacerbate structural problems

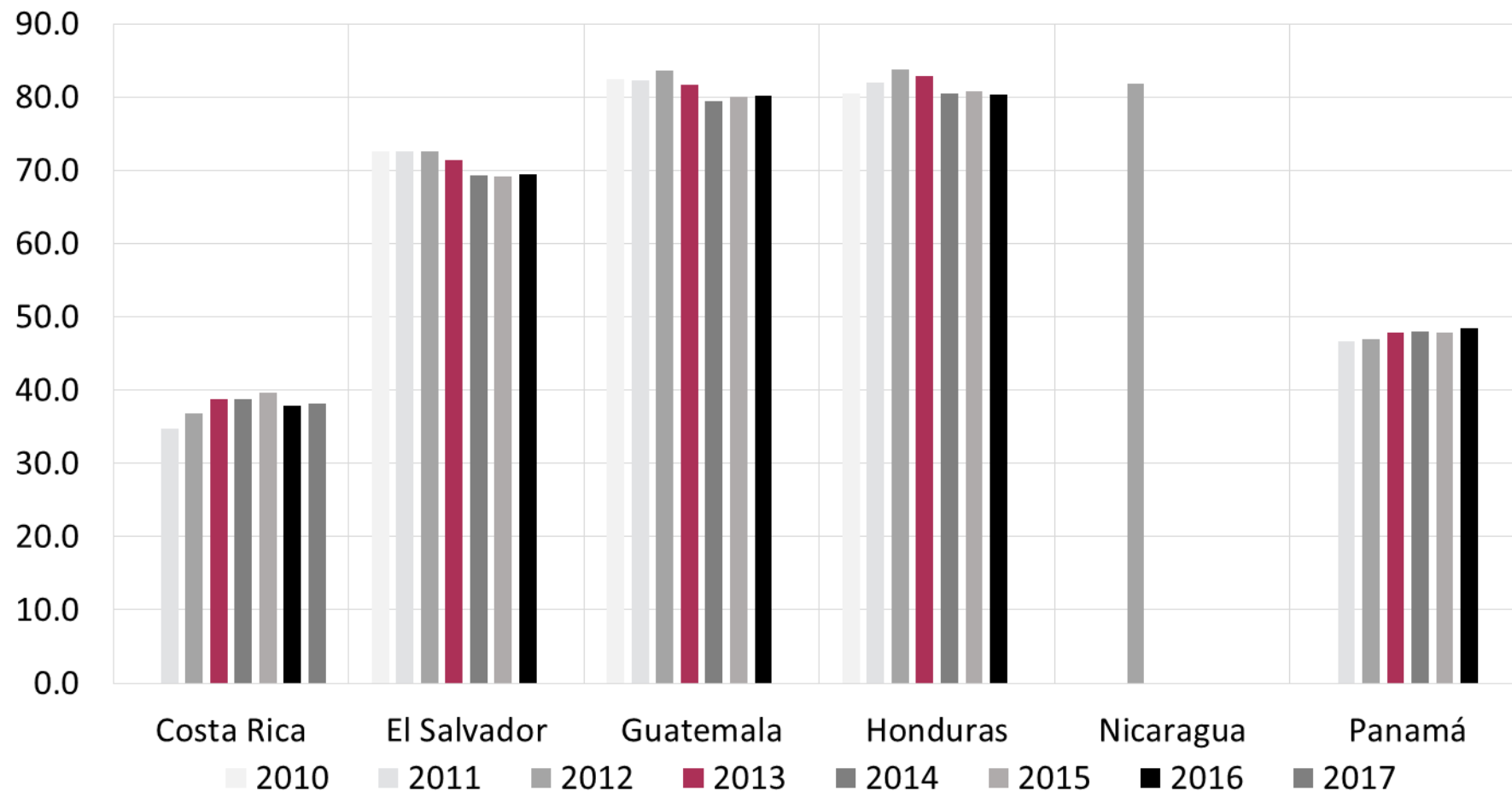
Central America: 22.5 million people live in poverty (45 out of 100 inhabitants); 18.4 million in GT, SV and HND



The richest 20.0% of population concentrates more than a half (52.6%) of the national income, while the poorest 20.0% only keeps the 4.3%

Covid-19 impacts exacerbate structural problems

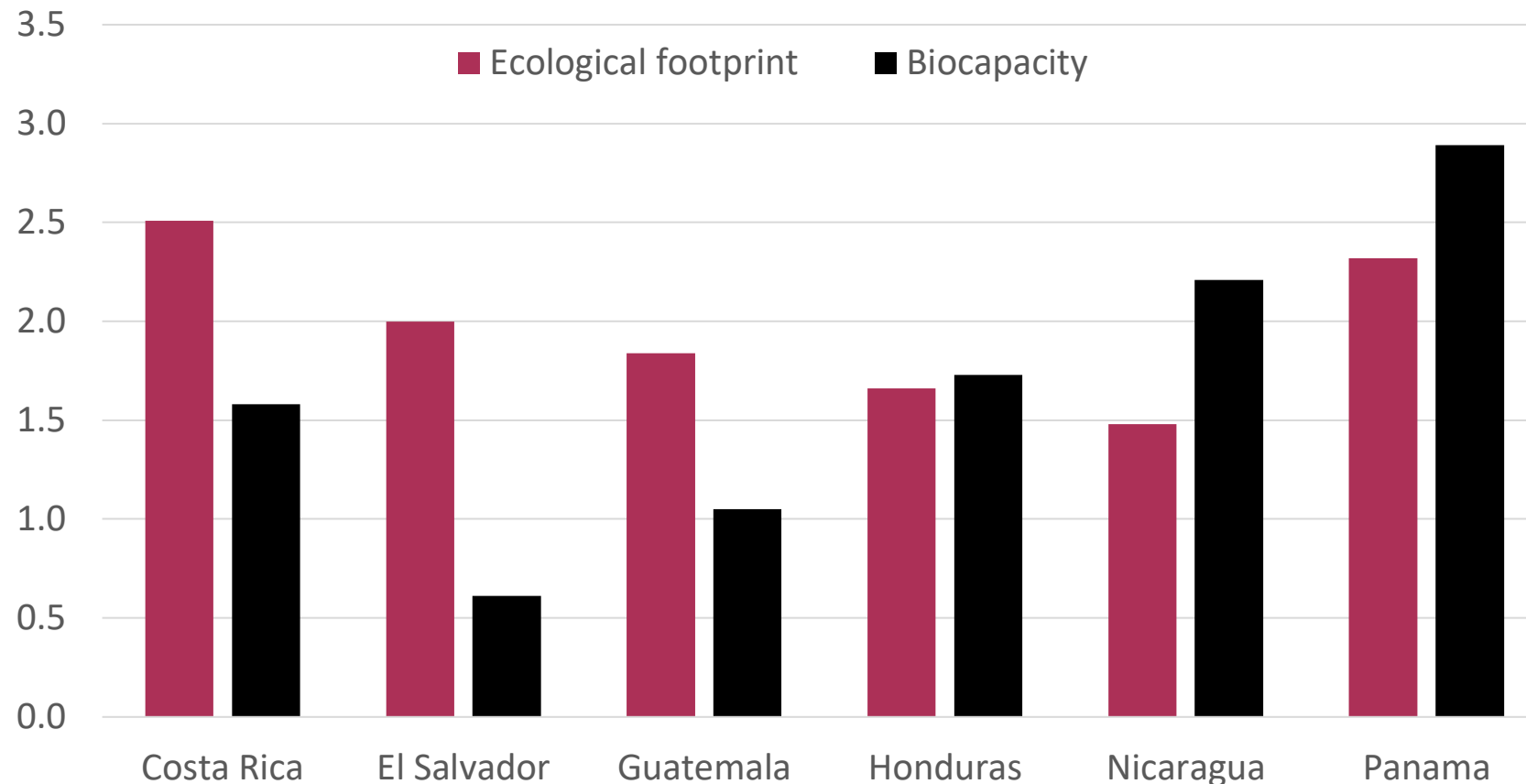
Central America: 6 out of 10 workers in the informal sector



