DECEMBER 2020

FORESIGHT 2021

FUTURE FAST FORWARD | DEGLOBALISATION? NO, DIVERSIFICATION | THE RETURN OF THE STATE | DIGITAL HEALTH IN THE SPOTLIGHT

ISI Emerging Markets Group
EMIS CEIC

ISI Emerging Markets Group

EMIS CEIC

About ISI Emerging Markets Group

ISI Emerging Markets Group incorporates CEIC and EMIS, renowned globally as the leading providers of data, analysis and research for the world's fastest growing and highest potential countries. For over 25 years, our businesses have gone out of their way to gather the very best data and analysis available for emerging markets. We believe we have a unique model that relies on local expertise and relationships, a quality assurance process that is second to none and the implementation of leading technology to deliver information in the ways our customers need it.

In November 2020, Montagu Private Equity acquired ISI Emerging Markets Group from CITIC Capital Partners and Caixin Global. If you would like to find out more about how we can help you with your emerging market information needs, please visit www.isimarkets.com. For more information about our services: Macroeconomic data – access to unparalleled coverage of 195 economies around the world with a particular focus on emerging markets. Visit www.ceicdata.com. Company and industry information – data for over 4mn emerging market companies and detailed research and news analysis from the world's best information providers.
www.emis.com

Foresight

ISI Foresight 2021 is the latest in our series of annual reports, providing a forward-looking perspective on the key issues and developments that are likely to shape the prospects of emerging markets in the year ahead. We draw on past and current events to form expectations about the future. Within this report you will find contributions from each of EMIS and CEIC.

EDITORIAL TEAM

HEAD OF EDITORIAL
Slavina Damyanova

FORESIGHT EDITOR-IN-CHIEF
Gabriela Gandovska

DATA STORY EDITORS
Boryana Nedyalkova
Radina Koleva

EDITORS
Adriano Morais
Alexander Ivanov
Biliana Hristova
Georgi Ninov
Natalia Yanakieva
Nikoleta Slavcheva
Rohini Sanyal
Svetoslav Mladenov
Xintong (Olivia) Wu
Yinglei Li

SENIOR DESIGNER
Elena Gamalova

DESIGNER
Hristiana Inkyova

CONTACT
editorial@isimarkets.com

Contents

LETTER FROM THE EDITOR

Game Over, Game On

SLAVINA DAMYANOVA
Head of Editorial

Do you remember that exact moment when you realised that you are a witness to history in the making and that COVID-19 is the event that would define our generation? It wasn't only you, we all had it, at different times. At that exact moment the entire world seemed to stand still for a second.

And then it continued to turn, but everything was different. In a matter of minutes entire societies were down to basics – stocking on food, reconsidering household arrangements, health exposure and job security. Government officials came to the forefront and delivered much-debated announcements about policies, quoting metrics our life was now to be guided by. A ferocious, unknown and invisible common enemy has snuck up on us, upending our physical health, our psyche, our trust in our own government, our own communities. And while one would think a global pandemic would garner a global response and make it self-evident that we can and absolutely must act together to defeat the enemy with one blow once and for all, the reality that unfolded was a far cry from this.

The new circumstances triggered a fast and furious change of the business environment. All over the world contingency plans were being enacted and goals were being reevaluated. And on this global battlefield of words, data and opinions, employees became the foot soldiers of business resilience and social responsibility. Our experience at ISI did not differ much. Being in the data industry, we were pushed to the limits by the hectic demand for faster and more relevant data and research. While on many occasions state institutions struggled to deliver even traditional data timely, we had to focus on adding alternative data, scenario building, forecasting and nowcasting to our platforms to help our clients understand the processes that were underway in the world economies, keep pace with the dynamic environment, and take informed decisions. "Tell me what I need to know now, and give it to me quickly," one client in India told me back in June 2020 and for me that is the essence of the leap we had to make.

The human brain has the laudable capacity to adapt to any change, however dramatic it may be, as long as it becomes an accepted routine. As of the time I am writing this, it looks like the virus is here to stay for a while, but its health impact will, hopefully, become less dramatic as mass vaccinations are already under way. From here on, we need to adapt our businesses to the new circumstances, uniquely affected by the pandemic, and to continue being aware of the important social and governmental moves that may overnight have a defining impact on our markets. It is not only risks, but also opportunities that transpire in such turnaround periods and our Foresight 2021 aims to give you a look at them.

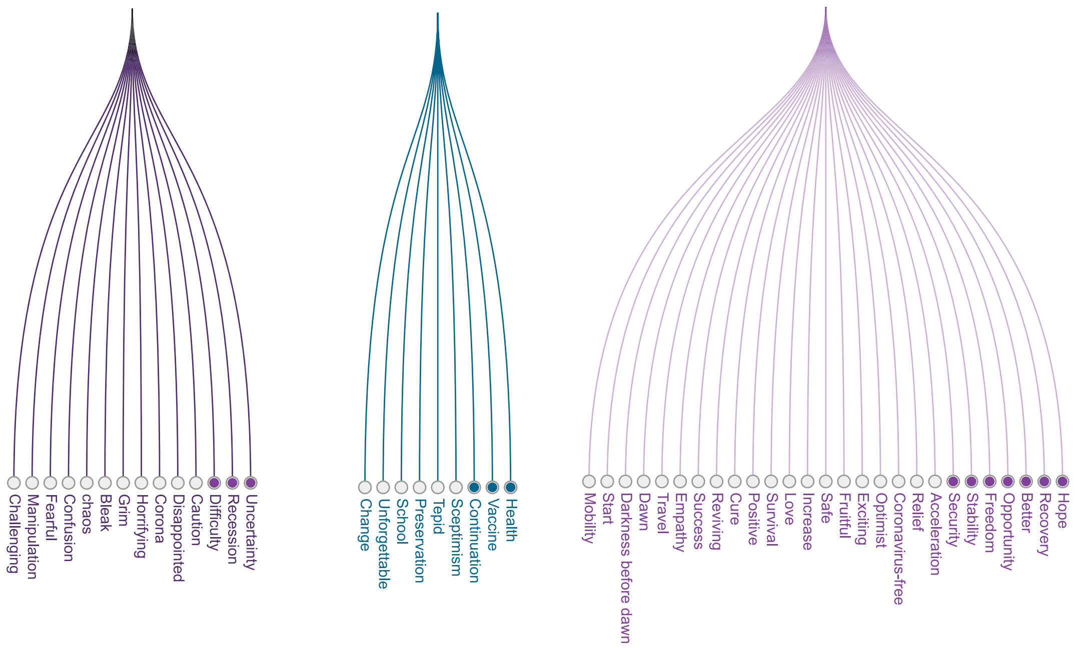
ISI FORESIGHT SURVEY

For this year's edition of our ISI Foresight report we conducted a special survey among our clients and the general public to gauge their expectations for 2021 - the year that many of us hope will see the end of the pandemic.

HOPE

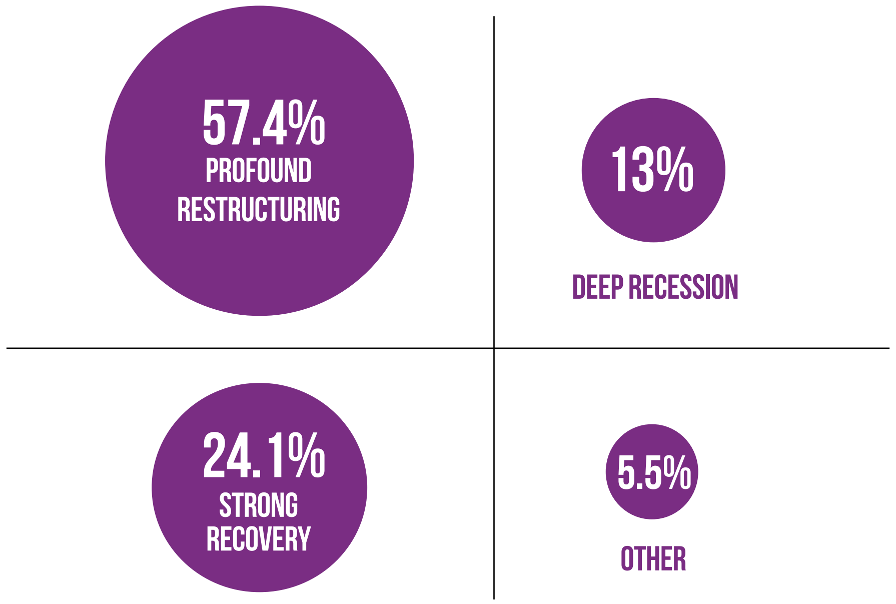
HOPE was the most frequent choice of respondents when we asked them to describe their expectations for 2021 with one word. Encouragingly, an optimistic view is shared by more than half of the interviewees and only a quarter are pessimistic.

IF YOU ARE TO DESCRIBE YOUR EXPECTATIONS OF 2021 WITH ONE WORD, WHICH ONE WOULD THAT BE?



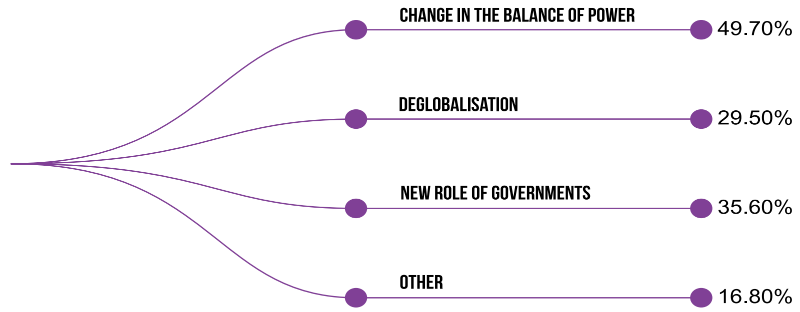
IN YOUR OPINION, 2021 WILL BE A YEAR OF...

Two out of three respondents believe that 2021 will be a year of profound restructuring, while every third said next year will see a strong recovery. Only a seventh of the interviewees expect a deep recession next year.

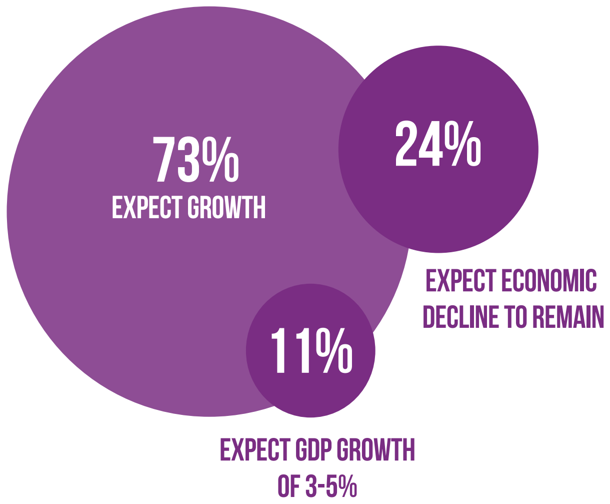


IN YOUR OPINION, WHICH OF THE LARGER ECONOMY CHANGES IN 2020 WILL BE HERE TO STAY IN 2021 AND BEYOND?

Half of the respondents expect changes in the global balance of powers in the post-pandemic world. More than a third believe governments will continue to play an increased role in the economy in the future, while a fifth say the pandemic has added momentum to the deglobalisation, a trend expected to gain further traction.

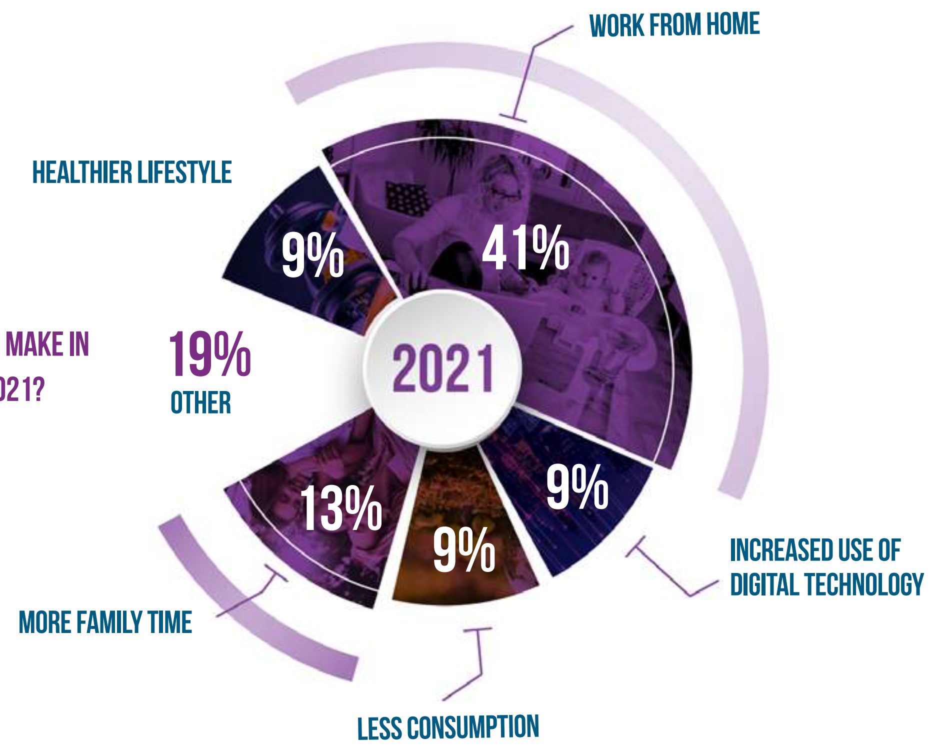


IF YOU ARE TO DESCRIBE YOUR EXPECTATIONS OF 2021 WITH ONE NUMBER, WHICH ONE WOULD THAT BE?



When we asked our clients to describe their expectations of 2021 with one number we received an overwhelmingly positive response with their anticipation for a global economic growth with an unexpected consensus forming around the 3%-5% range. The prognoses for their line of business were more divided as the pandemic has set apart completely new categories of industries, the resilient ones and those that suffer an immediate or delayed impact, as many forecast that the number of infected cases will approach 100mn in 2021.

WHICH OF THE CHANGES YOU HAD TO MAKE IN 2020 WOULD YOU LIKE TO KEEP IN 2021?



