RIDGE 2020 Workshop on International Macro

The Real and Fiscal Aftermath of the Pandemic

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Globally, Decisive Response to the Pandemic…

- Fiscal response to COVID-19 (till September 2020, from *IMF Fiscal Monitor*): about **12 percent** of **world GDP**

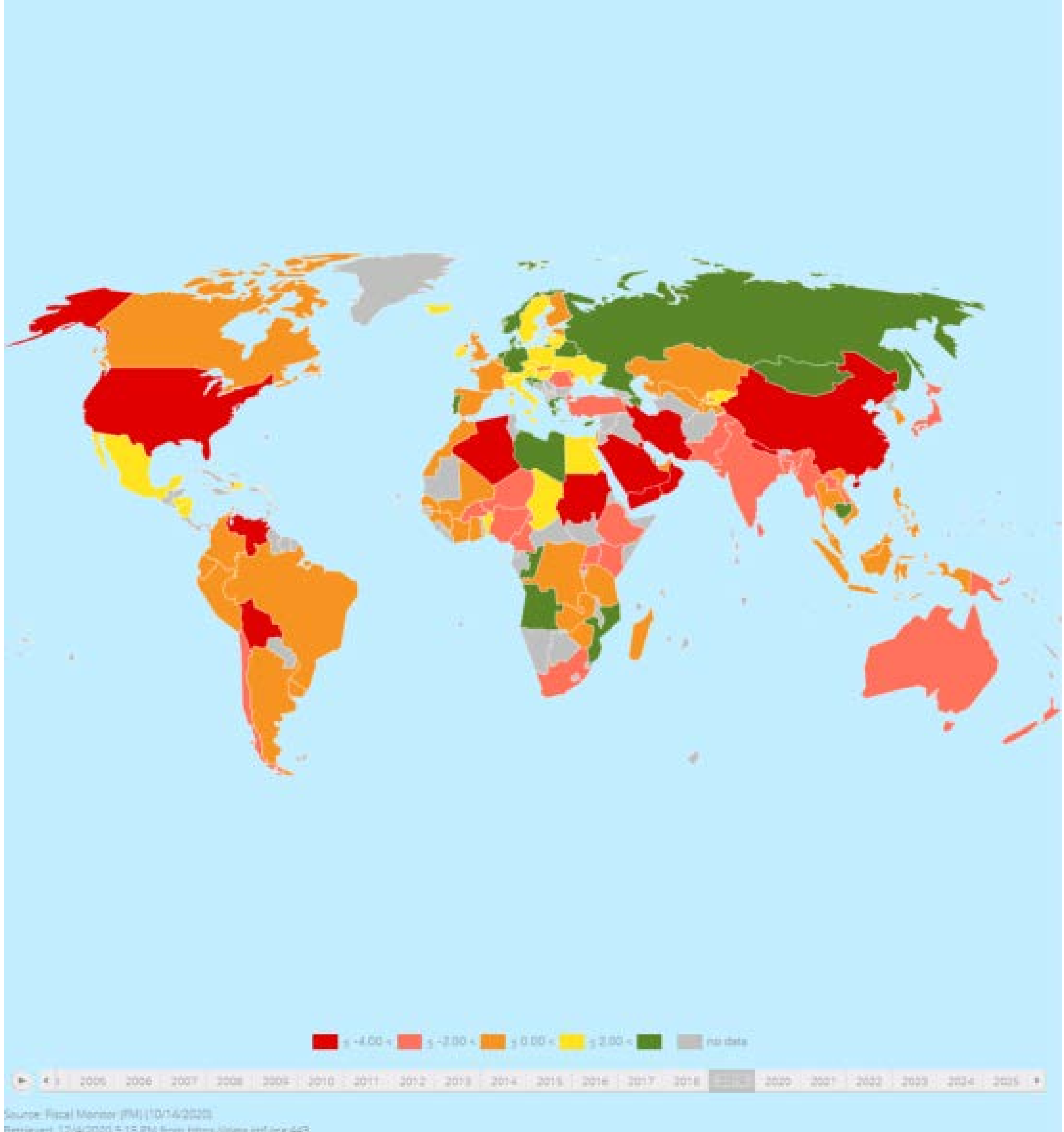
- Increase in government **deficits**: **9 percent** of GDP