Covid-19 impacts exacerbate structural problems

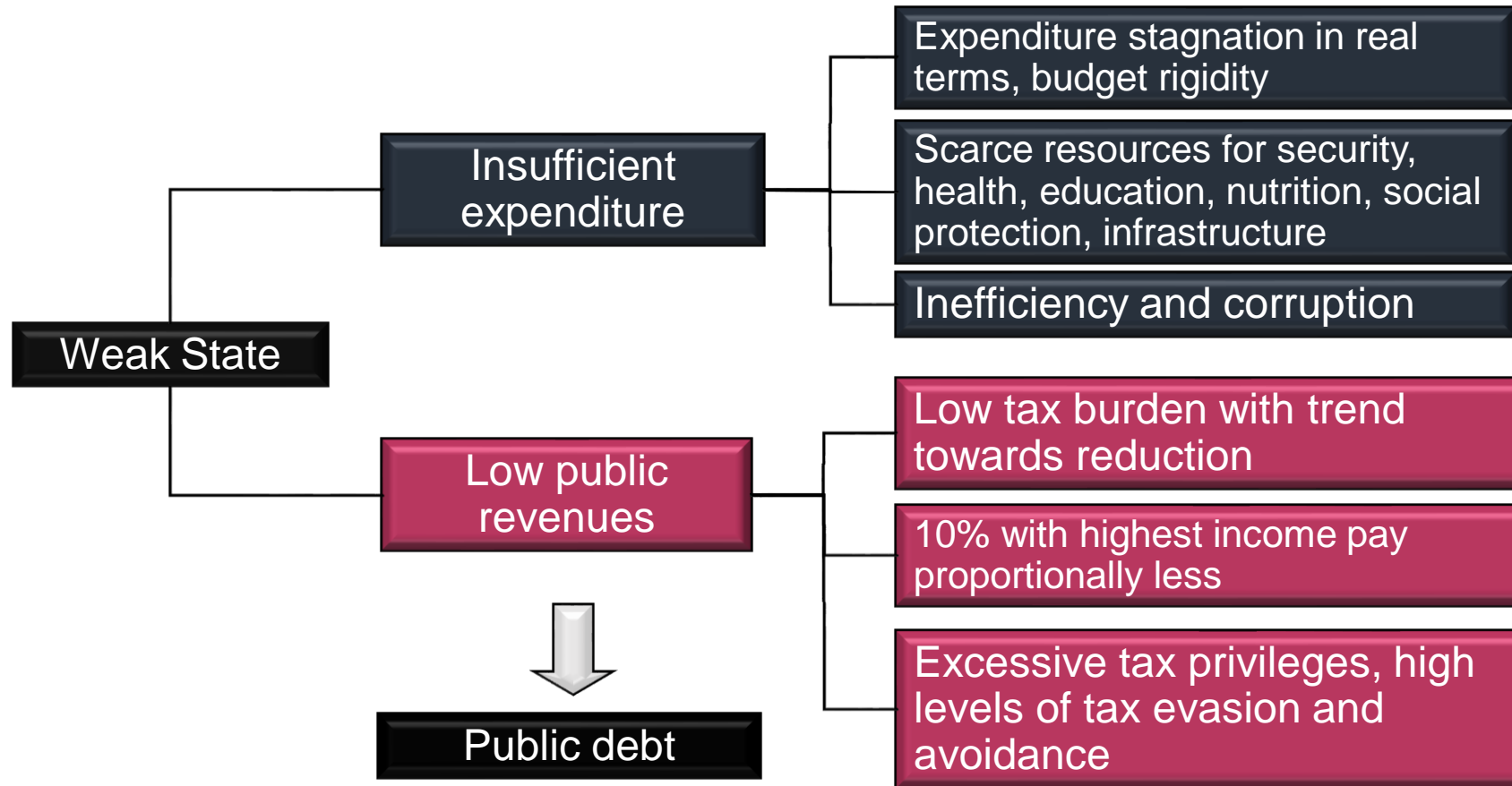
Unsustainable consumption patterns

Central America: ecological footprint and biocapacity in global hectares per capita (2014)



Covid-19 impacts exacerbate structural problems

A fiscal policy for survival



3 Fiscal forecasts (tax burden, public expenditure, fiscal deficit and public debt stock)

Central America: main economic and fiscal measures adopted by the countries to address the Covid-19 emergency (part 1)

Measure	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua	Panama
Tax moratoriums	Tax moratorium from April to June; moratorium on airplane ticket taxes	Extension of the income tax payment period and possibility of paying in 8 installments; suspension of the tourism tax (5%) for three months; tax exemption for donations; exemption from Import Tariff Duty (DAI) and VAT for purchases of white corn, beans and rice.		General tax moratorium; 25% reduction of anticipated income tax; 8.5% discount on income tax for small and medium enterprises. Additional 10% deduction for employers who retain their workers. Cessation of IHSS contributions.		Extension of tax amnesty to June; 120 days for paying taxes during this period; one more year of income tax exemption for small and medium enterprises.
Public service payment moratorium	Prohibition of basic services suspension due to lack of payment.	Grace period of 3 months for payment of electricity, water, telephone and cable TV; debt can be deferred for two years. Freezing of rent payments for three months, divided into 12 months.	Law passed to provide for a moratorium on water, electricity, telephones and the Internet.			Suspension of payment for telephone, the Internet and electricity.
Credit payment moratorium		Grace period of 3 months for the payment of different types of credits and house debts.	Bank moratorium on loan payments for up to three months; the balance is carried forward to the end of the loan period.	Three months' grace for debtors; the balance is carried forward to the end of the loan period.		The Savings Bank announces a 90-day deferral of credit payments.