Editorial Voice

WINNING THE WAR

ALEXANDER IVANOV

Head of
Macroeconomic Research

It was time for the next recession. Even before COVID-19, economic growth was slowing down and the yield curve was reversed. Central banks had already tightened monetary policy and virtually all leading indicators signalled a looming downturn. However, the labour market was robust, inflation and inflation expectations were not much lower compared to the average levels during the whole expansion period, capacity utilisation was at normal rates, and there was no evidence that the global economy was overheating. It was more about expectations. Since 1857, when the US National Bureau of Economic Research (NBER) started to define the business cycle reference dates, the average length of expansion periods, from trough to peak, was 41.4 months. The expansion period that ended in February 2020, according to the NBER methodology, lasted 128 months, the longest one ever. And it was time to end. But the trigger that ended the period of expansion was far from what we expected.

ECONOMIC GROWTH WAS ALREADY SLOWING BEFORE COVID-19

The business cycle has been an integral element of the modern economic history since the Industrial Revolution. Periods of contraction were preceded by expansions with a relatively stable and predictable periodicity and duration. The cycle stages were mostly associated with the cyclical behaviour of the economic agents - households and companies. To a great extent, the business cycle stages have been determining the development of economic thought since then. The Great Depression in the 1930s gave birth to the Keynesian theory and the pivotal role of government spending to maintain aggregate demand, which was then replaced by the monetarist interpretation of the "great contraction". The oil price shocks in the early 1980s marked the beginning of the supply-side economics – the dominant paradigm until recently that has led to what we know today as the "Great Moderation" era. The orthodox economic thought during that era was driven by the belief that inflation is the biggest threat to economic stability, that governments should balance their budgets and keep the deficit low, that public investments crowd out private ones, and that central banks have the exclusive power and responsibility to manage the business cycle. The government role existed, but it was limited and more supplementary to that of the central banks.

This prevailing economic policy was not born out of ideology as some critics argued. Rather, it was a response to the economic reality and circumstances in that period. The business cycle stages were driven by the debt cycles that were propelled by the monetary policy actions of the central banks. Low interest rates boosted demand for credits and investment thus driving the economic boom. The boom led to economic overheating and rising inflation, so central banks had to act by tightening the monetary policy, which ended the expansion and turned the economy into a contraction that lasted until the central bank lowered the interest rates again and thus reversed the cycle. By doing so, central banks were meeting their main, and in some cases like the European Central Bank their only, mandate to keep the price stability. But the period of high inflation is over.

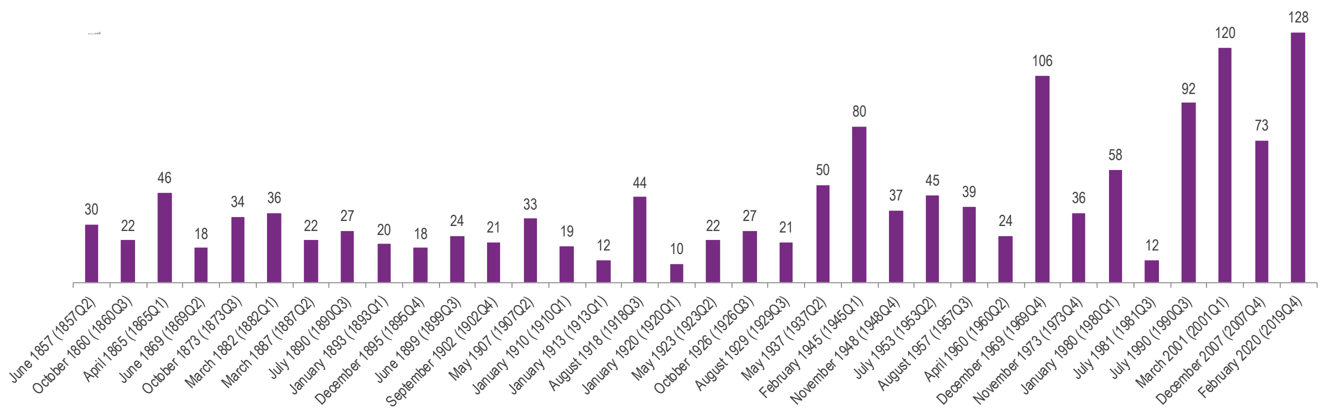
INFLATION IN DEVELOPED COUNTRIES HAS BEEN BELOW CENTRAL BANK TARGETS IN THE PAST DECADE

BUSINESS CYCLES HAVE INFLUENCED ECONOMIC THOUGHT SINCE THE INDUSTRIAL REVOLUTION

Over the last decade inflation in developed countries has been constantly below the central bank targets, even in the period of strong economic growth and historically low unemployment rates. Economic fundamentals and market expectations suggest that this trend is here to stay for at least a decade ahead.

41.4
MONTHS
AVERAGE LENGTH OF ECONOMIC EXPANSION PERIOD

US Expansion Periods, number of months from trough to peak



Note: The X-axis reflects the peak months and quarters in brackets.
Source: US National Bureau of Economic Research (NBER)

A Different Crisis at a Different Time

The contraction in 2020 was a different one. The timing was in line with the modern history of the business cycles, but the trigger looked more like the ones of the pre-Industrial Revolution era when the economic cycle stages, and in particular contractions, were driven by external forces, mainly associated with wars and natural disasters like draughts, climate changes and... epidemics. The COVID-19 outbreak unleashed an economic meltdown unseen in modern economic history. We've had sudden economic stops before, but they were either local ones, or much softer than the lockdowns in 2020. And different crises require different approaches. The role of the central banks in mitigating the current crisis is not to be underestimated. By providing the necessary liquidity the central banks prevented the biggest risk – the sudden stop in the real economy that hit the financial sector did not loop back to the real economy. Thanks to the central banks' timely measures, credit flows were not disrupted, banks remained liquid and the financial markets recovered quickly. There was no panic in the air and even though the global economy was hit hard by the lockdowns, things would have been much worse if the central banks had failed to prevent a financial crash. But while the central banks' toolkit was strong enough to absorb the initial shock, their ability to boost the economic recovery after this crisis is limited. Central banks cannot provide vaccines or ensure safe workplaces and travels. They can support private investment in new projects, but they cannot replace it. Moreover, the central banks' ability to boost the real economy was already limited before the COVID-19 outbreak. Over the past two decades the demographic changes have permanently shifted the saving-investment balance in developed countries towards a substantial excess of savings over investment, which has pushed interest rates to the zero-lower bound and exhausted the central banks' strongest weapon to support the real economy - cutting interest rates. The central banks in the major emerging markets still have some room for effective monetary policy, but with the aging population, especially in China and Eastern Europe, private investment will not be able to absorb excess savings and the central banks, with interest rates stuck at the zero-lower bound, will not be able to support the real economy.

The central banks' toolkit to support the economy in a downturn cycle phase is exhausted. This has been the reality in developed markets in the past two decades and this will be the reality that the emerging economies will have to deal with for at least a generation ahead, if the demographic trends persist. With the limited power of central banks and monetary policy, fiscal policy remains the only force that can fix the economy.

GIVEN THE ALREADY LIMITED POWER OF MONETARY POLICY, FISCAL POLICY REMAINS THE TOOL TO FIX ECONOMY

NOW IS THE RIGHT TIME FOR AN ADEQUATE GOVERNMENT REACTION AND THIS IS A LESSON THAT CAN BE LEARNED FROM CHINA'S QUICK RECOVERY

In the absence of private investment and consumption, government spending is the only way to overcome the insufficient demand and restore economic confidence. Even companies that sit on piles of cash due to the strong wealth effect of the asset price gain would refrain from investing unless they see the government's readiness to support the overall economy. The massive public spending was the driver of the robust economic recovery after the global financial crisis and the recovery from the COVID-19 crisis would not come from anywhere else. It is even more obvious now than it was 12 years ago, because the negative impact on the real economy is much higher than it was back then. But the fiscal hawks are right – it is not only about the amount of government spending. It is about the quality and this could not be emphasized more.

IT IS NOT ONLY ABOUT THE SIZE OF GOVERNMENT SPENDING – IT IS ABOUT QUALITY TOO

Current expenditure, for example, would not only have limited economic impact beyond supporting the most vulnerable in the short term, but it would be politically impossible to cut it back to the previous levels when the crisis ends, which would result in growing structural deficits and a devastating negative effect on the fiscal positions, especially in emerging countries. On the other hand, an increase in capital expenditure would have exactly the opposite effect – it would have a much stronger and a more direct impact on economic recovery. Moreover, this expenditure can be cut back at a more limited social and political price when the crisis ends and it is no longer needed.

Time to Act

Now is the right time for governments to react properly and this is a lesson that can be learned from China's quick recovery. When the virus is under control and life goes back to normal, consumption cannot drive the recovery on its own. The services sector is the one that has been hit the hardest by the lockdown, so it is the rebound of the industrial sector that can speed up economic activity and such a rebound is impossible without government investment, strong enough to offset insufficient demand. Construction of new roads and bridges, modernisation of old airports, investments in healthcare, technology, energy, defence and education are where the money should flow. And debt should be the last thing to worry about now. Debt would be a problem for tomorrow.

Given the fact that the annual growth of the nominal GDP has been constantly exceeding the one-year interest rates in almost all of the developed and the major emerging economies, the debt surge that would pay for such investment may not be as big a problem in the future as it may seem now.

128 MONTHS
US Longest Expansion Period

CONSUMPTION CANNOT DRIVE RECOVERY ON ITS OWN

Theoretically, such an approach means a substantial shift back to the conventional Keynesian theory. And there is unprecedented consensus among policy-makers globally over the necessary action. The years when governments and international institutions were embracing austerity are long gone and now even the International Monetary Fund is calling for more generous fiscal stimulus. The macroeconomic science has always been a battlefield of different ideas. And it was not only science that has benefited from that, but the society as a whole. Sweet-water economists and their supply-side economics have played a vital role in economic history and they certainly will continue to do so in the future. But now is a time to get the economy back on track, save lives and prevent millions of people from falling into extreme poverty. To quote the World Bank's chief economist and a long-time austerity supporter, Carmen Reinhart, "first fight the war, then figure out how to pay for it". ISI

THE ECONOMY IN NUMBERS

FocusEconomics GDP Forecasts for 2020 and 2021 by Panelists

BRAZIL

3.4% Median Forecast for 2021

	2020	2021
Petros	-4.5	5.3
Kiel Institute	-5.9	4.8
Credit Suisse	-4.6	4.1
Itaú Unibanco	-4.1	4.0
Banco BV	-4.5	4.0
Goldman Sachs	-4.5	4.0
Julius Baer	-7.0	4.0
4E Consultoria	-4.4	3.9
ING	-4.8	3.9
DekaBank	-4.8	3.8
Banco MUFG Brasil S.A.	-4.6	3.7
Standard Chartered	-4.6	3.7
Société Générale	-4.7	3.7
Barclays Capital	-4.4	3.5
Commerzbank	-5.5	3.5
Credit Agricole	-5.1	3.4
Haitong	-4.5	3.4
Median	-4.7	3.4
Santander	-4.8	3.4
KBC	-5.1	3.3
LCA Consultores	-4.3	3.2
Euromonitor Int.	-6.5	3.2
Fitch Ratings	-5.0	3.2
HSBC	-4.2	3.2
S&P Global	-4.7	3.2
Torino Capital	-6.1	3.1
UBS	-4.5	3.0
Pezco Economics	-4.2	3.0
Citigroup Global Mkts	-5.8	3.0
BNP Paribas	-4.5	3.0
Scotiabank	-3.8	3.0
Tendências Consultoria Integrada	-5.6	2.9
JPMorgan	-4.7	2.6
Parallaxis Economia	-5.3	2.3

CHINA

8% Median Forecast for 2021

	2020	2021
Kiel Institute	2.0	9.7
Nomura	2.1	9.4
Julius Baer	1.7	9.2
DekaBank	2.0	9.1
Berenberg	2.7	9.0
Danske Bank	1.0	9.0
Scope Ratings	1.3	9.0
UniCredit	2.0	9.0
ANZ	2.1	8.8
Bank of China (HK)	2.1	8.6
Bank of East Asia	1.9	8.6
JPMorgan	2.0	8.6
Scotiabank	2.1	8.5
Euromonitor Int.	2.6	8.4
Citigroup Global Mkts	2.1	8.2
KBC	2.0	8.2
OCBC Bank	2.1	8.1
Median	2.0	8.0
BMO Capital Markets	2.0	8.0
Commerzbank	1.7	8.0
Nordea	1.5	8.0
Standard Chartered	2.1	8.0
Fitch Ratings	2.7	7.7
Société Générale	2.5	7.5
BNP Paribas	2.5	7.5
Eurobank	2.1	7.5
Hang Seng Bank	2.0	7.5
HSBC	2.4	7.5
UBS	2.1	7.5
Itaú Unibanco	2.3	7.5
Goldman Sachs	2.0	7.5
Credit Suisse	2.2	7.1
Emirates NBD	2.1	7.0
ING	1.7	7.0
S&P Global	2.1	6.9
Daiwa	1.8	6.5
NORD/LB	3.1	6.0
Pezco Economics	1.7	5.7
DBS Bank	2.0	5.6
BBVA Research	2.2	5.5
Shanghai Commercial Bank	1.5	5.0

Source: FocusEconomics, CEIC

INDIA

8.9% Median Forecast for 2021

	2020	2021
Kiel Institute	-10.6	16.1
Euromonitor Int.	-13.0	14.0
KBC	-8.4	14.0
Goldman Sachs	-10.3	13.0
Daiwa	-6.5	12.5
JPMorgan	-9.0	12.0
Fitch Ratings	-10.5	11.0
DekaBank	-8.0	10.8
CII	-9.5	10.6
Crisil	-9.0	10.0
S&P Global	-9.0	10.0
Standard Chartered	-8.0	10.0
UBS	-10.5	10.0
Nomura	-9.0	9.9
Julius Baer	-10.0	9.0
Citigroup Global Mkts	-8.0	8.9
Median (2021)	-9.0	8.9
Eurobank	-8.8	8.5
BBVA Research	-4.5	8.0
HSBC	-11.0	7.8
ING	-16.4	7.7
Société Générale	-8.6	7.6
DBS Bank	-10.5	7.5
ANZ	-10.1	7.2
Commerzbank	-4.4	7.1
Scotiabank	-8.0	7.0
United Overseas Bank	-7.0	6.3
Coface	-4.5	5.5
BNP Paribas	-11.4	3.6