- "Global **public debt** projected to approach 100 percent of GDP, a record high"

…but marked heterogeneity

- **Advanced countries** enacted **larger** fiscal programs than **emerging economies**

- Notable differences **across emerging countries**



Primary **Fiscal Deficits**, **2019** (Percentage of GDP_
<u>Source</u>: IMF

Primary **Fiscal Deficits**, **2020** (Percentage of GDP)
Source: IMF

Primary Fiscal Surplus (% of GDP)

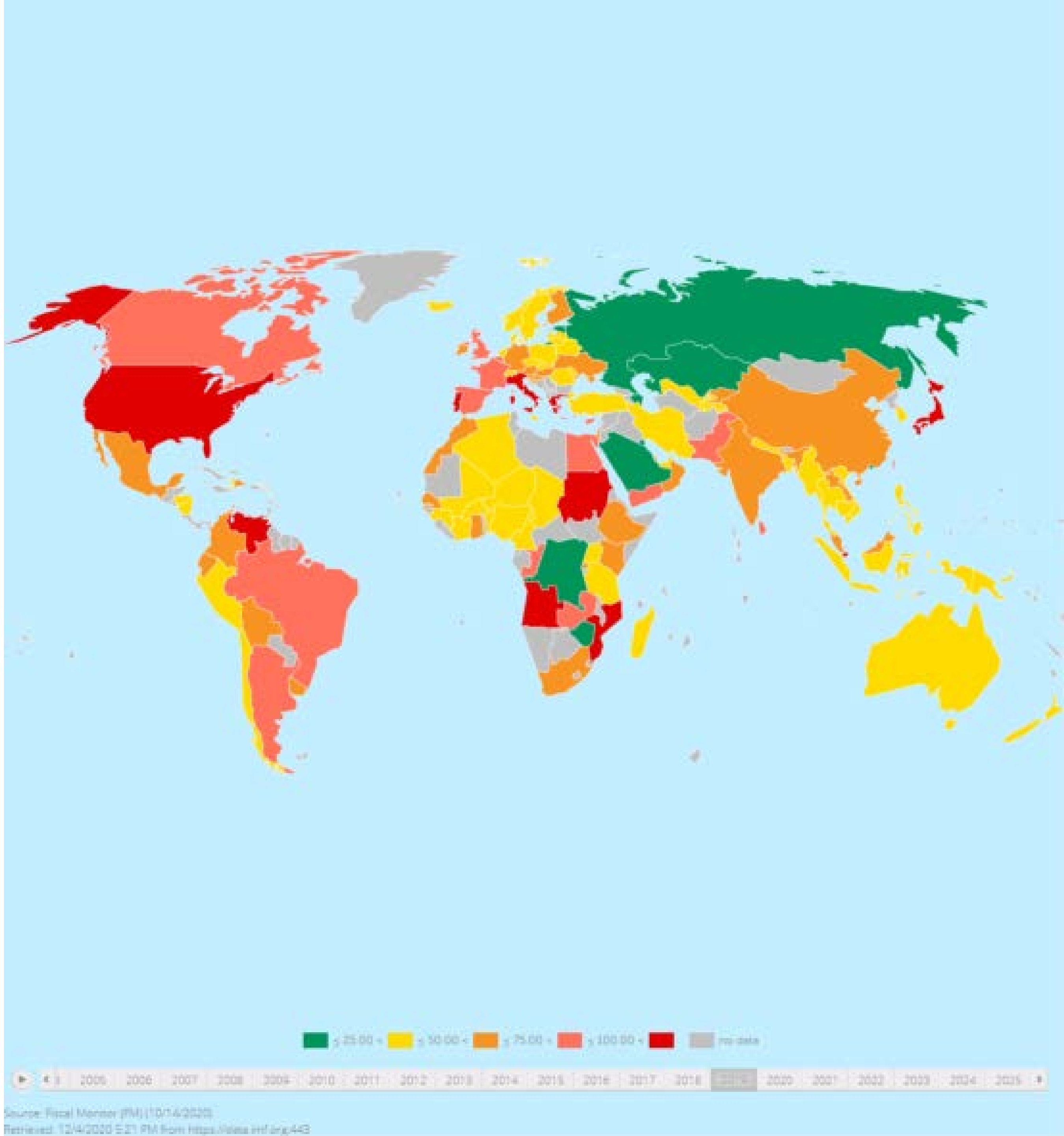
	2019	2020
G20	−4.0	−15.5
United States	−6.3	−18.7
Euro Area	−0.6	−10.1
Emerging Economies	−4.9	−10.7
Middle-income Latin America	−4.1	−11.1