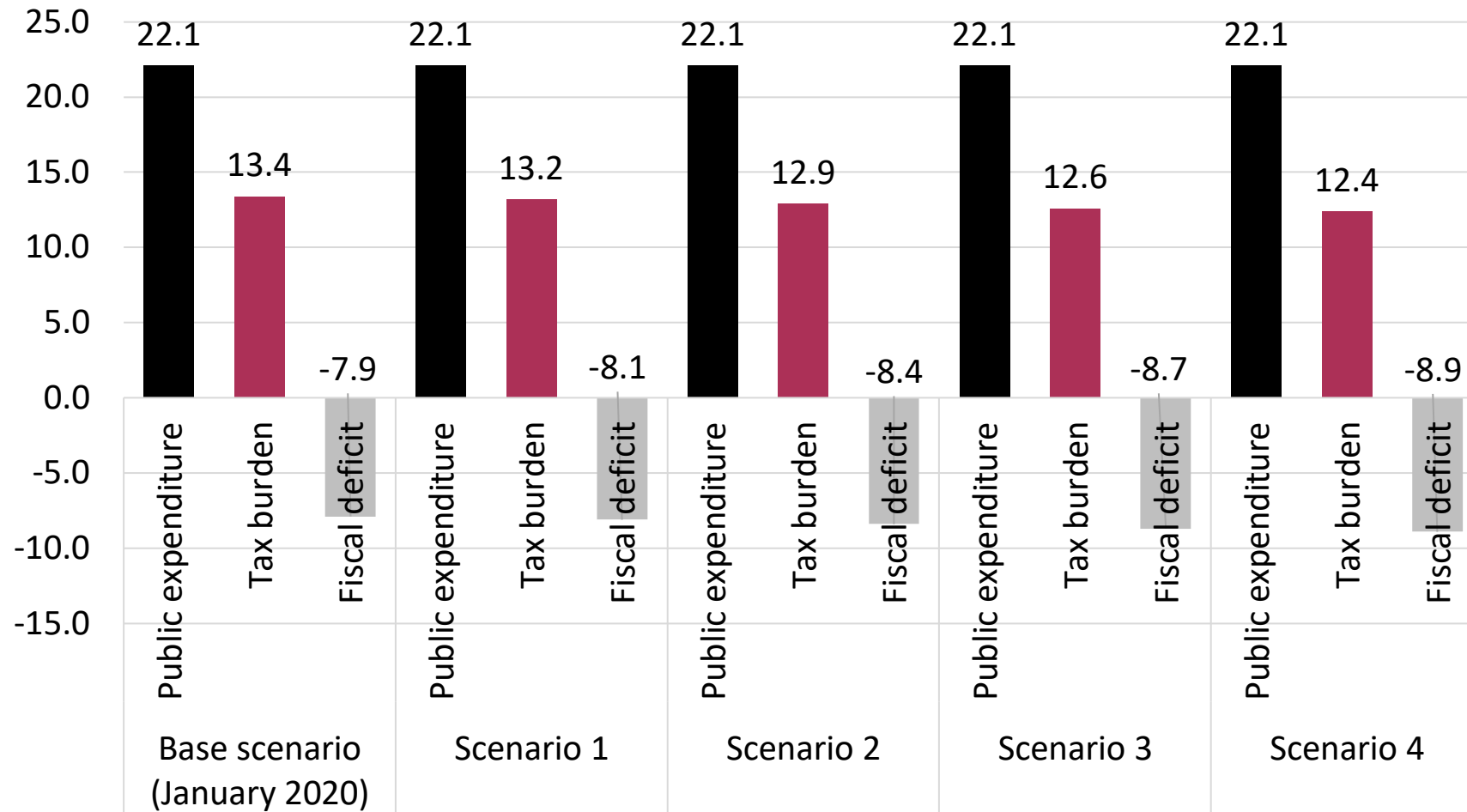
Central America: main economic and fiscal measures adopted by the countries to address the Covid-19 emergency (part 2)

Measure	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua	Panama
Authorization of extraordinary credit lines in public or private banks		Lines of credit for the companies concerned. Loans are intended for the payment of payroll, basic services, transport of merchandise or customs, payment of accounts payable or receivable, and the company's operational expenses.	Lines of credit for small and medium enterprises; credit for companies in general, including those owned by politicians.	Expansion of credit lines for banks, cooperatives, rural savings and credit banks; as well as for housing construction. Credits for entrepreneurs.		
Increase in public spending	A budgetary expansion and a budgetary modification to finance USD 885 million for policy measures to address Covid-19.	Negotiation of USD2,000.0 for the emergency fund; provision of USD 300 to serve 1.5 million households for a total of USD 450.0 million for one month.	Three budgetary expansions that mix administrative aspects and support elements to address Covid-19. The three expansions total Q19.8 billion.	Credit secured USD143 million with the IMF; budgetary expansion of USD 2 billion. The Sefin informed that the expenditure for the emergency is		USD 5.8 billion to address the impact; of which USD 2.5 billion are in bonds to cover the effect of tax moratoriums and low tax collection.
Measures related to fiscal control	Lifting of the fiscal rule (only for specific institutions)	Suspension of the Fiscal Responsibility Law		The debt should not exceed 55% of the GDP		
Other	Protection Bond: a subsidy for workers affected.	ISSS coverage for disability or quarantine coverage; establishment of maximum prices for the basic food basket.	Price control of the basic food basket.	Reduction of the basic policy rate to 4.5% and of other financial availabilities.		

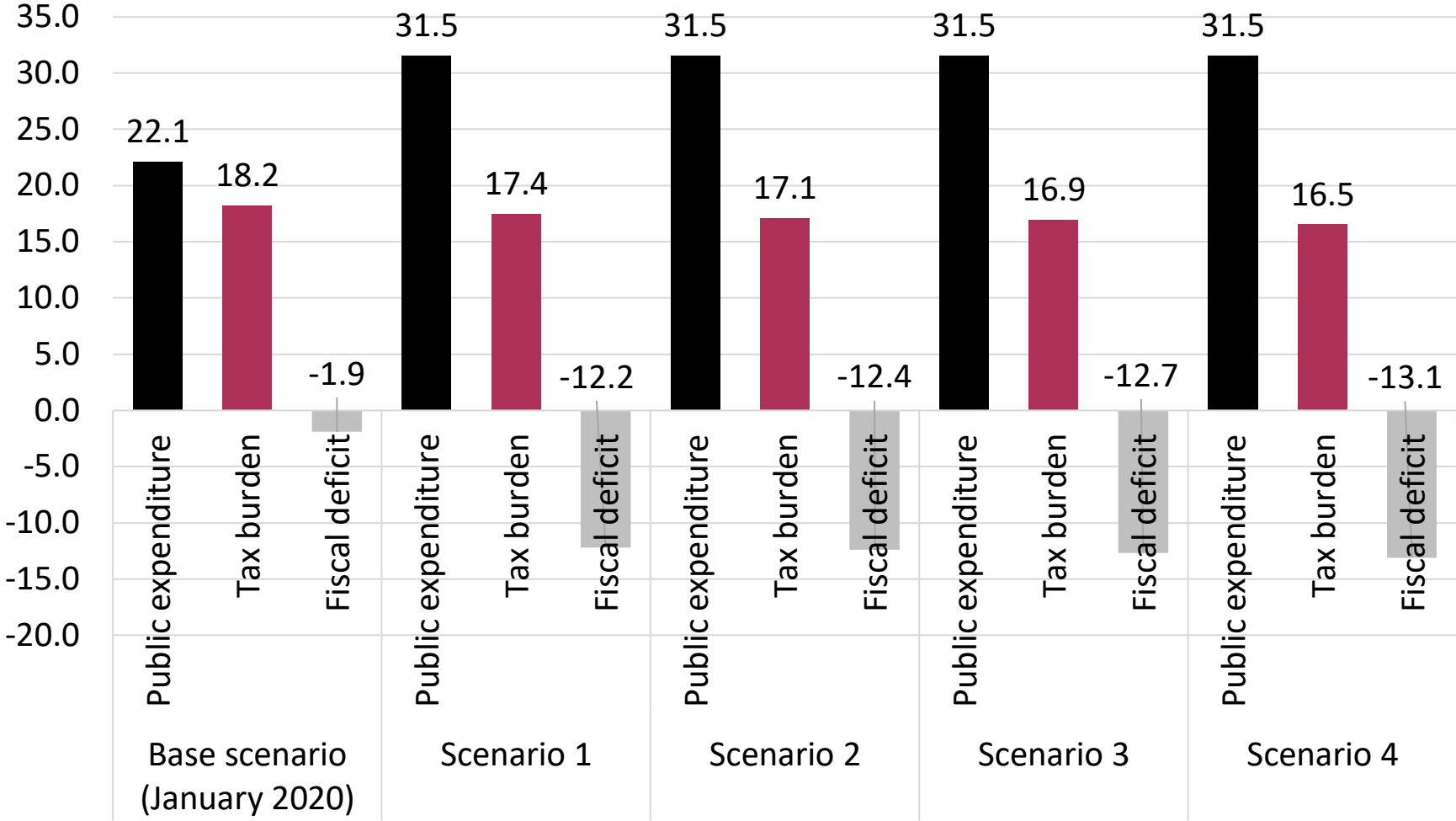
Central America: increase in public spending to address the COVID-19 crisis and sources of financing