EURO AREA

4.9% Median Forecast for 2021

	2020	2021
La Caixa	-8.2	6.6
TD Economics	-7.4	6.3
Scope Ratings	-8.5	5.8
Ifo Institut	-7.4	5.6
IHS	-7.4	5.6
ANZ	-7.9	5.5
Commerzbank	-6.5	5.5
Fitch Ratings	-9.0	5.5
Piraeus Bank	-8.5	5.5
Standard Chartered	-7.7	5.5
Danske Bank	-7.0	5.4
Goldman Sachs	-7.2	5.3
Scotiabank	-8.3	5.3
Kiel Institute	-7.1	5.3
UBS	-7.4	5.2
BNP Paribas	-8.0	5.2
United Overseas Bank	-8.0	5.2
Berenberg	-7.4	5.0
Eurobank	-8.0	5.0
Nomura	-6.6	5.0
Nordea	-8.0	5.0
Zürcher Kantonalbank	-7.4	5.0
Median (2021)	-7.5	4.9
Emirates NBD	-9.0	4.8
Julius Baer	-7.5	4.8
DekaBank	-7.1	4.7
FUNCAS	-7.5	4.7
JPMorgan	-7.3	4.7
NORD/LB	-7.8	4.7
Pezco Economics	-7.1	4.7
Euromonitor Int.	-9.3	4.6
Credit Suisse	-7.6	4.6
HSBC	-7.5	4.5
Citigroup Global Mkts	-7.3	4.4
Raiffeisen Research	-7.0	4.3
Berliner Sparkasse	-7.2	4.2
SEB	-7.6	4.0
DBS Bank	-8.0	4.0
Rexecode	-7.2	4.0
Société Générale	-6.8	3.9
DZ Bank	-7.4	3.8
Swedbank	-7.3	3.7
ADA Economics	-8.2	3.5
ING	-7.1	3.5
PBZ Croatia Osiguranje	-7.5	3.5
UniCredit	-7.4	3.0
KBC	-7.5	1.9

US

3.7% Median Forecast for 2021

	2020	2021
Goldman Sachs	-3.5	5.3
Danske Bank	-3.4	5.2
DBS Bank	-3.5	5.0
Citigroup Global Mkts	-3.6	4.9
DekaBank	-3.4	4.9
DZ Bank	-3.6	4.6
Commerzbank	-3.5	4.3
BNP Paribas	-4.2	4.2
Credit Suisse	-3.6	4.2
Pezco Economics	-4.9	4.2
Ifo Institut	-3.6	4.2
Fitch Ratings	-4.6	4.0
Actinver	-3.7	4.0
Eurobank	-5.0	4.0
KBC	-3.7	4.0
Scotiabank	-3.9	4.0
Desjardins Group	-3.5	4.0
Berenberg	-3.5	3.9
ING	-3.7	3.9
Kiel Institute	-4.1	3.8
BBVA Research	-4.6	3.8
Handelsbanken	-4.0	3.8
Median (2021)	-3.8	3.7
NORD/LB	-3.6	3.7
Nordea	-5.5	3.6
RBC Capital Markets	-3.6	3.6
SEB	-4.0	3.6
TD Economics	-3.5	3.6
Julius Baer	-3.7	3.5
CIBC World Markets	-3.7	3.4
Société Générale	-4.2	3.4
UBS	-3.6	3.3
JPMorgan	-3.6	3.3
Raiffeisen Research	-3.6	3.3
National Bank of Canada	-3.6	3.2
Euromonitor Int.	-4.0	3.2
HSBC	-4.1	3.1
IHS Markit	-3.6	3.1
Emirates NBD	-4.5	3.0
Swedbank	-3.9	3.0
Nomura	-3.6	2.8
ANZ	-4.5	2.5
Standard Chartered	-5.4	2.1
UniCredit	-3.8	1.8

01

Spotlight

01 Spotlight

FUTURE FAST FORWARD

NATALIA YANAKIEVA
Head of Industry Research

The COVID-19 pandemic is one of the toughest challenges humanity has yet faced, but it has also become the tipping point for the accelerated development of innovative technologies. Digitalisation itself is no news – its role in our lives has been growing steadily for quite some time now. What this slow paradigm shift needed was a big push to speed it along and that is what the COVID-19 outbreak did. During the pandemic, trends like the adoption of direct-to-consumer and direct-to-home approaches and the use of connected devices as our sole access to food, medical services, work, and loved ones, once again demonstrated the seemingly endless expandability of technologies. It is, of course, impossible to automate every aspect of life, but digitalisation played a vital role in many key activities during the pandemic. The services sector was the fastest to adapt to this new cyber environment, and while some of its segments thrive, others are bound to strive.

40%
Increase in mobile apps use globally in Q2 2020

From Virus to Virtual

When a large chunk of the active population shifted to home offices and teleworking, office furniture retailers had a blast. Yet, the growth of their sales was nothing compared to the boom in video conferencing and other work apps' popularity. Globally, there was a 40% y/y increase in the usage of mobile apps during the second quarter of 2020.

The first spike in the number of work app downloads was in February, when China announced a country-wide lockdown. The downloads of China's three most popular work apps - Alibaba's DingTalk, Tencent's WeChat Work and ByteDance's Lark - skyrocketed by 6,085%, 1,446% and 572% y/y, respectively, from January 22 to February 20, according to Sensor Tower data quoted by TechCrunch. With Tencent's WeChat being the most popular messaging and social media app in China, its video conferencing software Tencent Meeting saw a rise in its membership from 250,000 to 5mn in the first two months of the outbreak. AliBaba and Tencent also launched international versions of their software, named DingTalk and VooV, respectively.

Although it faced some restrictions in China and India, the Zoom app was one of the biggest global winners from the pandemic. Zoom was the most downloaded app in India between March 1 and April 10, app analytics firm App Annie data showed, as quoted by Inc42. Since then India has advised against using Zoom over concerns about the data privacy of users.

On another note, the rise of so many apps facilitating work from home is good news for hackers. The rushed shift from physical offices to remote working was bound to compromise security and data protection and in the future corporations are expected to invest more in online data safety - a sector that will also benefit from the pandemic, although with a delay.

Shopping Spree

The stay-at-home orders and the social distancing measures made retail platforms the go-to means for the purchase of essential and non-essential items, and also for ordering food from restaurants. The retail sector suffered a severe blow from the lockdowns that were imposed everywhere. Sensor Tower data on iOS app downloads showed that grocery delivery app downloads in China surged to 52% of all shopping app downloads in the week starting February 3, 2020, which is when the lockdown in the county was imposed, as opposed to 33% in the week staring January 13. Food delivery app downloads almost doubled to 27% from 15%. Unsurprisingly, there were no downloads of store loyalty apps once the lockdown started, while in mid-January they accounted for 36% of iOS app downloads.

Switching to online shopping was quite easy for China, where the SARS pandemic of 2003 kick-started the popularity of e-commerce. The most used platforms for online shopping currently are Meituan-Dianping, JD.com and Alibaba. Alibaba's grocery delivery app Fresh Hema reported 100,000 downloads in a day on February 8 versus an average of 29,000 per day in 2019.

SWITCHING TO ONLINE SHOPPING WAS QUITE EASY FOR CHINA

Although widely successful, online shopping in emerging markets has to overcome obstacles such as the digital divide, crashing websites due to suddenly increased traffic, and internet speed limitations. Still, major retailers expect the online shopping trend to stay. The Economic Times has reported that Amazon and Flipkart intend to lease, respectively, 2mn ft2 and 1mn ft2 of warehouse space in major cities across India for five years.

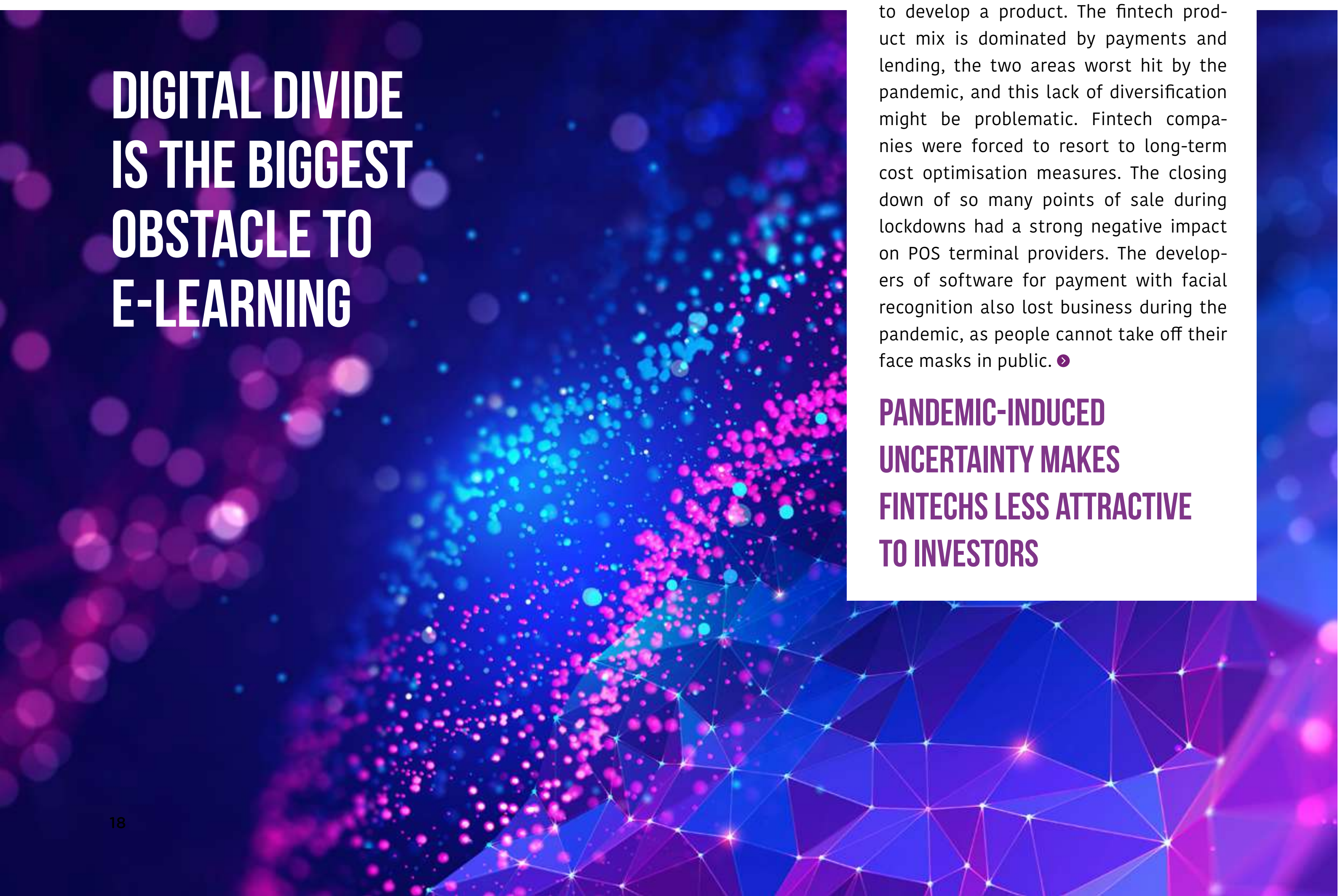
Learning Curve

Technology has already been playing an increasing part in the education sectors across emerging markets. Although the general consensus is that students should return to the classrooms the moment it becomes safe, it is to be expected that some changes will remain.

The biggest obstacle to e-learning in emerging markets is the digital divide. Socially vulnerable groups do not have readily available internet access and cannot afford the devices needed for online education. In rural areas electricity supply is also problematic. Edtech companies are working to solve the problem with internet speed, creating platforms that require minimal bandwidth and are web-based, meaning that users do not have to have personal devices or install software.

Tech companies have risen to the challenge of e-learning by providing a wide variety of solutions for all aspects of the process - online repositories for digital study materials, platforms for online teaching, remote proctoring, automated exam generation and assessments, real-time tracking of student performance, assignment and class schedule management. Emerging market governments have been very vocal in encouraging students to take advantage of the online educational resources. For example SWAYAM, the flagship online learning platform of the Indian government, provides over 1,900 open online courses with a credit transfer feature approved by 140 universities. The government also supports multiple online education channels, from primary to postgraduate levels, and virtual labs for science and engineering.

In China one of the biggest gainers from edtech is education and technology enterprise TAL, which has partnered with more than 300 public schools across the country and whose net revenues in the quarter ending August 2020 surged by 20.8% y/y to USD 1.103bn on a 65% hike in students enrolments.



DIGITAL DIVIDE IS THE BIGGEST OBSTACLE TO E-LEARNING

Coins and Clicks

The pandemic has revealed two opposing trends on emerging markets' fintech sector.

On the one hand, there is a growing customer acceptance of the use of digital services despite the poorer financial literacy and the digital divide. Another positive trend is the growing digitalisation of traditionally offline channels including shopping, gaming, entertainment, working, education, eating out, and payments towards the state budget. And third, those that still shop at stores increasingly prefer to make contactless payments.

On the negative side, people are more cautious about spending and borrowing, and that makes the fintech sector less attractive to investors. While banks have the financial strength to introduce changes, fintech companies are often start-ups that require upfront investment in order to develop a product. The fintech product mix is dominated by payments and lending, the two areas worst hit by the pandemic, and this lack of diversification might be problematic. Fintech companies were forced to resort to long-term cost optimisation measures. The closing down of so many points of sale during lockdowns had a strong negative impact on POS terminal providers. The developers of software for payment with facial recognition also lost business during the pandemic, as people cannot take off their face masks in public.

PANDEMIC-INDUCED UNCERTAINTY MAKES FINTECHS LESS ATTRACTIVE TO INVESTORS

Financial institutions had a tough time too. They were forced to urgently reconsider the type of services they offer and the channels through which these services are provided, and they also had to adjust their internal systems to this change in no time. Many of the financial institutions in emerging markets faced problems that are inherent to these markets, above all the low starting point in terms of technological advancement. They had no choice but to quickly catch up with the global developments in the fields of mobile and digital channels for supply of services, digital identity of the clients and automation of processes.