Source: IMF

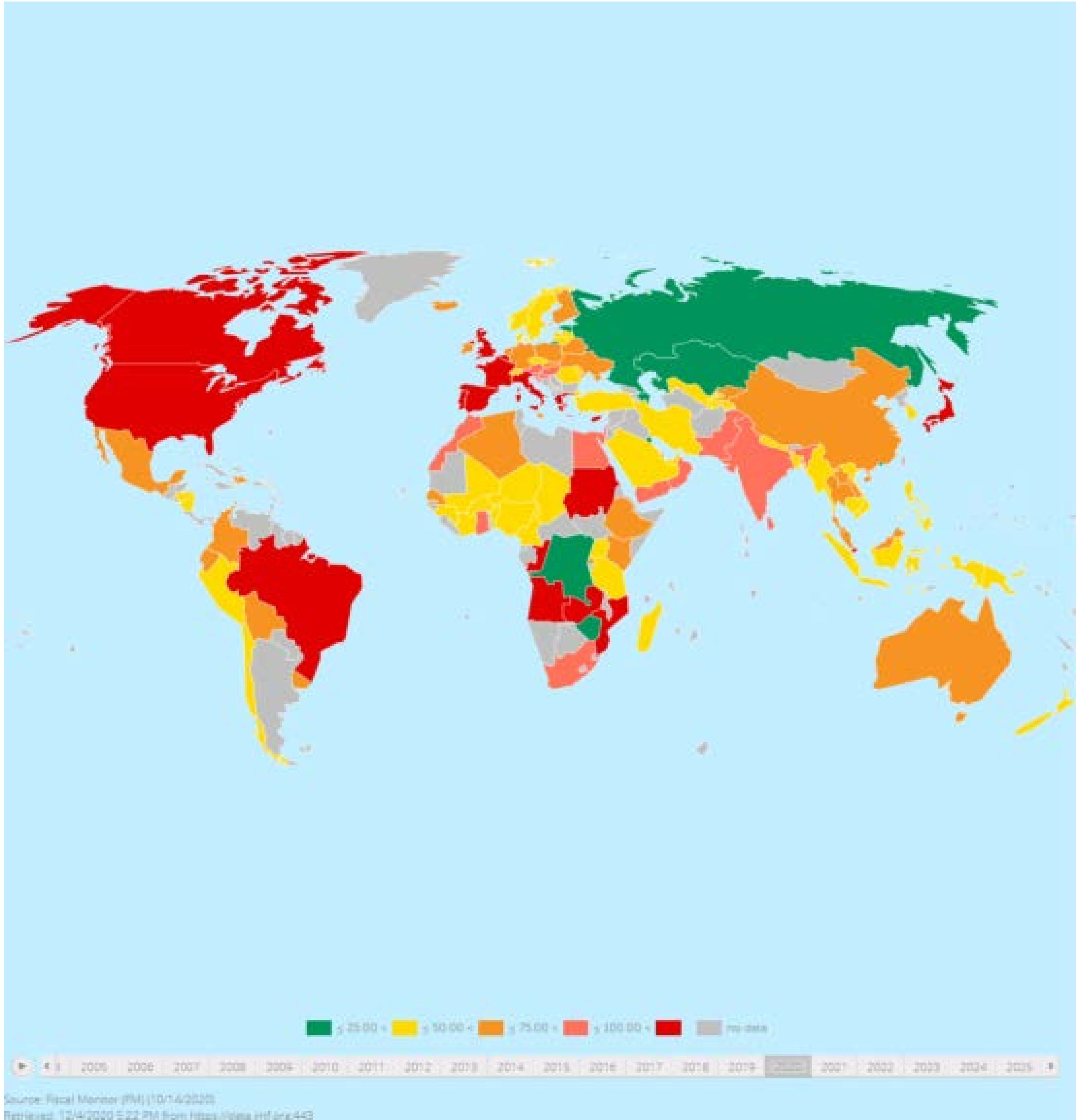
Primary Fiscal Surplus (% of GDP), Selected Latin American Countries