Measure	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua	Panama
Increase in public spending in local currency (in millions)	135,665.0	2,046.0	13,756.0	62,220.5		4,400.0
Increase in public spending in millions of US dollars	238.6	2,046.0	1,786.5	2,500.0		4,400.0
Increase in public spending as a percentage of the GDP	0.36 - 0.38	7.40 - 7.90	2.26 - 2.39	9.64 - 10.16		6.35 - 6.78
Sources of funding in millions of US dollars						
World Bank			200.0	194.0		
IADB			79.0			
CABEI						
FMI		389.0		143.0		
CAF	290.7					
Treasury bonds			79.0			5,800.0
Treasury bills		426.2				
Loans between public institutions		25.0	1,428.5			
Use of cash						
Taxes						
Other	1.8	46.0				
Without source of funding		1,184.8		2,163.0		

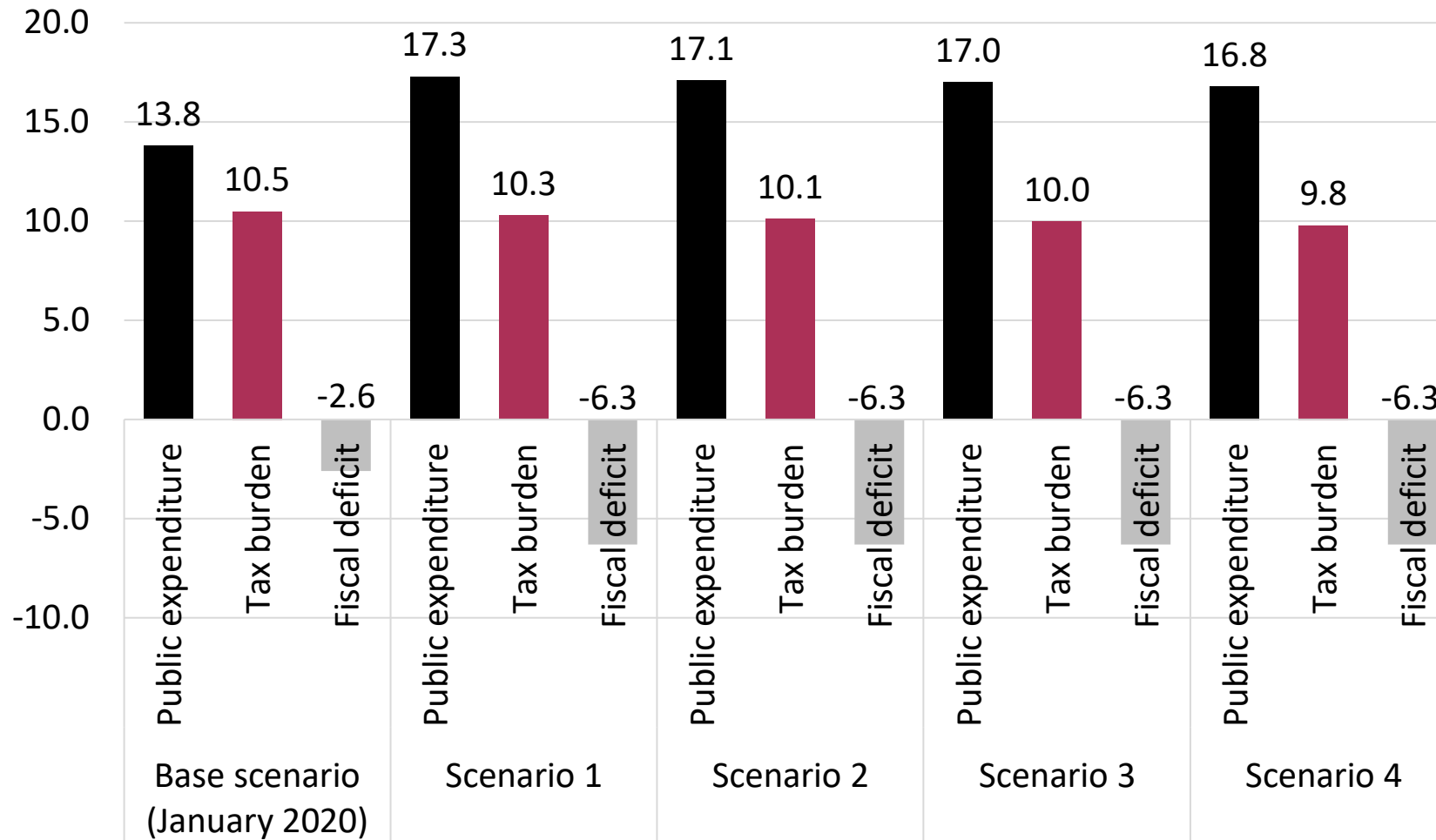
Costa Rica: estimated impact in public finances in the four scenarios



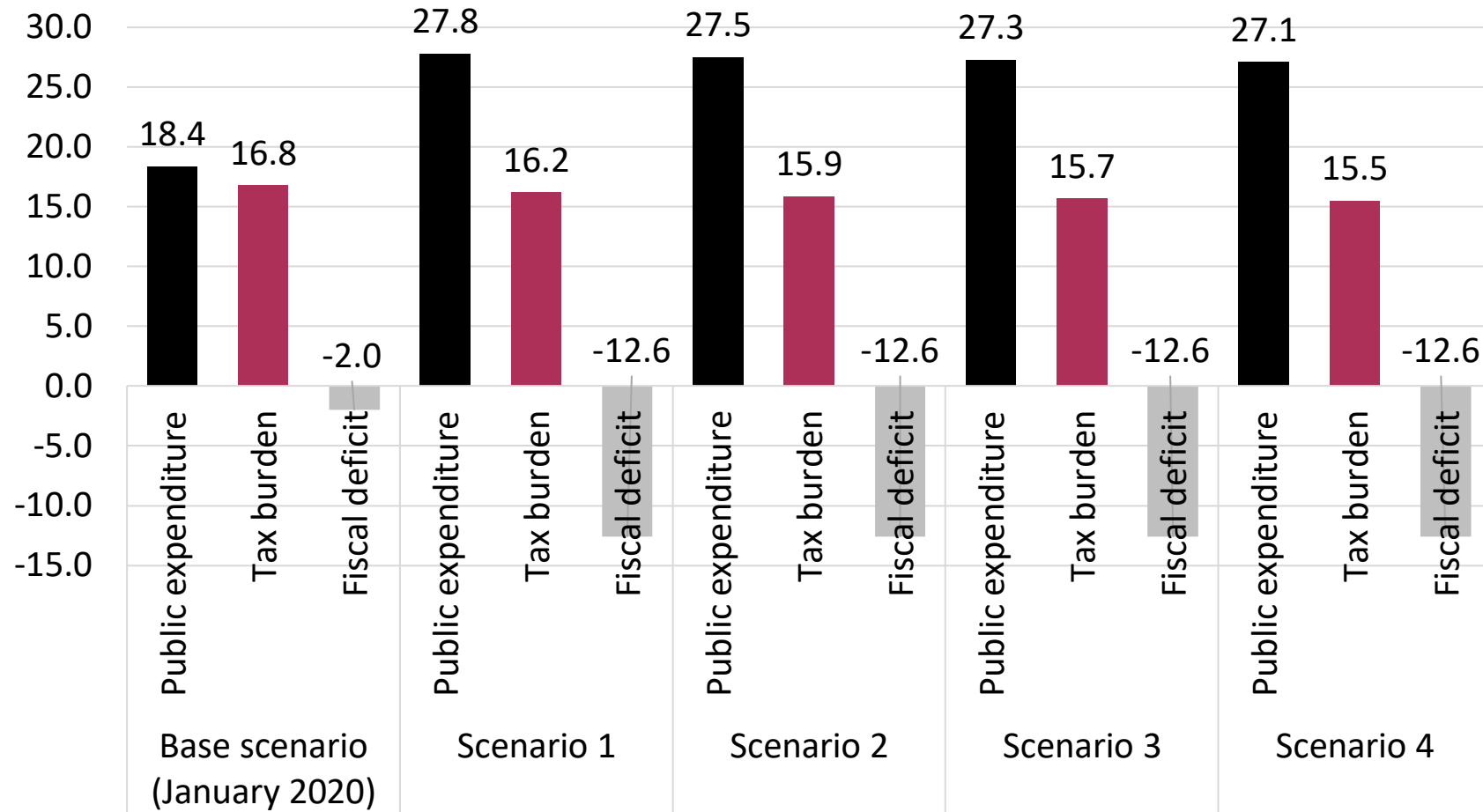
El Salvador: estimated impact in public finances in the four scenarios