As of March 2020, India and China accounted for the highest fintech adoption rate in all emerging markets in the world. China and India ranked third and fourth in the world by number of fintech companies with 2,500 and 2,100 firms, respectively, Fintechnews reported. In Latin America, the leaders are Brazil with 600 companies and Mexico with 500.

In China the real time payment market is dominated by two major rivals, Ant Financial's AliPay (1bn users) and Tencent's Tenpay/WeChat Pay (800mn users), which together control about 90% of the market. The number of mobile electronic payments as reported by China's central bank increased by 23.3% y/y to 87.139bn in the first nine months of 2020, while their volume rose by 24.4% y/y to RMB 313.7tn. The growth rates in India are even more striking with the number of mobile payments surging by 79.8% y/y to 14.232bn and the volume growing by 33.7% y/y to INR 37.575tn.

2,500
Number of fintechs in China

A Video a Day Keeps the Doctor Away

As with many of other technological advancements, telemedicine is not something created because of COVID-19. Before the pandemic, telemedicine has been an alternative for providing better healthcare in less developed regions, where traditionally the doctor-to-patient ratio is very low, if a doctor is available at all. But the pandemic has also highlighted the advantages of having the option to get medical help from a distance, if self-treatment is possible. The advantages are plenty, ranging from relieving the stress on hospitals to avoiding the spread of the disease. As medical staff are urging the sick to seek help as they normally would, video consultations allow many to get that help remotely.

However, the lack of infrastructure and the poorer access to digital devices in remote areas in emerging markets are a problem. Also, the sector is still not very well regulated as it is very new and the current development push is too quick, leaving issues like data privacy open.

The only two emerging markets that can boast substantial progress in the field are China and India. China was already far ahead even before the coronavirus. The Chinese telehealth market is forecast to grow nine-fold to reach USD 54.2bn by 2025, UBS estimates in its report Future of Humans published in September 2020. In 2023, the Chinese telehealth market will even get ahead of the US market. Tencent's WeDoctor app reported having around 250,000 doctor registrations on its platform. Ping An Good Doctor, another popular telemedicine app, has 340mn registered users according to the most recent figures. During the coronavirus outbreak, these platforms and other giants such as JD Health offered free online consultations with growing popularity. Over the course of the pandemic so far the number of remote diagnosis and treatment service apps in China quadrupled to 600 and the number of newly-registered users on these platforms grew almost 10 times.

CHINA TELEHEALTH MARKET TO REACH USD 54.2BN BY 2025

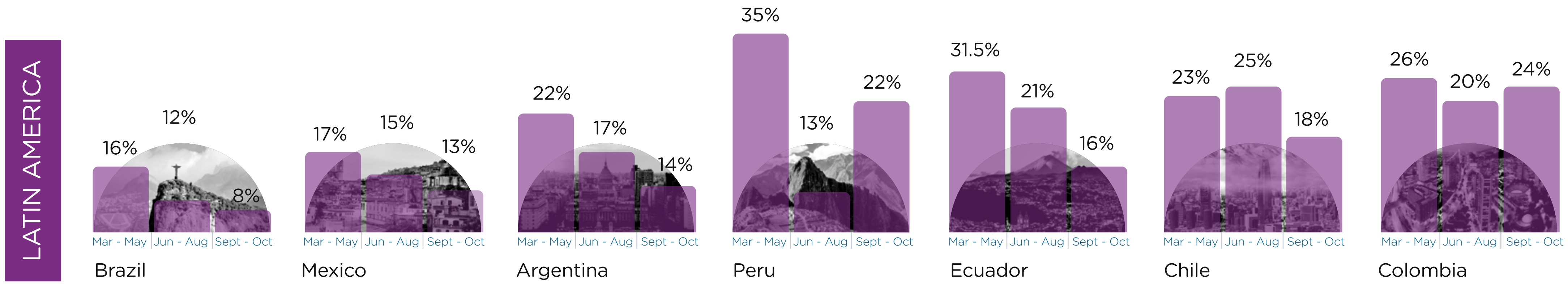
Indian digital health platform Practo saw a 50% increase in the number of doctors joining the platform in the period from March 24 to mid-April, the Economic Times reported. According to an EY-IPA study, the Indian telemedicine market will grow at a CAGR of 31% over 2020-2025 and reach USD 5.5bn in the final year of that period.

It was the best of times, it was the worst of times

There's no denying the huge impact that a massive crisis like a pandemic has on pushing novelties that were "nice to have" into the "need to have" category. The next in line for a digital revolution is manufacturing. Changes there take a bit longer to introduce as they often are capital-intensive and time-consuming. With digitalisation taking the lead in so many service sectors, there is no way manufacturing will be spared. Moreover, producers will have to deal with these challenges under tremendous pressure to be more environmentally friendly. With the world forced into a stand-still, we remembered what cleaner air and less traffic felt like, so there is no doubt that greener manufacturing will be demanded in the future. These past months, it turns out, were only the beginning of a very interesting story. ISI

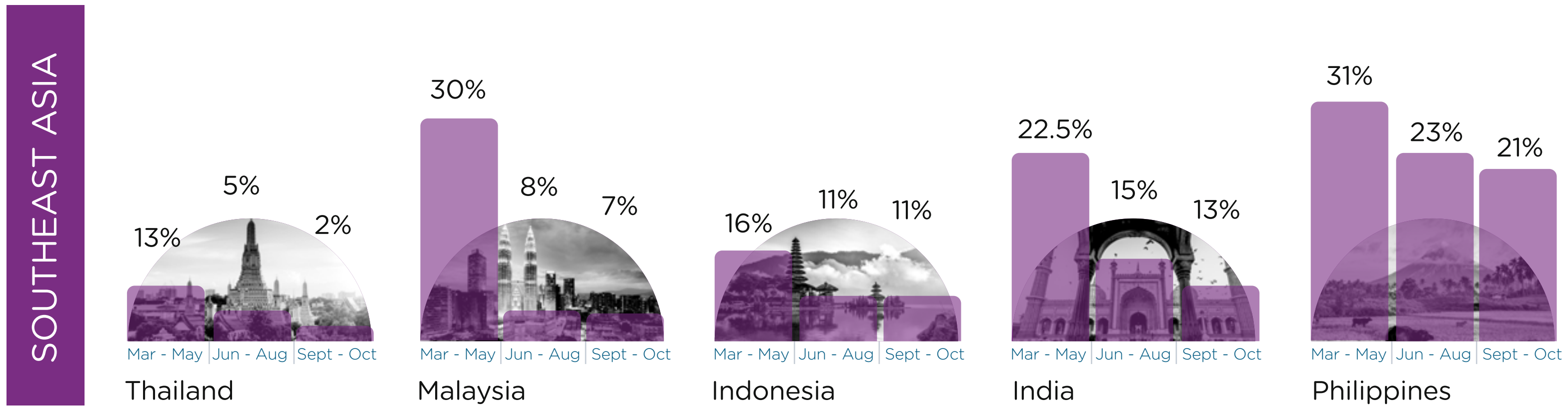
Change in the Duration of Time Spent at Home

No country in Latin America has been successful in containing the spread of COVID-19. Colombia, Chile, and Ecuador enforced some of the most effective nation-wide lockdowns, while only some states in Brazil imposed quarantine measures of different duration. Yet, the region has been hit hard by the pandemic, owing to long-standing economic weaknesses, inadequate wealth distribution, and poorly functioning healthcare systems.



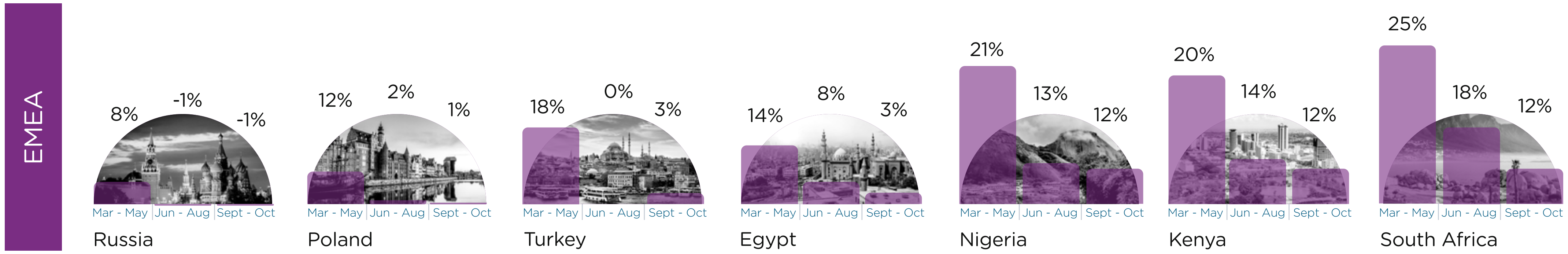
Source: Apple Inc, CEIC

TIME AT HOME



Source: Apple Inc, CEIC

Thailand and Malaysia lifted some of their movement restrictions in May and June 2020 respectively as the spread of COVID-19 looked under control. Thailand boasts one of the world's successes in handling the virus, reporting single-digit new cases per day at least since June 2020. The Philippines, in turn, enforced a nearly eight-month nation-wide lockdown, with limited success in containing the virus. India and Indonesia have also been facing difficulties in controlling their outbreaks.



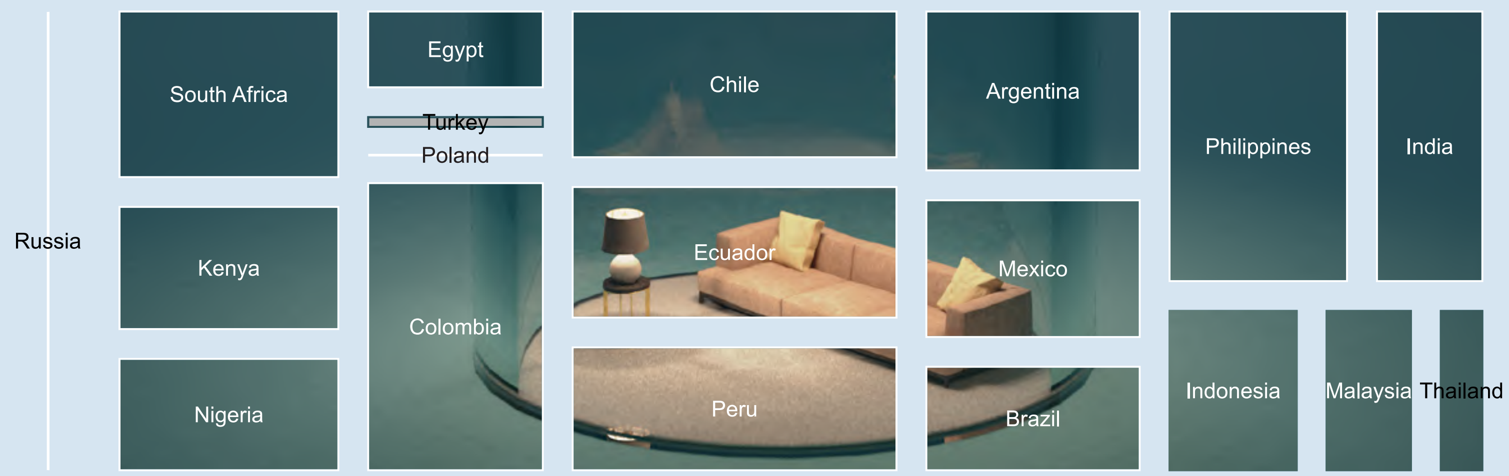
The percentages shown reflect the median values of work day-adjusted daily percentage changes in the duration of time spent at home compared to the corresponding day of the week during the five-week baseline period from January 3 to February 6, 2020.

Source: Apple Inc, CEIC

Beyond the March-May period, Russia, Poland, and Turkey failed to enforce effective stay-at-home policies. The African countries, with the exception of South Africa, seem to have been more successful in controlling the spread of COVID-19, with substantially fewer confirmed cases reported, compared to Russia, Poland, and Turkey. Based on WHO data, Nigeria reported as few as 62,000 confirmed COVID-19 cases as of November 8, 2020, against a population of roughly 196mn. The virus seems to be raging in Russia, with 1.8mn confirmed cases as of November 8, 2020, against a population of 145mn.

The confinement enforced upon the employed in many nations gave birth to a stay-at-home economy propelled by digital solutions. The lockdowns undermined the financial prospects of fragile middle classes and pushed into poverty the informally employed, who are not cushioned by social benefits in many developing countries. While there is no correlation between home confinement and the successful control over the spread of the virus, working from home has acted as a catalyst, opening up possibilities to some industries, and closing doors to others. ISI

WHO STAYS AT HOME THE MOST



Source: Apple Inc, CEIC

01 Spotlight

DE-GLOBALISA-TION? NO, DIVERSIFICA-TION

If Donald Trump's trade policies felt like putting a spoke in the wheel of global supply chains, the COVID-19 pandemic was more like pulling the emergency break. Are we facing the downfall of supply chain globalisation or have the rumours of its death been greatly exaggerated?

GEORGI NINOV

Macroeconomic Researcher

Just a few years back nobody would have thought of this. The most fearsome adversaries of globalisation seemed to be the masked protesters at G7 events and the occasional populist politician promoting protectionism. And rightfully so. Globalising supply chains seemed like a no-brainer, not just for big players like Apple, Volkswagen or Walmart – even medium-sized companies were taking up the opportunity to move their operations away from home. The biggest allure of a globalised supply chain is undoubtedly the cost factor – companies would generally get a better deal on raw materials, transportation options and labour. But it also enables access to a wider market thus giving opportunities for a business to grow and develop. Politically, the trend was almost exclusively supported by governments, especially after China's opening to market economy principles in the late 1970s, its subsequent admission to the World Trade Organisation (WTO) in 2000, and the collapse of the Eastern bloc. Regional trade agreements (RTAs) facilitated globalisation immensely and according to WTO, as of September 2020, 306 RTAs were in force.