	2019	2020
Brazil	−6.0	−16.8
Chile	−2.6	−8.7
Colombia	−2.5	−9.5
Mexico	−2.3	−5.8
Peru	−1.4	−9.4
Uruguay	−3.0	−5.8

Source: IMF



Public **Debt**, 2019
(Percentage of GDP)
<u>Source</u>: IMF



Public **Debt**, 2020
(Percentage of GDP)
<u>Source</u>: IMF

Public Debt (% of GDP)

	2019	2020
G20	113.2	135.0
United States	108.7	131.2
Euro Area	84.0	101.1
Emerging Economies	52.6	62.2
Middle-income Latin America	70.8	81.6

Source: IMF

Public Debt (% of GDP), Selected Latin American Countries

	2019	2020
Brazil	89.5	101.4
Chile	27.9	32.8
Colombia	52.3	68.2
Mexico	53.7	65.5
Peru	27.1	39.5
Uruguay	65.9	69.5

Source: IMF

Implications

- Heterogeneity is clear

- Fiscal strategy should be country dependent

Looking Ahead: Key Considerations

- *r* versus g: Room for further borrowing?
- *r* versus g: Where to Spend It? Growth Prospects, Financial Fragility
- Focus on Institutional Change (Including the Central Bank)

r versus *g*: Low interest rates

- World *real* interest rates are expected to be about zero for several years
- Why not take advantage of virtually interest-free borrowing?
- (Those countries that can, that is)

Learn to Stop Worrying and Love Debt

Opinion

Learn to Stop Worrying and Love Debt

Why you should ignore the coming Republican deficit rants.