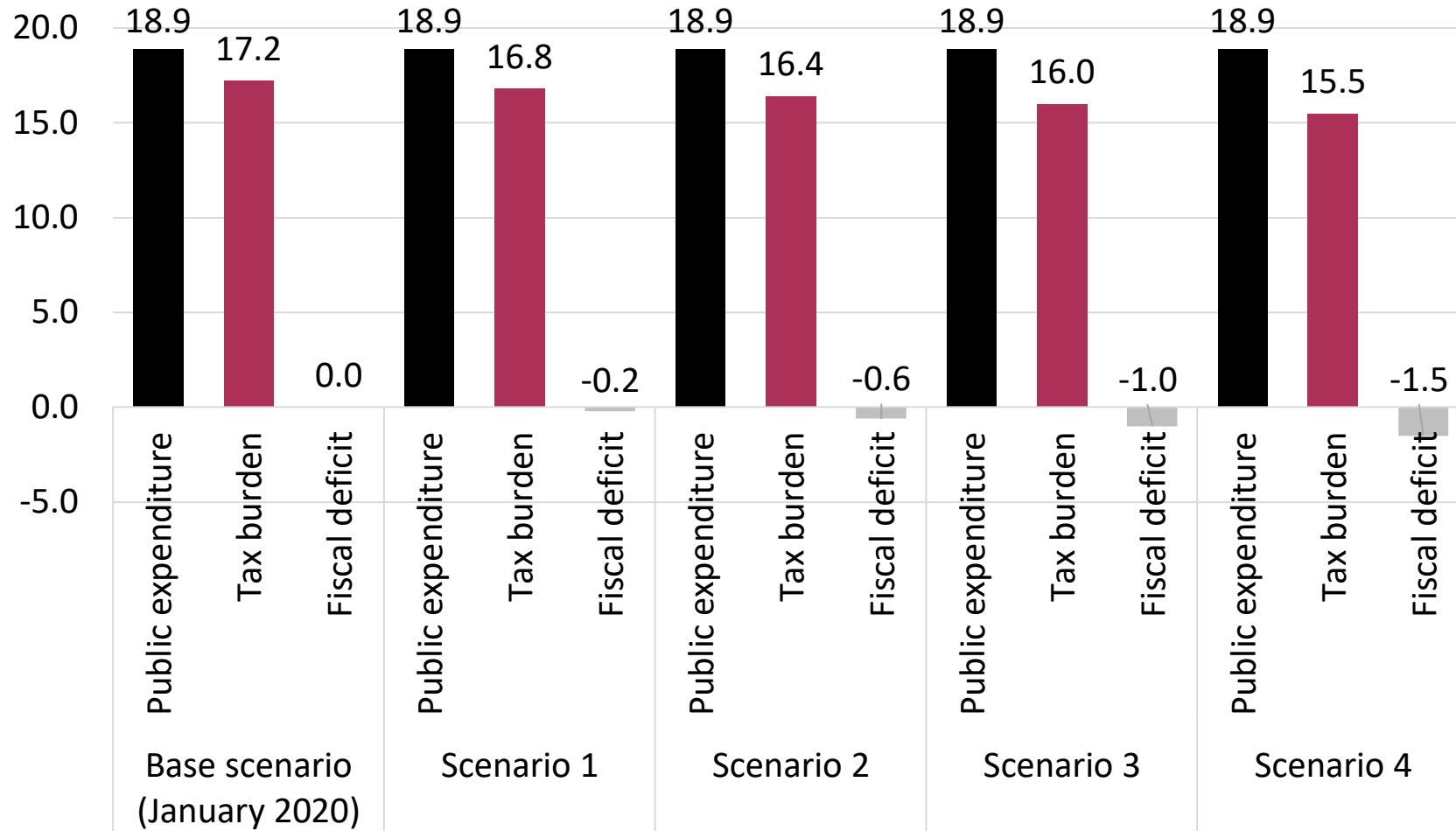
Guatemala: estimated impact in public finances in the four scenarios



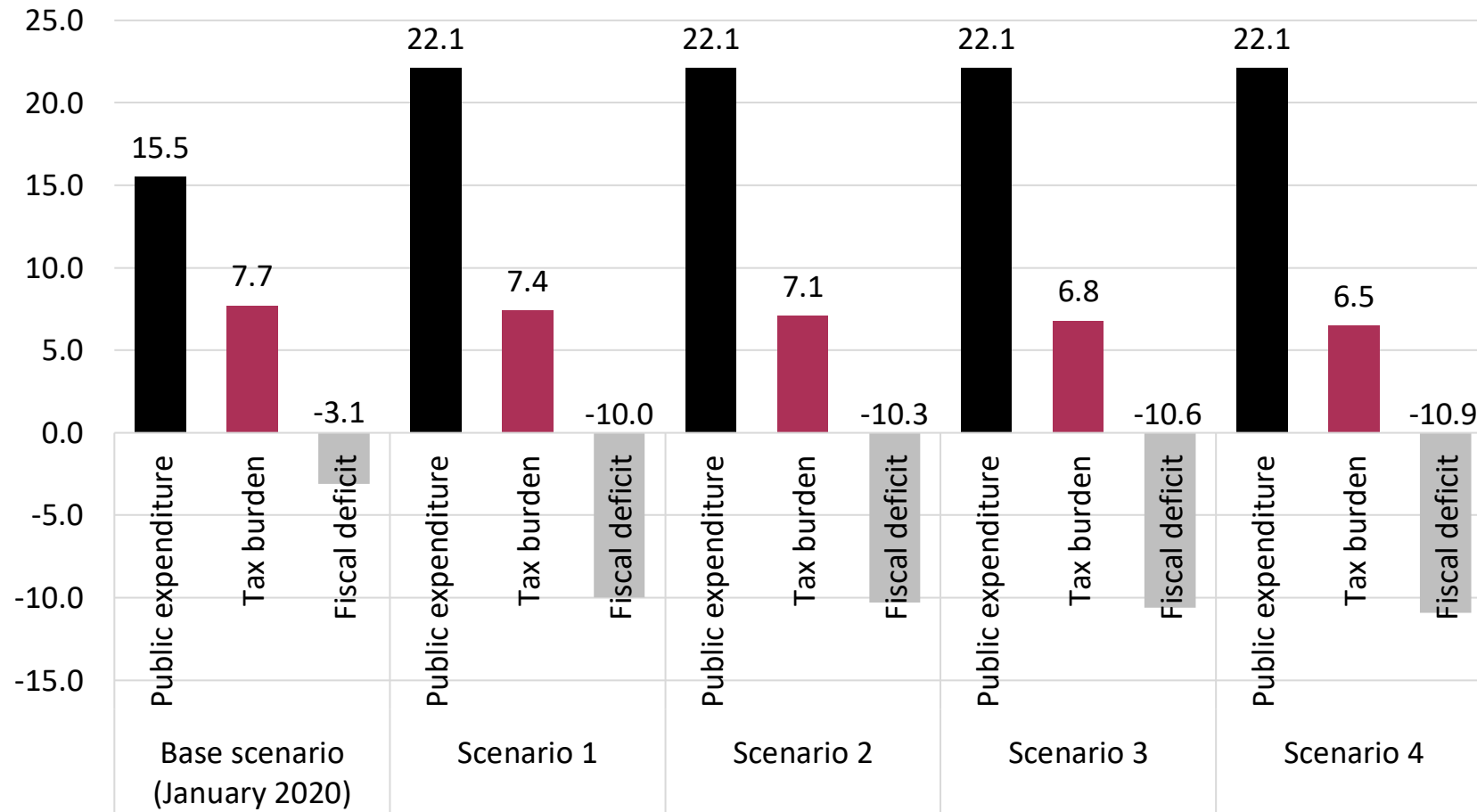
Honduras: estimated impact in public finances in the four scenarios