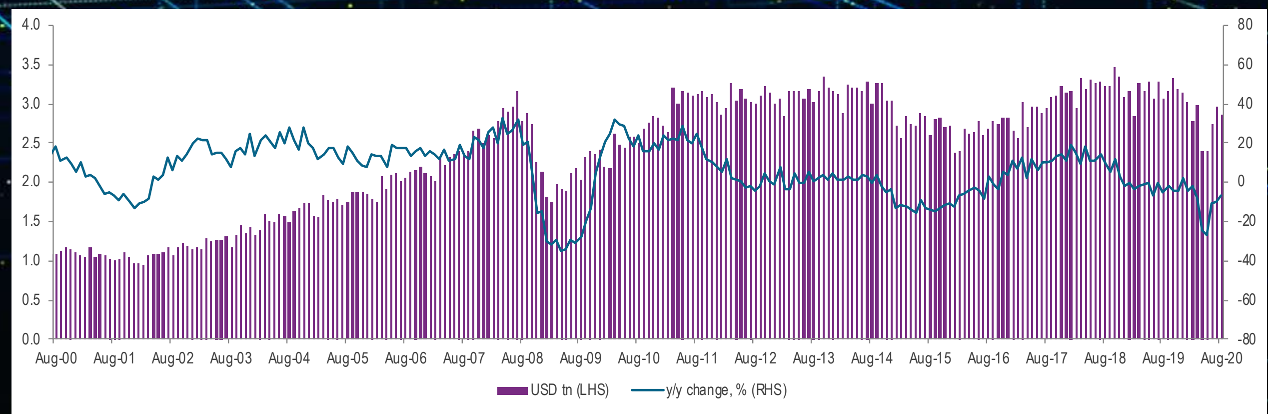
NOTHING LASTS FOREVER

So how did we end up here? While there were a few events in the past decade such as the Fukushima disaster in 2011 that highlighted the risks of increasingly co-dependent global supply chain networks, the first significant push towards de-globalisation came in 2016 with two notable events that marked the global political environment for the years to come – Brexit and Donald Trump's election to the US Presidency. It is safe to say that, up until then, the UK's retreat from arguably the globalisation's biggest success story – the European Union – had implications limited mainly to the parties involved. Trump's policies and the resulting US-China trade war, however, have been truly the first significant catalyst on the path to de-globalisation.

306

RTAs in force as of September 2020

Global Foreign Trade



Source: IMF

During 2019, the most intense year of the trade war, trade between the US and China fell by 15.6% y/y to its lowest level since 2012. Nevertheless, despite the fact that US trade deficit with China decreased in 2019, its overall trade deficit with the rest of the world did not change much – it amounted to USD 854.4bn compared to USD 872bn in the previous year, but was considerably lower in 2016 when Trump came to power, at USD 735.3bn. And while some US companies – most notably Apple and Walmart – did bring back home some of their production capacities, the more obvious effect of the tariffs was a relocation to other developing economies like Vietnam. In addition to this, the outcome for the US economy as a whole has been dubious to say the least – manufacturing production, already on a deceleration path, kept declining continuously between September 2019 and February 2020 and at the end of 2019 factory activity fell to its lowest level in 10 years. Such performance could hardly boost a worldwide shake-up of supply chains. Meanwhile, America's top economic rivals China and the EU were actively working in the opposing direction, championing themselves as free trade leaders and working on new RTAs such as RCEP or EU-Mercosur.

US-China Trade War Sets De-globalisation Trend in Motion

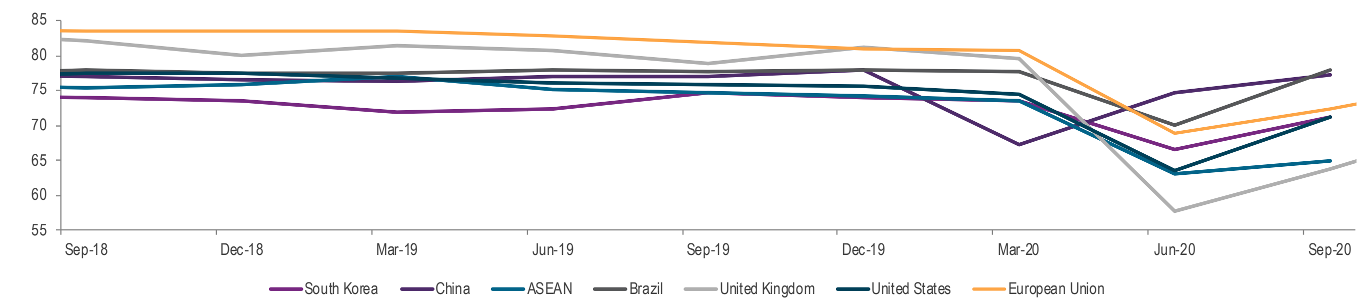
The de-globalisation trend that Trump's trade wars set in motion was accelerated by the COVID-19 pandemic, raising concerns whether global supply chains have been stretched too far. COVID-19 is reshaping the world in many ways and many say globalisation might be one victim of the pandemic. In a rather spectacular fashion, the coronavirus exposed critical weaknesses of the supply chain globalisation – starting from the lack of diversification.

For many years China was thought to be a safe haven for production – with cheap, abundant and qualified labour, excellent business ecosystem and accommodating regulatory framework. Moreover, despite the occasional political squabbles between world powers, the Chinese government's stability and continuity assured companies that everything would be going smoothly – seemingly forever. A pandemic of such scale, however, managed to destabilise even an economic giant such as China. Export bans and factory closures, albeit temporary, significantly rattled the manufacturing sector on a global scale. Naturally, the biggest victims are the automotive and electronics industries due to the complexity of their product processes. Motor vehicle production basically stalled in the immediate aftermath of the COVID-19's first wave in Q2 2020. US vehicle production declined by 69.7% y/y (and almost 99% in March) and according to data from the European Automobile Manufacturers Association, losses in the EU automobile market amounted to 1.2mn vehicles in March. Other sectors such as pharmaceuticals and various consumer products were also heavily affected. Overall manufacturing capacity utilisation dropped to 60.5% in the US in April, 63.3% in South Korea in May and 68.9% in the EU in the second quarter of 2020.

Easier Said than Done

Given the overall shock on the global manufacturing sector, it is not surprising that both companies and governments began to see the over-globalisation of supply chains as a significant threat to the well-being of their businesses and economies, respectively. In an uncommon unison, the two 2020 US presidential candidates Donald Trump and Joe Biden announced plans to curb supply chain vulnerability, with the then incumbent president Trump considering a USD 25bn reshoring fund to encourage more US companies to bring back their production home, while Biden pledged to do the same but also to build long-term resilient supply chains for the goods mostly needed in an extreme situation such as pharmaceuticals. In the meantime, in April Japan revealed a USD 2.2bn reshoring scheme, targeted specifically at its manufacturers in China. According to Nikkei, as of July, 87 companies have taken the offer, with 57 of them moving back to Japan and the others relocating to alternative hubs such as Vietnam and Laos. Even the EU, a champion of globalised trade by definition, has noted the dismal effect of the supply chain disruption and has called for diversification, although, for now, the primary target seems to be the pharmaceutical industry as part of the European Health Union initiative.

Capacity Utilisation, %



Source: National Statistics Offices, CEIC

Both Governments and Firms Call for Diversification

But while there are obvious reasons as to why a certain degree of de-globalisation might be a good idea, the question of how remains open. The first and most obvious issue lies in the extreme complexity of 21st century global supply chains – an intricate mechanism of logistics, subcontracts, company policies and regulatory frameworks at different stages of production – reminiscent of a game of jenga where pulling one element out threatens to crumble the whole structure. And if one thing is certain, it is that nobody – neither governments nor companies – want to see a collapse happening. Another major obstacle is the cost factor which could be considered as the fundamental reason why commercial globalisation happened in the first place. According to studies quoted by the Brookings foundation in August 2020, the trade war would cost the US economy USD 316bn by the end of the year and the US companies would lose USD 1.7tn in stock prices due to the tariffs imposed by the US. And the cost is not carried by producers alone – reshoring threatens to make end products more expensive for consumers as well. Making everybody poorer for a greater good would be an immensely difficult pitch to pass. Finally, replacing China might sound great on paper but there is a reason why the country is so attractive to corporations as a production hub. Finding and training new employees, at home or somewhere else, building new logistic networks for raw materials, moving whole management structures would be extremely costly and time consuming – two factors that make such a transition very difficult to implement.

The Future of Global Supply Chains

In spite of all the challenges to de-globalisation, the COVID-19 shock on the proper functioning of global supply chains is impossible to ignore. According to a global survey by Bolloré Logistics and Transport Intelligence published in the Logistics Manager magazine, 7 out of 10 supply chain professionals believe that the status quo of global supply chains has already been changed for good, while 6 out of 10 think that due to COVID-19 globalisation would be reconsidered as a business model. But if it is too costly to bring production back home and too risky to keep it in China, what should companies do? An answer to that could be the China Plus One strategy which is getting significant traction among multinationals. This strategy advocates for keeping part of the production in China and relocating the other part to other economies, especially in developing countries in Southeast Asia. The idea of shifting production out of China to other developing markets is not really new and was born out of purely practical reasons – labour costs in China have been increasing steadily in the past decade and tax incentives have diminished or expired. However, the COVID-19 pandemic seems to be the event that gave the necessary push in this direction.

Producers, Consumers to Both Bear the Costs of Potential Reshoring

Not surprisingly, the biggest beneficiaries from the China Plus One strategy are expected to be the MITI-V countries (Malaysia, India, Thailand, Indonesia and Vietnam), Mexico and South America, with Vietnam regarded as the economy most attractive to global companies due to the close proximity to China, cheap labour costs and stable political situation. Moreover, the country is a member of ASEAN and has a functioning trade agreement with the EU. Last, but not least, Vietnam is regarded as a success story in battling COVID-19, as only 1,300 cases and 35 deaths have been announced by its Ministry of Health as of November 18, 2020 – an impressive feat for a population of 96.5mn. Trade data also backs Vietnam's prosperity – it had the strongest export growth of all major regional economies in the period January-October 2020, at 4.9% y/y, with China and Taiwan being the only two other economies to record increases in the same period. And while foreign direct investment inflows were harmed by the pandemic, the 6% annual decrease in Q2 2020 was less pronounced than that of local competitors.

Although it would be naïve to believe that China would be happy with a mass exodus of foreign producers, the world's most populous country has shown a certain restraint in fighting this development – at least on the surface. This subdued behaviour could be explained with Beijing's own doubts about the future of globalisation. While the West seems preoccupied with analysing its own losses from the shocks on global supply chains, China has suffered considerably as well, despite the rather efficient tackling of the COVID-19 crisis within its own borders. Even though Beijing managed to contain the spread of the virus as early as in February and factories restarted activity around March, significant export growth returned as late as July and Q2 exports increased only by 0.6% y/y.

With global supply chains in a crisis situation proving as unreliable for China as for its trading partners, Beijing has started to look inward. In October 2020, the Chinese government announced its dual circulation strategy as the next phase of its economic development. Simply put, the country will concentrate on stimulating domestic consumption on equal footing as foreign trade. This strategy relies on tapping into China's enormous consumer base which has progressively become wealthier in the past decade – according to the National Bureau of Statistics, the average annual per capita wage in 2019 amounted to RMB 75,229 (USD 10,892), 64.7% higher compared to 2013. According to Reuters, the plan also includes increasing urbanisation among migrant workers to expand the Chinese middle class.

Nevertheless, China still does not seem to be eager to burn bridges and initialise protectionist policies. In November 2020, the Regional Comprehensive Economic Partnership (RCEP) was finally signed after nine years in the making. The RCEP is a free trade agreement in the Asia-Pacific region between China, Japan, South Korea, the 10 ASEAN members, Australia and New Zealand and is the world's biggest RTA. China's leading role in RCEP is hardly disputed – it is the biggest and most populous economy among the signatories and its influence was the reason India pulled out of the treaty in late 2019. And while RCEP might not stop the relocation of global supply chains, it could provide China with fresh new opportunities to explore. ISI