By Paul Krugman
Opinion Columnist

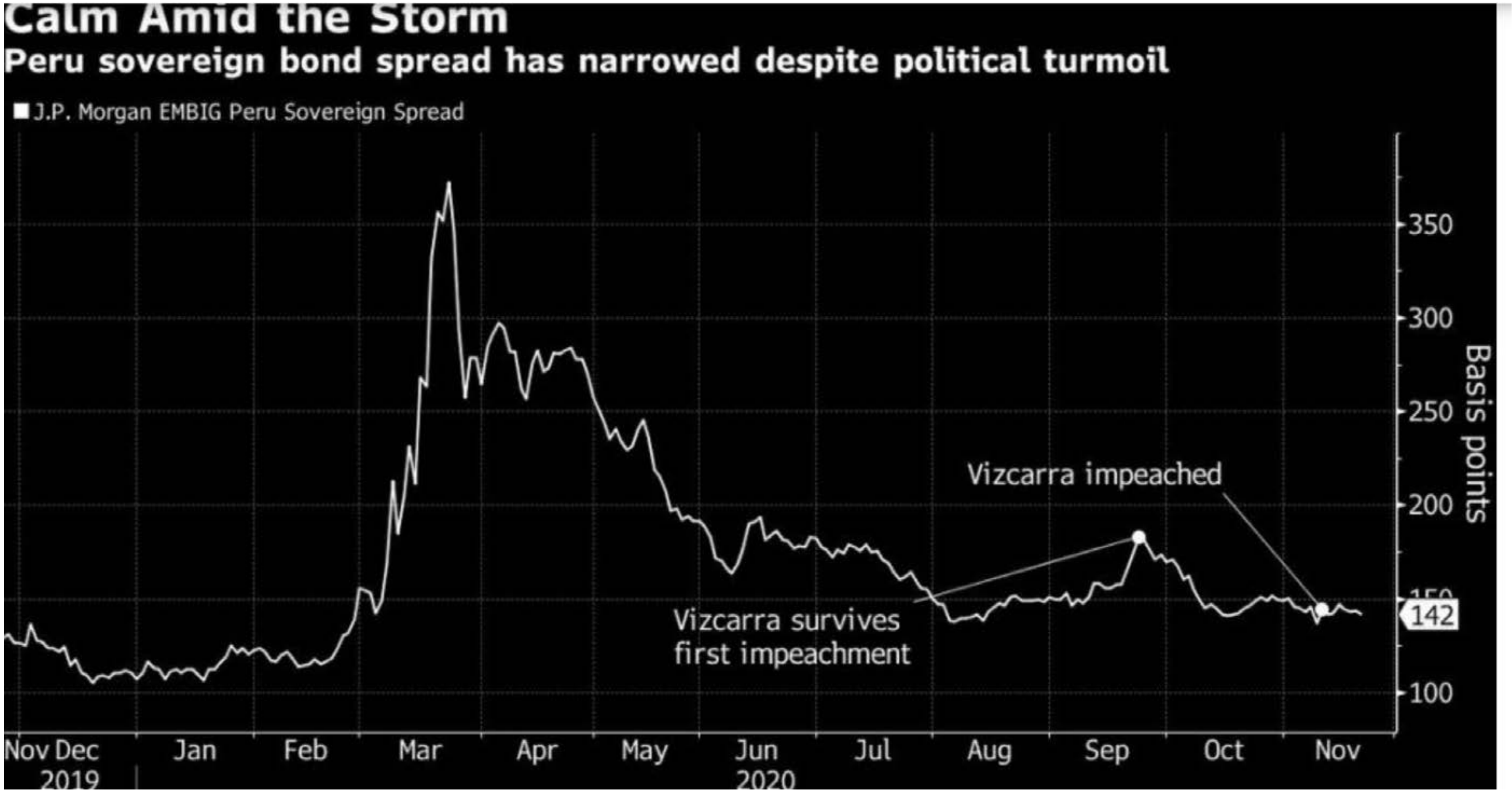
Dec. 3, 2020

Markets

Peru's 100-Year Bond Sale Shows Markets Can Defy Political Chaos

By Ben Bartenstein

November 23, 2020, 10:49 AM EST *Updated on November 24, 2020, 5:00 AM EST*



Source: JP Morgan via Yahoo! Finance

If One Can Borrow More, What For?

- Calls for “changing the world” policies have become commonplace
- For instance, proposals for a “Biden infrastructure shock” in US
- Or, from *IMF Fiscal Monitor:*

Policies for the new post-pandemic economy should focus on tackling poverty and inequality to ensure social peace and sustainable growth…Finally, reducing emissions will remain a core long-term challenge…This will call for policies to increase carbon prices and catalyze investment in low-carbon technologies

A Useful Focus?

- Emissions and climate change policies largely a matter of international cooperation

- *Tackling poverty and inequality to ensure social peace and sustainable growth* was a priority much before the pandemic: why should it be easier or different now?

- If anything, what the pandemic has underscored has been that (at least some of) our states suffer from much deeper deficiencies than we wanted to believe (e.g. Peru)

Fiscal Policy and AD Management

- A different argument: fiscal expenditures warranted because aggregate demand is likely to remain weak
- But not all crises are the same, nor are all recoveries
- The Covid crisis has been very different from others in the recent past
- In particular, the *financial sector* has shown surprising resilience
- *Asset prices* booming, and also *commodity prices*

Financial fragility and frictions

Serious pitfalls will *remain* when coming out of the Covid-19 crisis:

1. Temporary Liquidity Needs May Result in Bankruptcies and Job Losses with a Permanent Effect (See Céspedes, Chang, and Velasco 2020)

1. Corporates (and, in some cases, also households) surviving the worst of Covid (perhaps thanks to fiscal help) may arrive to the recovery phase with seriously impaired balance sheets

➔ Credit and Liquidity Support Programs May Need to be Extended Well Beyond the Pandemic

Where to Focus: Institutional Reforms

- Inclusiveness (Economic and Political)
- Reducing Informality
- Combating Corruption
- Redistribution
- Fiscal Institutions (including rules and architecture)

Central Banks as Quasi-Fiscal Agents

- Central banks in advanced countries, including the ECB, pledged to supply "whatever it takes" liquidity
- In emerging economies: not so much
- Key difference, perhaps due to the role of *international* liquidity
- Central bank credibility, reputation, independence, robustness matter
- Inflation Targeting 2.0?