Nicaragua: estimated impact in public finances in the four scenarios

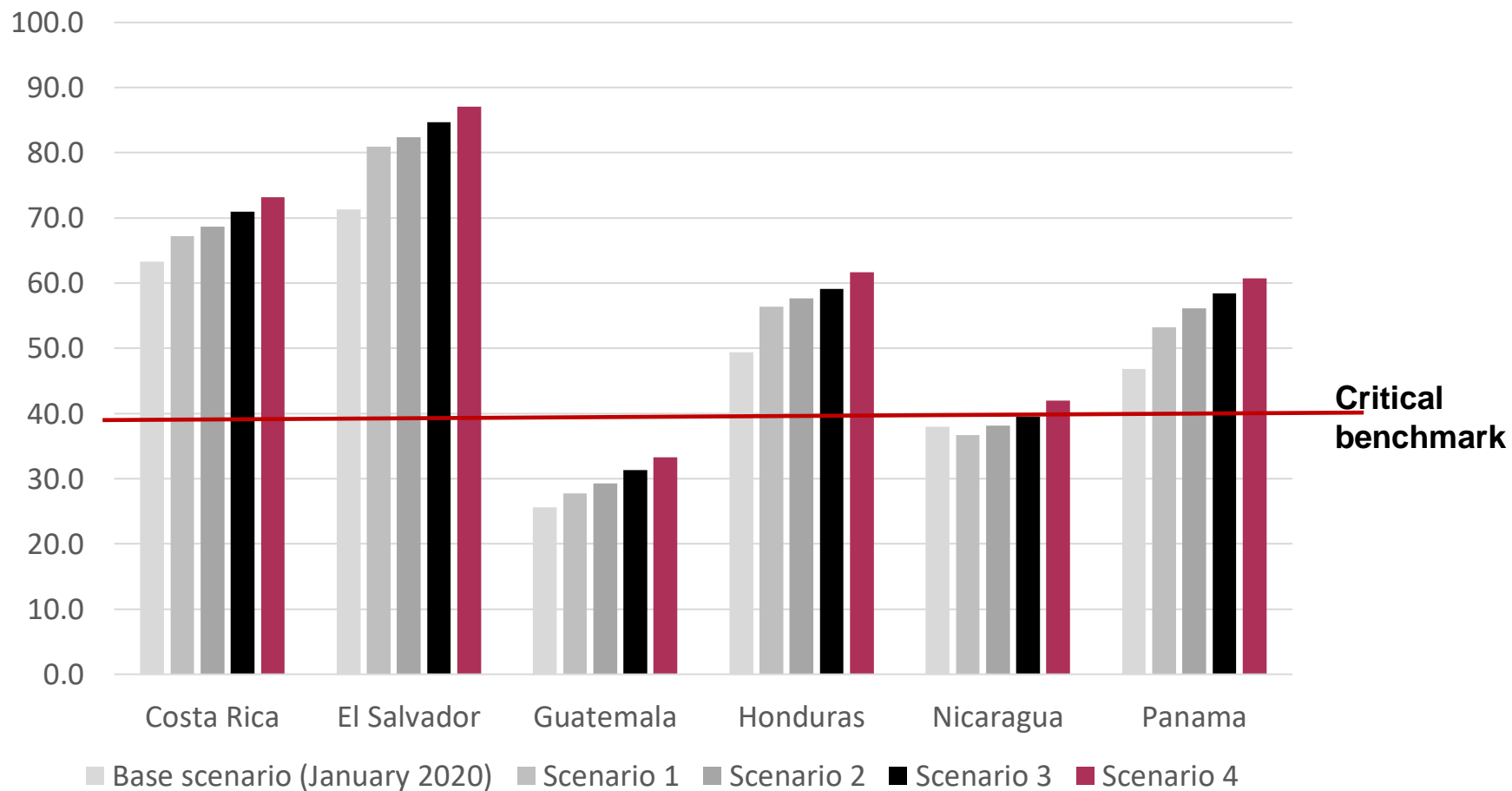


Panama*: estimated impact in public finances in the four scenarios

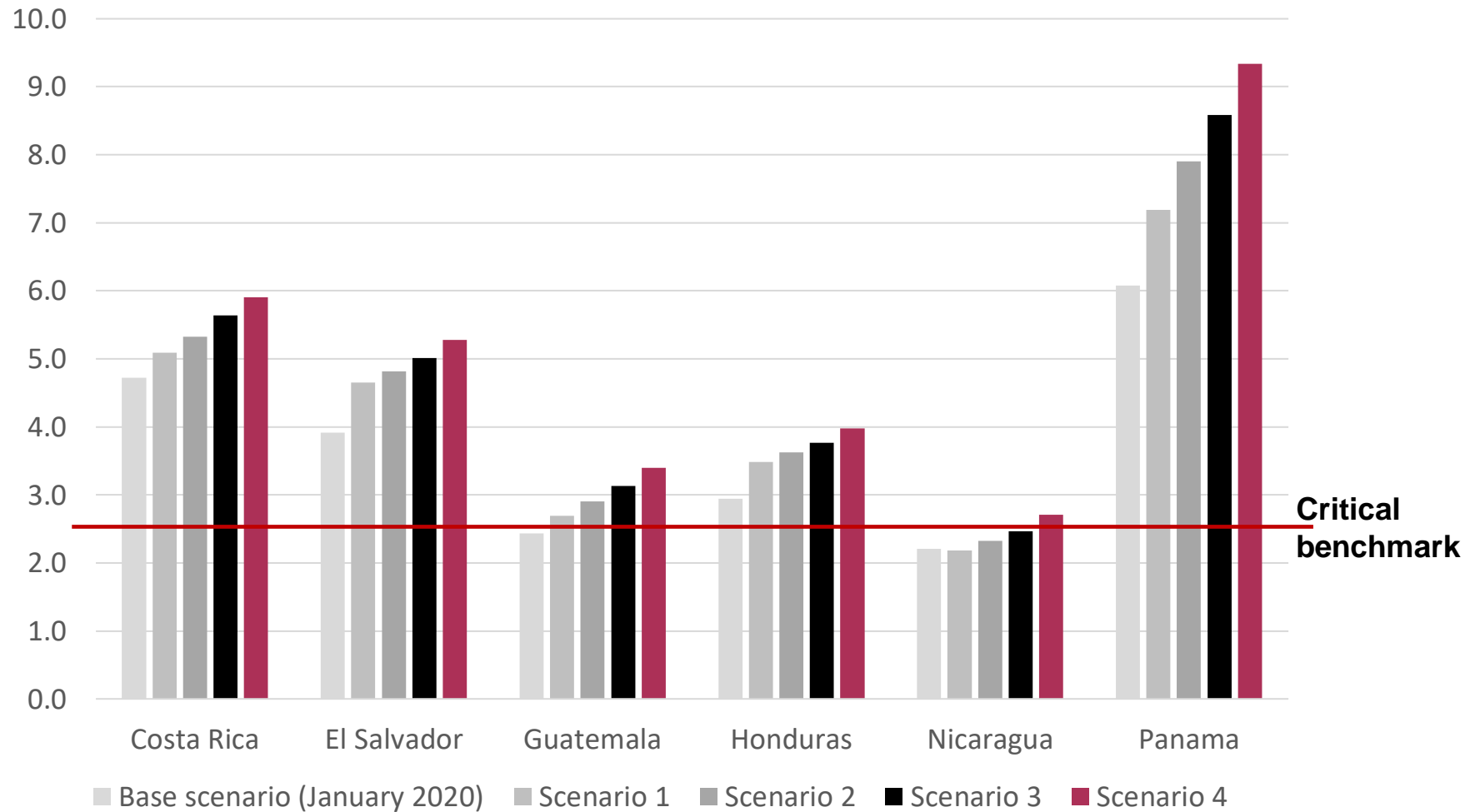


*/ Fall in the Panama Canal revenues are not included.

Central America: public debt stock as % of GDP at the end of 2020 in the four scenarios



Central America: public debt stock as % of tax revenues at the end of 2020 in the four scenarios



Central America: Legislative power sharing in favor of changes in fiscal policy

País	Taxes				Public expenditure increase	Public investment increase	Public debt increase	Transparency and accountability measures
	Increase	Moratorium	Cuts	New privileges				
Costa Rica	Majority is not achieved	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Majority is not achieved
El Salvador	Majority is not achieved	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Majority is not achieved
Guatemala	Majority is not achieved	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Yes, by majority agreement	Majority is not achieved

Honduras

The Government party has majority in Congress or Assembly

Nicaragua

The Government party has majority in Congress or Assembly

Panama

The Government party has majority in Congress or Assembly

4 Icefi's short, medium and long term recommendations

I. Strengthen the role of the State

1. Effective guarantee of economic, social and cultural rights

- 1.1. Guarantee equitable access to health, achieving the smallest number of deaths and, in the medium and long terms, the structural strengthening of the health system
- 1.2. Guarantee free and universal access to pre-elementary, elementary and high schools, advancing towards the development of non-contact modalities
- 1.3. Guarantee free and universal access to work training
- 1.4. Advance towards social protection systems with the objective of universalizing the right of water, environmental sanitization, housing, social security and guaranteed basic income, at least for the working-age population (from 15 years old)