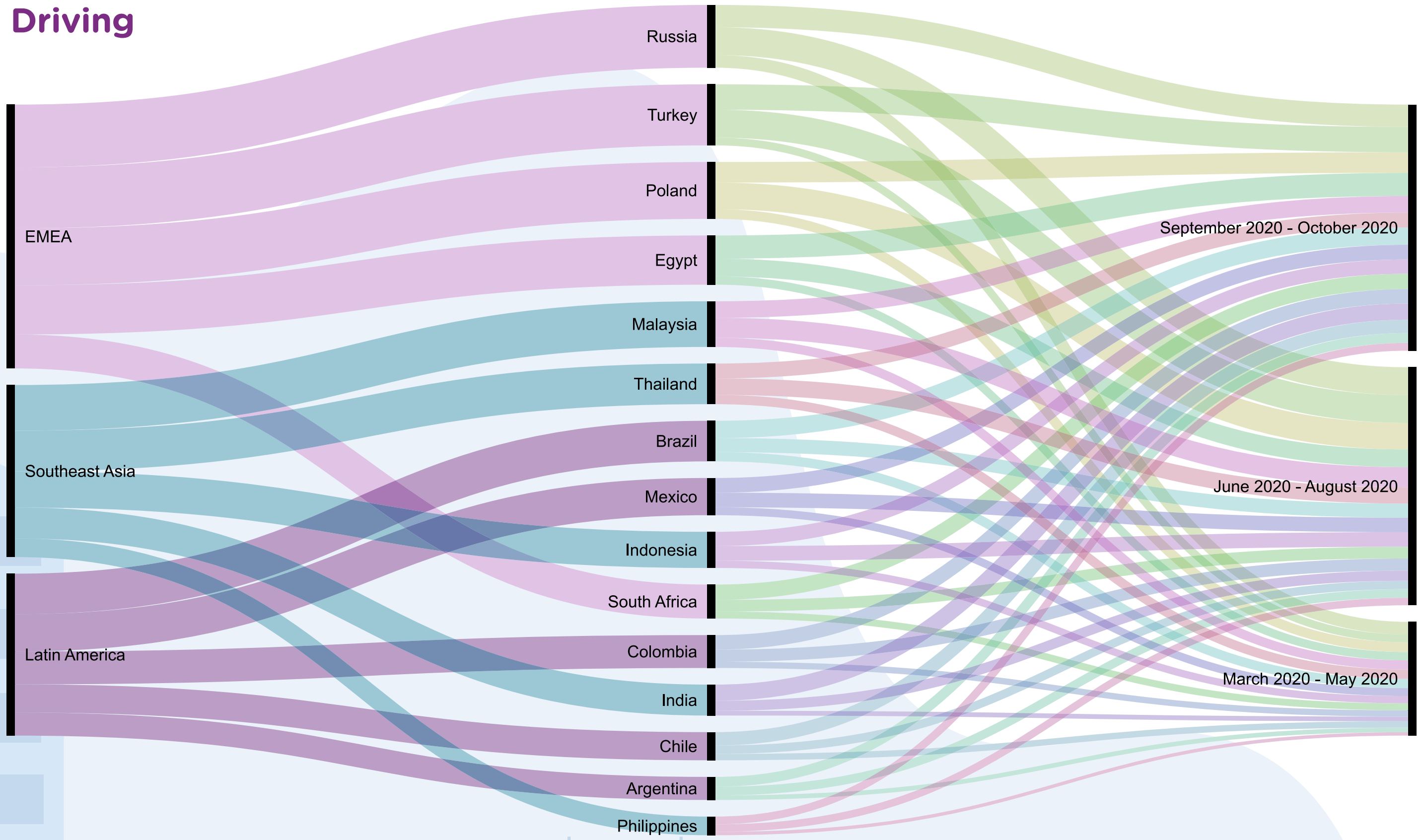
01 Spotlight

OUT INTO THE OPEN

DURING THE COVID-19 PANDEMIC

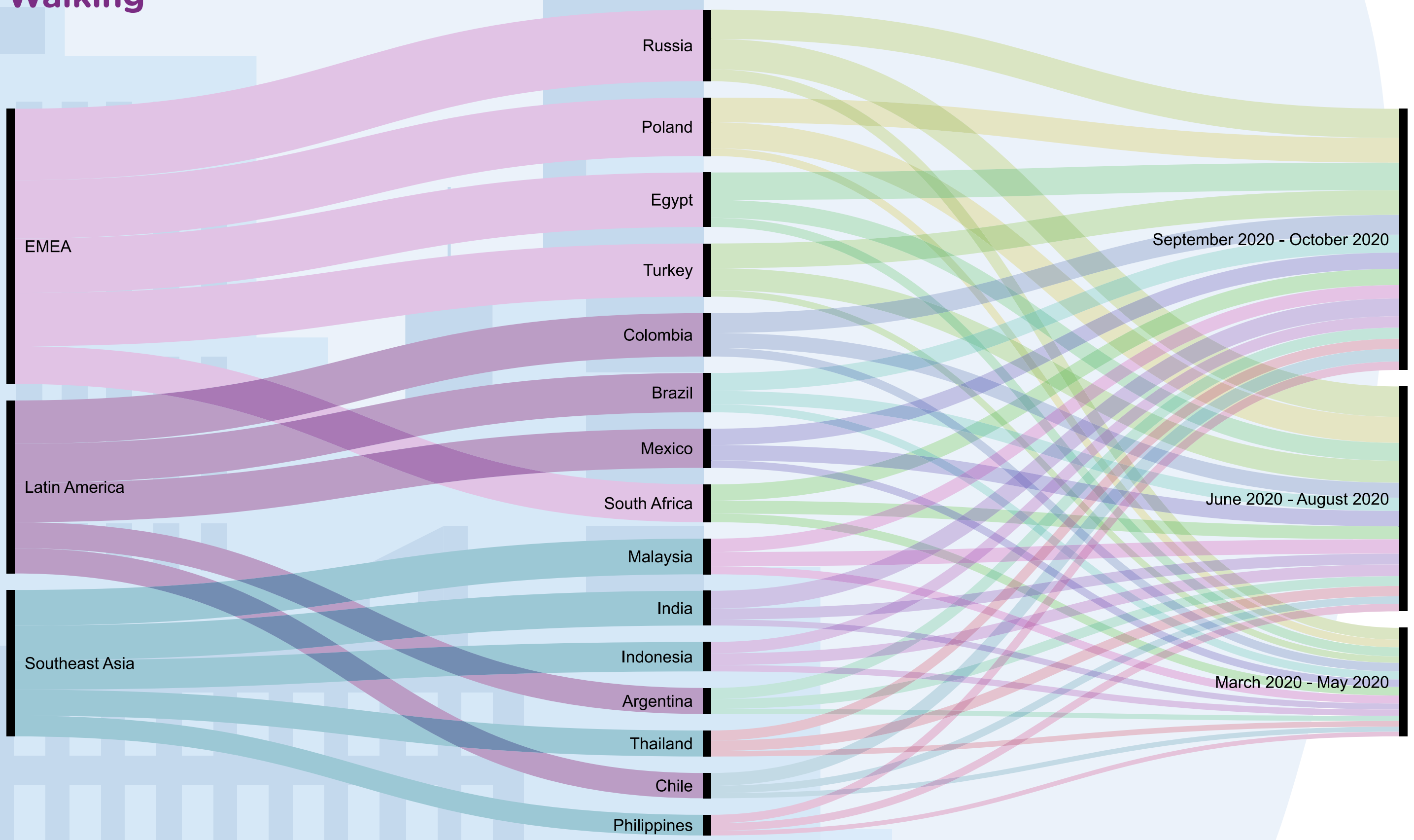
In March-May 2020 driving frequency saw a significant drop as a result of the lockdowns that were enforced across the globe. Once the restrictive measures were lifted, driving frequency rose. In the periods of the highest driving activity, most driving has taken place in EMEA countries (Russia, Turkey, Poland, and Egypt) and Malaysia and Thailand in Southeast Asia. In the European and Southeast Asian countries, most movement restrictions were lifted in May-June. South Africa, which ranks high in time spent at home, performs poorly in Driving but better in Walking, in line with movement restriction realities. The notoriously long lockdown of the Philippines has put the country at the bottom of Driving and Walking alike.

Driving



Source: Apple Inc, CEIC

Walking

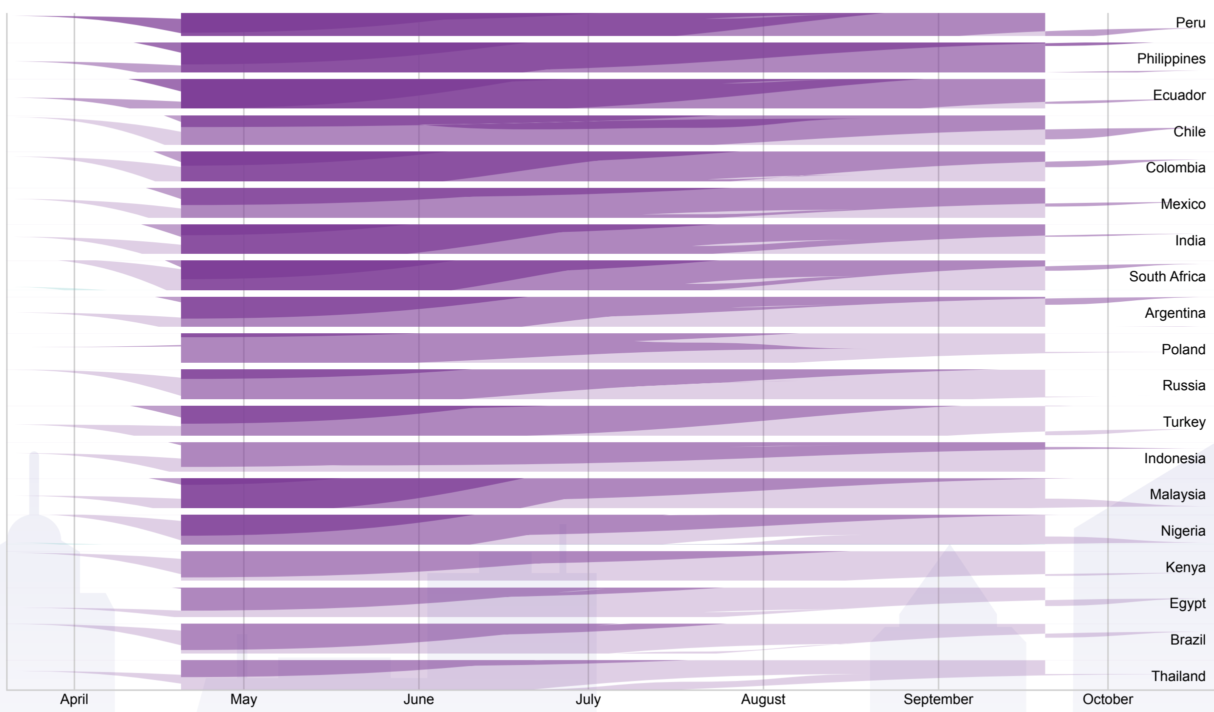


The datasets are compared to a baseline volume on January 13, 2020 to reflect a change in volume of pedestrians and drivers.