- 1.5. Priority for the universalization process of the traditionally excluded groups: childhood and adolescence; indigenous and afro-descendant population; people living in rural areas; women and female headed households; households in poverty and extreme poverty
- 1.6. Forbid basic services suspension, like water, electric power, phone and Internet, and suspend bills during quarantines and social distancing measures
- 1.7. Measures to keep and improve general social wellbeing

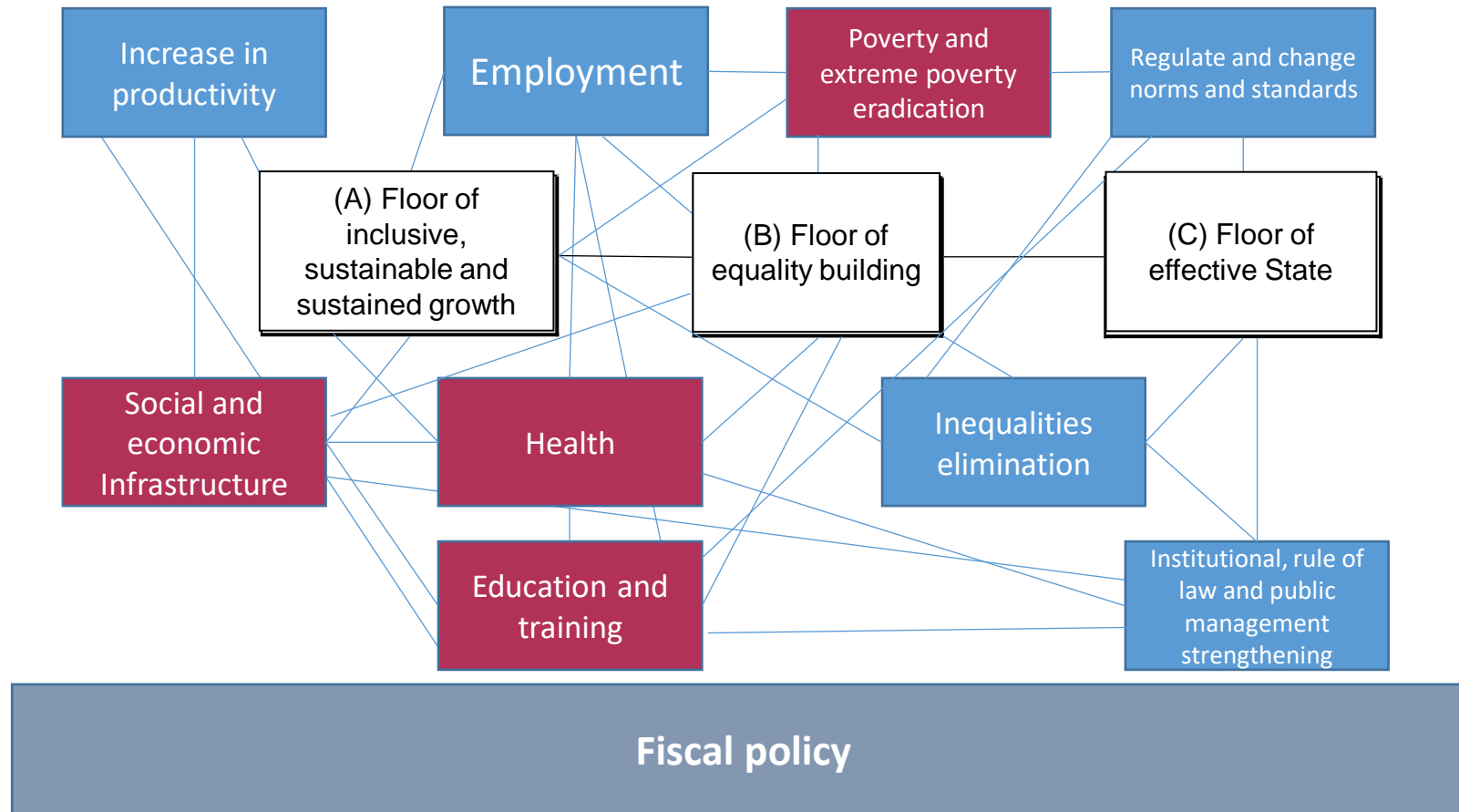
I. Strengthen the role of the State

2. Extend the domestic market: reduce international dependence, increase employment and eradicate poverty

- 2.1. Guaranteed basic income in cash, at least for people in working-age, with the aim to increase aggregate demand and national and Central American productive supply
- 2.2. In two weeks, allow micro, small and medium enterprises (MSMEs) renegotiate loans accessing to softer conditions (grace periods, terms and interest rates)
- 2.3. Via loans and capitalization renegotiation support big corporation, as long as its existence is strategic due to formal jobs generation, technological level or adaptation capability to the new international economic conditions
- 2.4. Build and implement a regional economic policy which achieve more integration and take better advantage of the each Central American country own productive capabilities
- 2.5. Design and execute a plan to achieve in the medium term food sovereignty
- 2.6. Design and execute a plan to build the social and economic infrastructure required for a sustainable and sustained development
- 2.7. Use public resources to create a fund for innovation, to reduce the technological gap in the productive units of each country, and advance towards environmental sustainability
- 2.8. Design and execute a scholarships program for the working-age population training, based in sustainable and sustained growth strategies