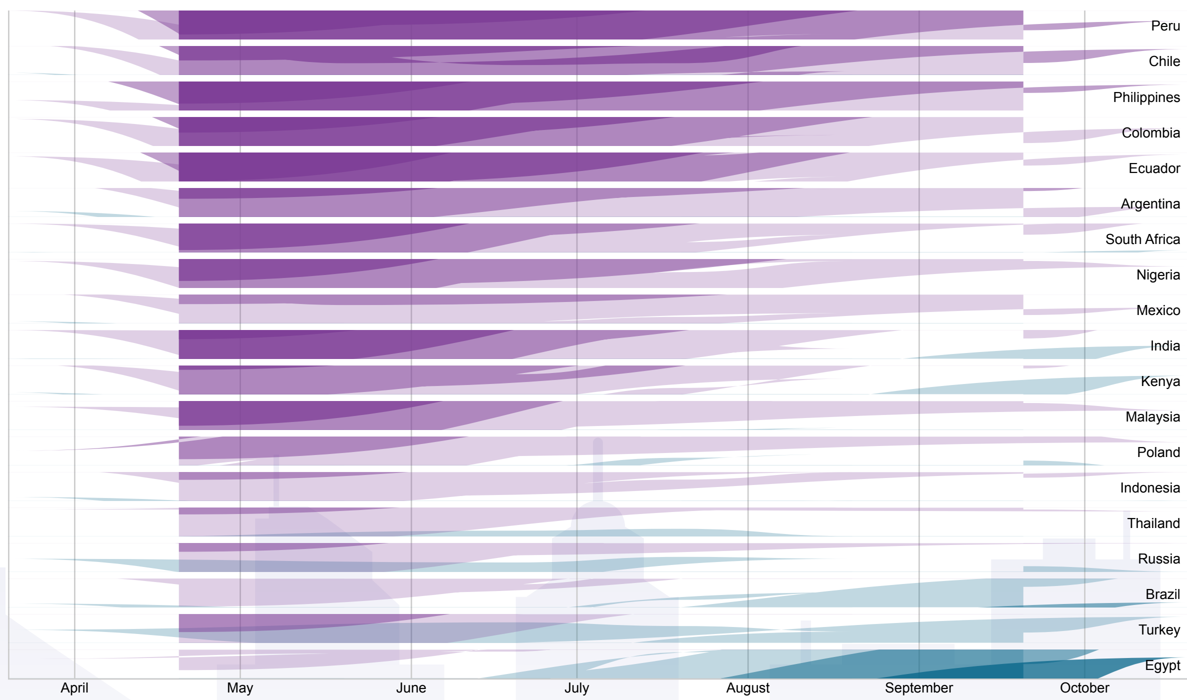
Source: Apple Inc, CEIC

01 Spotlight

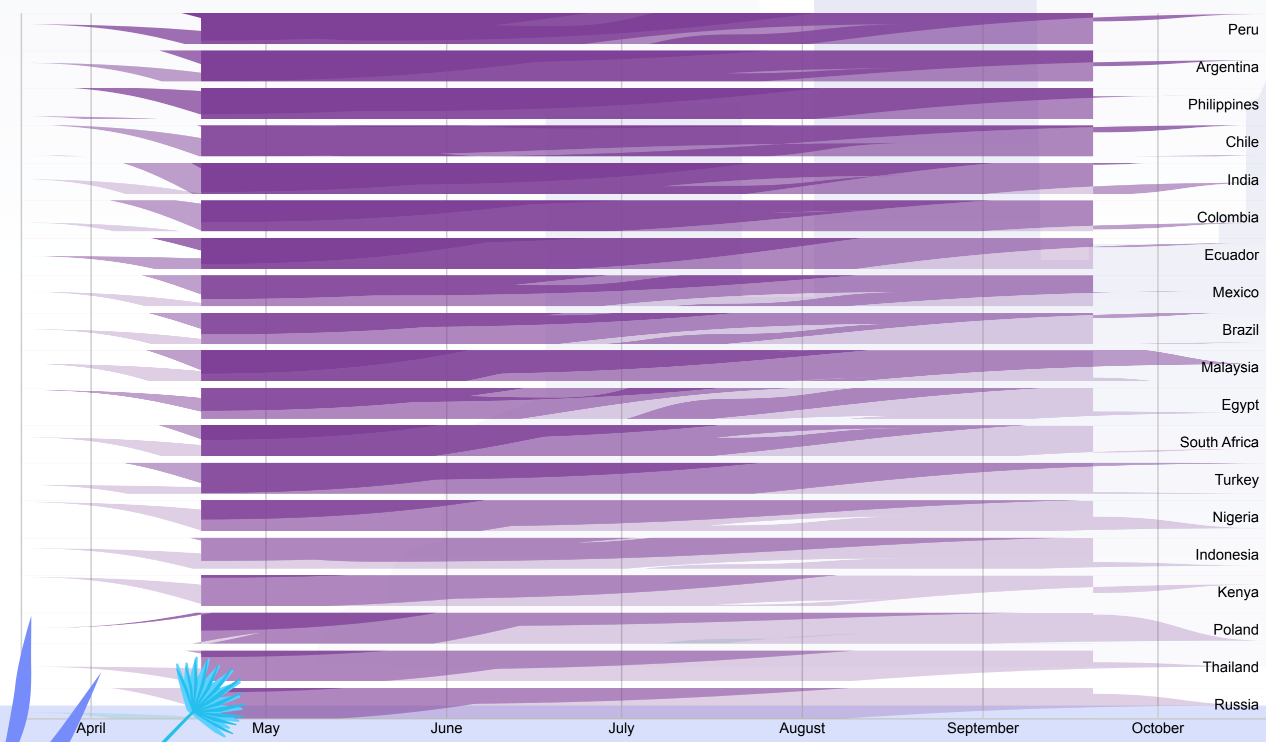
Change of Mobility in Workplaces



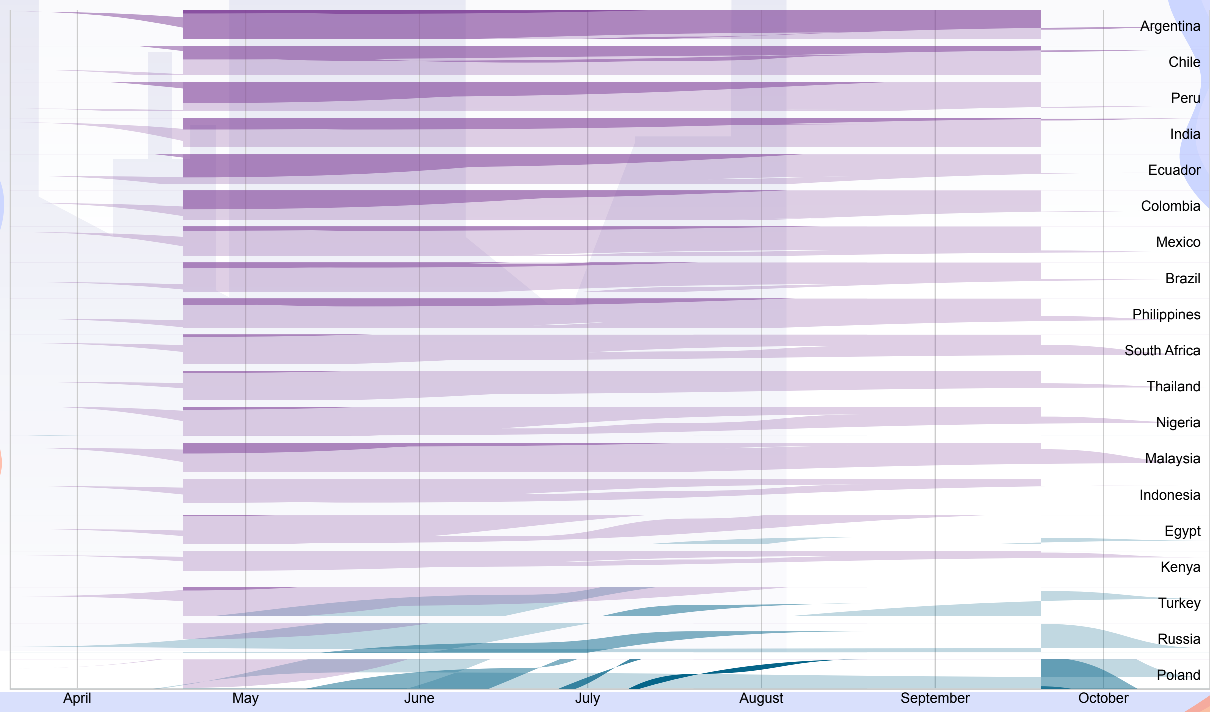
Change of Mobility in Groceries and Pharmacies



Change of Mobility in Retail and Recreation Sites



Change of Mobility in Parks



negative changes to mobility   positive changes to mobility

The graphs depict the monthly median values of workday-adjusted percentage changes in the mobility to selected public places compared to a five-week baseline period from January 3 to February 6, 2020.

Source: Google LLC

THE RETURN OF THE STATE

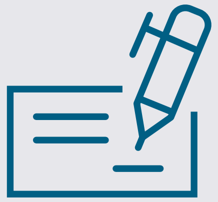
In a few years' time, when we look back at 2020 we will certainly see it as one of the biggest milestones in modern human history. The COVID-19 outbreak made the world stop in its tracks.

SVETOSLAV MLADENOV

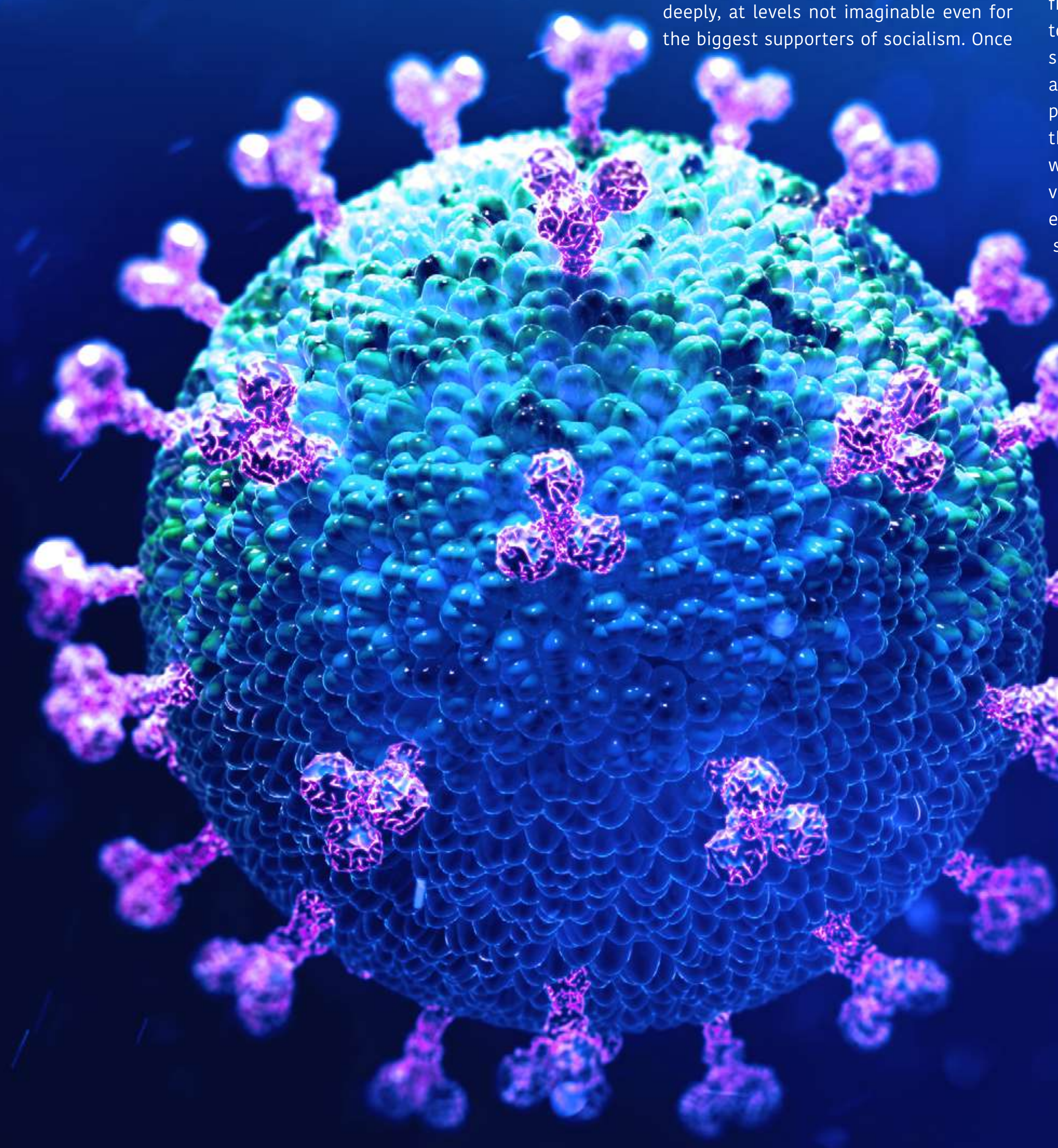
Global Industry Researcher

Then, in the blink of an eye, everything changed - traditional business models, old habits and work routines, rigid government institutions, and even the way we interact with each other. The pandemic – one of the defining events of our time – enforced new rules, new practices and new ways of living. It has also spawned new expectations towards the governments and their role as the ultimate guardians of all citizens.

In the first quarter of 2020, as COVID-19 engulfed more and more countries, governments around the world resorted to unprecedented measures to protect citizens from this new and unfamiliar threat. Lockdowns with different levels of severity, bans on social gatherings, state border closures and restrictions on international trade became the new norm. To mitigate the negative effects of these measures, governments also launched a plethora of unconventional policies to support household incomes, jobs and businesses. These included cash transfer programmes, subsidies, price controls, tax breaks, debt repayment moratoriums, financing at preferential terms and even nationalisation of companies – either in financial distress or of strategic importance to the national security. More or less hesitantly, we accepted the higher government intervention in the economy and our everyday life. We even began considering political and economic ideas that had previously been repudiated as far-fetched or utterly unacceptable, such as universal basic income and state surveillance on individual activity. Why? This was in line with our innate expectations – in times of crisis, governments need to act in order to protect the common good. An unprecedented threat requires unprecedented actions.



IN TIMES OF CRISIS GOVERNMENTS NEED TO PROTECT THE COMMON GOOD



The State Steps In

In a flash, many pundits proclaimed the end of the neoliberal economy and the laissez-faire capitalism. And they had a point. When COVID-19 struck, we expected the governments to minimise the threat posed to our lives regardless of the economic costs. These expectations materialised in massive lockdowns and restrictions that disrupted economic activity. Governments intervened quickly and deeply, at levels not imaginable even for the biggest supporters of socialism. Once the initial COVID-19 shock faded away and governments started to reopen the battered economies, our expectations shifted again. This time we expected governments to try to guarantee our future incomes. Individuals working in the hardest-hit sectors, self-employed, informal workers and those with lower levels of education and incomes pleaded with government to reduce the mounting economic risks they were facing. Companies of all sizes and from an array of industries — from tourism to transportation and energy – followed suit, requesting financial support. It was all just history repeating itself. In previous periods of major economic turmoil such as the Great Depression in the 1930s, there were expectations for a higher state intervention too. And governments met those expectations. According to the IMF, in response to the COVID-19 pandemic governments around the world had announced fiscal measures worth a staggering USD 11.7tn, as of early September 2020. About 51% of this amount corresponded to additional public spending or foregone revenues, including temporary tax cuts, while the remaining 49% accounted for liquidity support, such as loans, guarantees, equity injections and asset purchases by the state. The combined value of these measures is equivalent to a massive 11.8% of global GDP in 2020.

USD 11.7TN

Global fiscal measures to fight COVID-19 as of September 2020

Central banks also joined the mission to safeguard the world's economy, with an unorthodox, ultra-expansionary monetary policy. Since the beginning of the COVID-19 outbreak, the five leading central banks – those of the US, the eurozone, the UK, China and Japan – have injected over USD 5tn into markets. And these figures are set to climb further, as governments continue to ramp up spending, while central banks pump liquidity as a response to the new waves of the pandemic in late 2020.

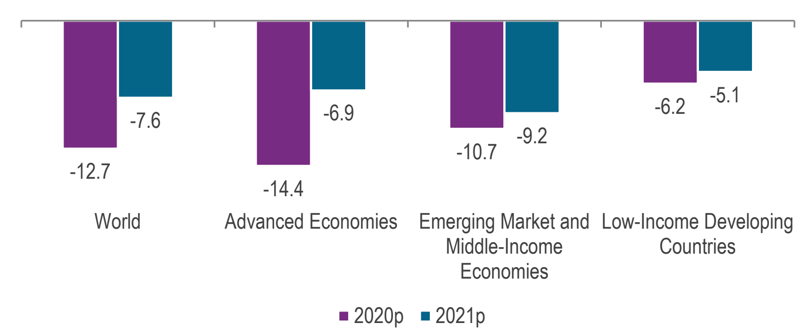
It is hard to imagine the alternative scenario: where we would be if we had relied entirely on the "market knows best" doctrine to confront the health and economic havoc wrought by the novel coronavirus. A crisis of such proportions made it clear that even the most powerful industries are vulnerable to external shocks. It also demonstrated that markets do not have the coordination needed to address such shocks or the ability to offer social protection to vulnerable populations. Besides, markets do not have the capacity to provide transparent and proportionate ground rules that only legitimate governments have. Nevertheless, it is too premature to declare the death of capitalism – it will survive this crisis as it has previous ones. With a sensible and targeted state intervention, we can repair the flaws of contemporary laissez-faire capitalism – especially the rising inequality. We can evolve towards a system that prioritises collective over individual responsibility related to the mounting risks that we are facing – health, economic, social and environmental, to name but a few. No matter how we call this new system, whether it is regulated market capitalism, progressive capitalism, democratic socialism or state capitalism 3.0, one thing is certain: in the post-COVID-19 world, governments will undoubtedly play a bigger role in the economy and our everyday life.

Paying the Bills

Still, a key question arises. How to resolve the conflict between the calls for governments to tackle the COVID-19 pandemic and the economic recession, on the one hand, and the swelling public debt that limits the possibilities for state intervention, on the other? Without a doubt, the fiscal and monetary measures in response to the pandemic have saved many lives, supported vulnerable people and businesses, and prevented a collapse of the economy. However, they proved to be rather costly, especially in times of falling tax revenues and declining economic activity due to the recession. According to the October 2020 estimates of the IMF, in 2020 government deficits around the world will surge to 14.4% of GDP for advanced economies, 10.7% for emerging markets and middle-income economies, and 6.2% for low-income developing countries. Despite a mild moderation, government deficits are projected to remain close to these levels in 2021 and this is expected to push global public debt to a record high of nearly 100% of GDP in 2021.