II. Advance in the compliance of the 2030 Agenda for Sustainable Development

Study the lags that the COVID-19 crisis will generate and propose a roadmap for its compliance



II. Advance in the compliance of the 2030 Agenda for Sustainable Development

Concept	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua	Panama
Fight against extreme poverty	0.03%	0.11%	0.43%	1.13%	0.16%	0.03%
Education improvement	1.81%	2.01%	2.56%	1.45%	2.85%	1.00%
Health improvement	0.60%	0.99%	1.52%	1.68%	0.75%	0.42%
Social spending	2.44%	3.11%	4.52%	4.26%	3.76%	1.45%
Social and economic infrastructure improvement	4.36%	1.90%	1.29%	2.35%	2.76%	2.43%
Total	6.80%	5.01%	5.81%	6.61%	6.52%	3.88%

Source: Icefi (2020). III informe de política fiscal centroamericana

III. Better responsibilities sharing. A fiscal covenant for development and democratic consolidation (2020-2030)

1. On revenues

- 1.1. Propose a roadmap to advance in the make public revenues, tax and other, sufficient and sustainable to finance public spending
- 1.2. Approve an extraordinary business solidarity and social responsibility tax (2021-2030): increase the personal income tax bracket for income over USD 50,000 and the lucrative activities tax with utilities over USD 2 million
- 1.3. Reduce yearly and strongly tax evasion and elusion, especially in income and value added taxes
- 1.4. Reduce yearly and strongly smuggling
- 1.5. Evaluate at detail current tax expenditures and eliminate fiscal privileges ineffective in terms of job creation, higher wages and direct foreign investment attraction
- 1.6. No fiscal privileges approval during the following decade
- 1.7. Approve new taxes and increase tax rates for luxury consumption and second house purchases
- 1.8. Consider increase the income and value added taxes rates, together with mechanisms toward a globally progressive tax systems

III. Better responsibilities sharing. A fiscal covenant for development and democratic consolidation (2020-2030)

2. On public expenditures

- 2.1. In the short term, grant quick and timely access to information on public spending related to the COVID-19 crisis
- 2.2. Link public spending and investment with international and national targets and results (SDG 2030), and the objective of universalizing guarantees to economic, social and cultural rights
- 2.3. Evaluate and redesign public policies in order to contribute as much as possible to equality
- 2.5. Study the current fiscal rules and eliminate those that in the following decade may hinder the efforts to prevent a decline in wellbeing and development, proposing actions to keep fiscal and macroeconomic stability

III. Better responsibilities sharing. A fiscal covenant for development and democratic consolidation (2020-2030)

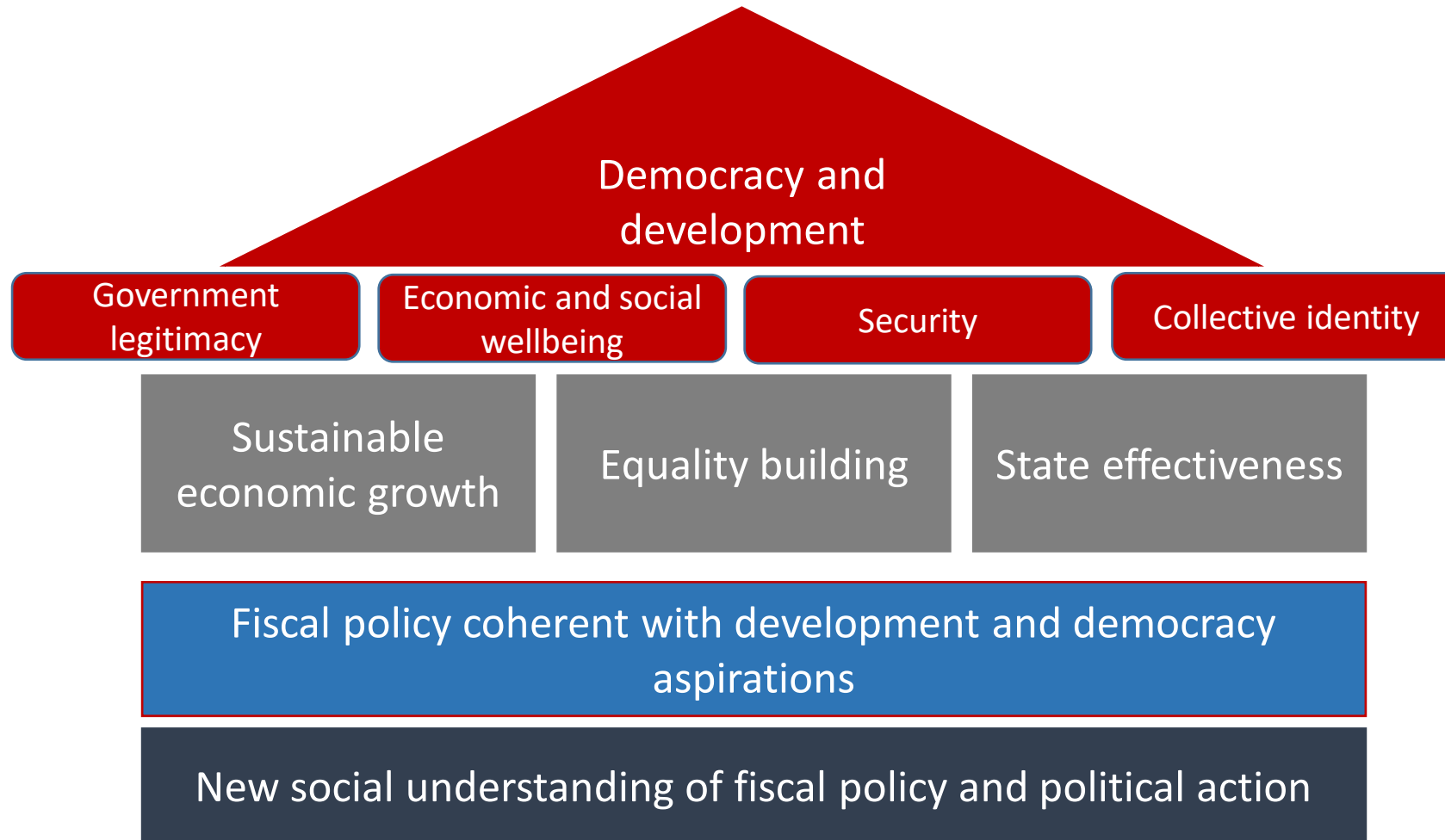
3. On public debt

- 3.1. Within the international debate, propose revising options for cancellation of debt with the international financial institutions
- 3.2. Renegotiate the conditions of the public debt held with private entities
- 3.3. Activate the existing legal and constitutional mechanisms that allow extraordinary financing for emergencies and catastrophes, including, when possible, the Central Bank direct lending to the Government

4. On transparency and fight against corruption

- 4.1. Make transparent and disclose the use of public resources, particularly those addressed to attend the COVID-19 crisis
- 4.2. Design, approve and execute, consistently with the social demands, national policies of transparency and probity
- 4.3. Reform the comptroller offices and close the identified spaces to corruption, especially in public works, public procurement and civil service.

Fiscal policy is the base of a new social contract



Source: Icefi (2020). III informe de política fiscal centroamericana

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