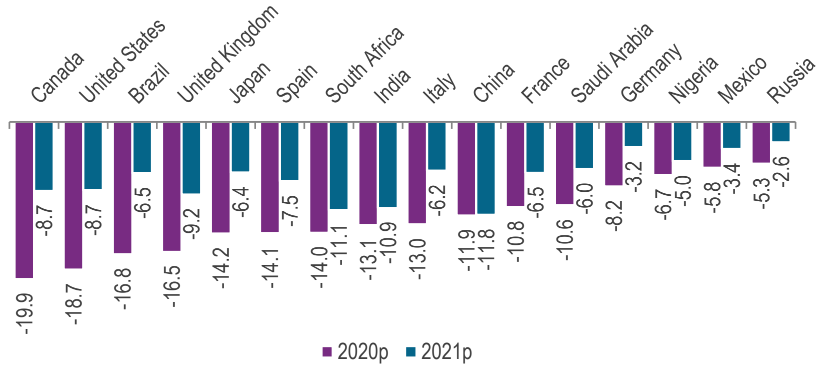
GLOBAL PUBLIC DEBT TO REACH NEARLY 100% OF GDP IN 2021

General Government Fiscal Balance in Selected Country Groups, % of GDP



Source: IMF

General Government Fiscal Balance in Selected Countries, % of GDP

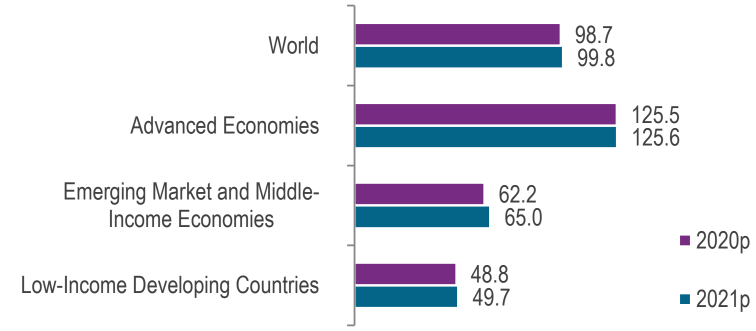


Note: Data for the United States excludes the imputed interest on unfunded pension liabilities and the imputed compensation of employees. Data for Spain includes financial sector support.
Source: IMF

The COVID-19 pandemic has also prompted us to rethink our perception of public debt sustainability. The emergency government measures to tackle the pandemic resulted in surging public deficits that forced states to increase borrowing at an unprecedented pace. In a post-COVID-19 world, it would be normal for the government debt to surpass the value of a country's annual output. Why? Without the emergency government measures, the economic contraction would have been longer and more painful, so the debt burden in relation to the GDP would have increased in any case. Additionally, as the growing indebtedness is a widespread phenomenon across the globe, investors would certainly change their perception of financial risk and increase their tolerance thresholds for debt. A public debt of around 150% of GDP is now the new 100%. Additionally, as long as central banks continue their ultra-expansionary monetary policy through record-low interest rates and massive purchases of public debt, the debt bonanza will suit both investors and governments.

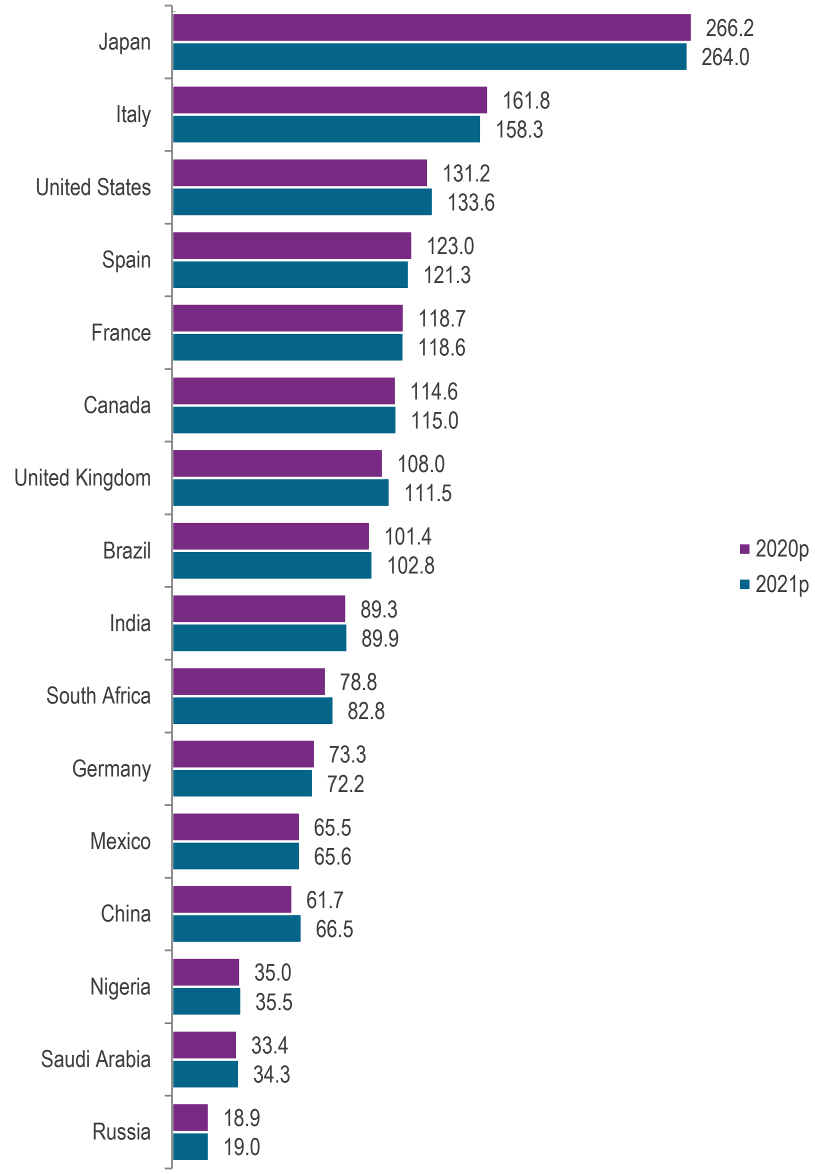
Governments should – and will continue – spending and borrowing at an accelerated pace. At least in the short term. As uncertainty about the course of the pandemic persists, the governments cannot risk withdrawing fiscal support too quickly. The COVID-19 pandemic led to a massive decline in global labour incomes – they collapsed by 10.7% y/y, or USD 3.5tn, in the first nine months of 2020, according to the International Labour Organisation. Additional losses in labour incomes are projected for the last quarter of 2020 and early 2021, as new waves of the pandemic unfold, forcing governments to preserve employment and income support measures. Even with the announced fiscal support, the World Bank expects an increase of the global poverty for the first time in over two decades, with close to 90mn people falling into extreme poverty and living on less than USD 1.9 a day. Moreover, inequality will keep climbing, as the pandemic hurt disproportionally individuals with lower levels of education and income, younger people, self-employed and informal workers. Further, after a projected rebound in 2021, the global economic growth is expected to moderate significantly, with the average GDP per capita not likely to return to the pre-pandemic levels at least until 2023.

General Government Gross Debt in Selected Country Groups, % of GDP



Source: IMF

General Government Gross Debt in Selected Countries, % of GDP



Note: Data for Canada and the United States excludes unfunded pension liabilities of government employees' defined-benefit pension plans. Data for Brazil refers to the non-financial public sector, excluding state-run companies Eletrobras and Petrobras, and includes sovereign debt held on the balance sheet of the central bank.

Source: IMF

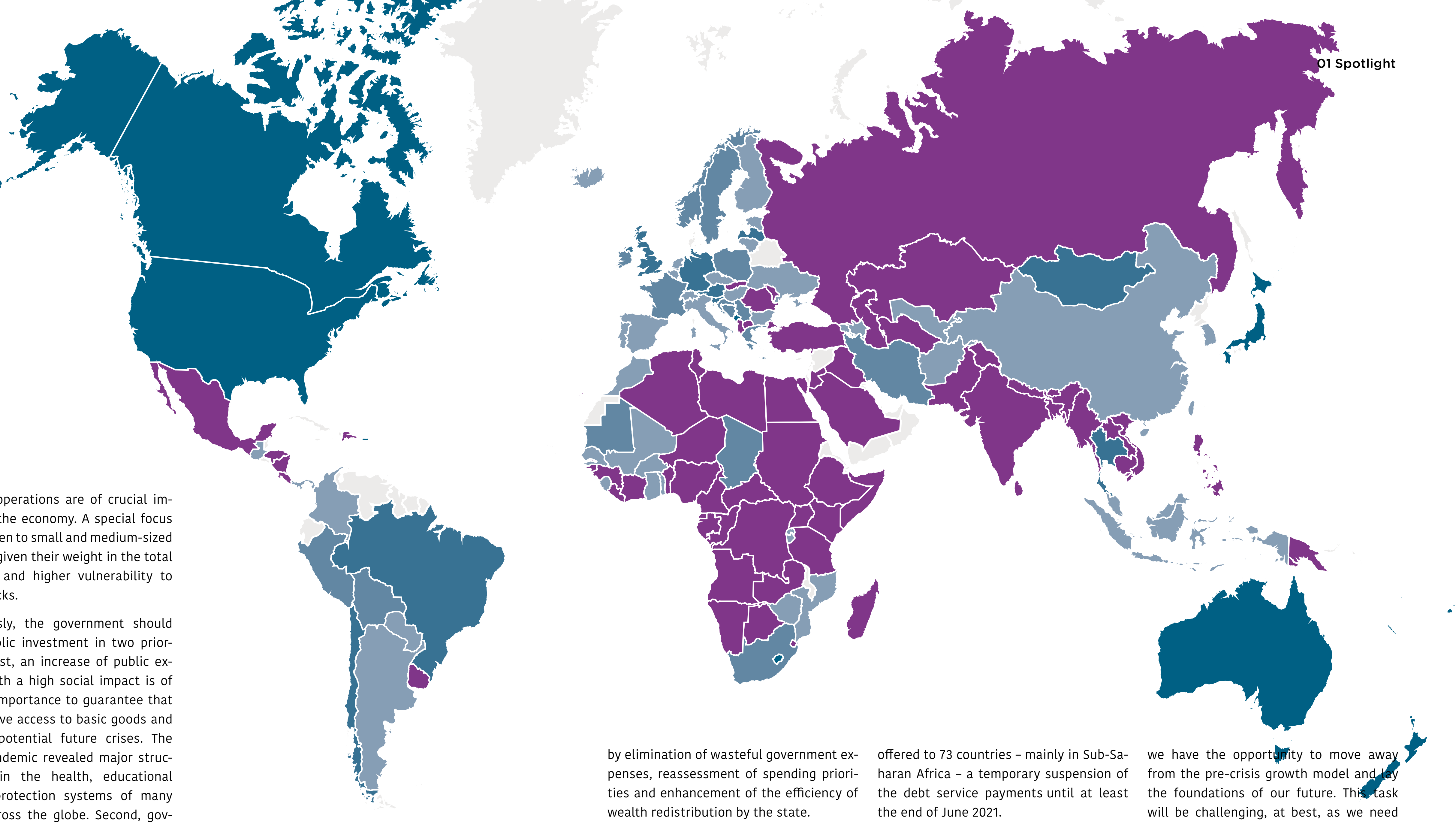
01 Spotlight

COUNTRY FISCAL MEASURES

Value of Additional Spending and Foregone Revenue in Response to the COVID-19 Pandemic, % of GDP

- More than 10%
- 7.5% - 10%
- 5% - 7.5%
- 2.5% - 5%
- Less than 2.5%
- No data

Note: Data as of September 11, 2020
Source: IMF



Addressing the Legacy of the COVID-19 Pandemic

Nevertheless, the period of loose fiscal policy cannot last for too long, as it poses a threat for a deeper crisis in the future. Once the pandemic is under control through effective vaccines and medical treatments, the government should start addressing the legacy of the COVID-19 pandemic – including the rising inequality and poverty, the battered economies, the fragile public finances and the mounting debt.

To start with, fiscal measures should be gradually phased out or transformed into more targeted measures that support the structural transformations that we observe at all levels of society.

For instance, job retention schemes can be re-tooled to programmes that foster new economic activities enabled by digital technologies and help individuals find new, more productive jobs. Funds can also be allocated to lifelong learning initiatives for improving the qualification of workers and adopting digital skills. With regard to companies, support should be more selective and cover only the hardest-hit sectors. In addition to lowering public costs, this will encourage necessary restructurings of unviable business models and promote competition. In other words, support should be destined only to viable companies whose operations are impaired by health risks, government restrictions or supply chain disruptions, or to companies whose operations are of crucial importance to the economy. A special focus should be given to small and medium-sized enterprises, given their weight in the total employment and higher vulnerability to external shocks.

Simultaneously, the government should ramp up public investment in two priority areas. First, an increase of public expenditure with a high social impact is of the utmost importance to guarantee that all people have access to basic goods and services in potential future crises. The COVID-19 pandemic revealed major structural gaps in the health, educational and social protection systems of many countries across the globe. Second, governments should prioritise investments that accelerate the transition towards the post-COVID-19 growth model. Priority should be given to data and digital infrastructure, as enablers of the digital economy, and measures that mitigate greenhouse gas emissions and facilitate the transition towards green and circular economy. The increased public investment in times of record-low interest rates and high levels of uncertainty can boost business confidence in the recovery and induce the private sector to invest as well. To fund the higher public investment, governments can opt for introducing new taxes or enhancing existing revenue sources. Possible measures in this field are higher taxes for the more affluent and less-affected by the pandemic individuals and businesses; broader tax base, better compliance, and stricter enforcement of tax collection; and modernisation of the taxation on multinational companies.

FISCAL MEASURES SHOULD BE GRADUALLY PHASED OUT OR MADE MORE TARGETED

All of these measures, if implemented in an efficient and timely manner, have the potential to bolster economic growth and reverse the rise of poverty and inequality. They can also improve public finances and curb budget deficits. The high debt levels should not be a cause of much concern as long as the growth rate of the economy exceeds the average interest rate paid to service public debt. In other words, a joint effort of governments and central banks is needed to spur growth and preserve interest rates at record-low levels – a scenario that will turn interest rate growth differentials negative and subsequently push down the share of public debt in GDP. Without a shred of doubt, addressing fiscal imbalances should also be accompanied by elimination of wasteful government expenses, reassessment of spending priorities and enhancement of the efficiency of wealth redistribution by the state.

Nevertheless, the path to fiscal recovery will differ across countries. Developed economies can take advantage of the record-low interest rates to scale up public spending, attract private investment, and subsequently boost growth and employment. Simultaneously, they should start preparing fiscal adjustment measures for the medium term. Emerging economies with enough fiscal space should follow suit and be even more ambitious in terms of public investment. On the other hand, emerging markets with limited fiscal space and low-income economies should focus on improving the efficiency of public spending. Some of them will also need external financial support and extensive debt relief programmes to bring their finances in order after the COVID-19 shock. Fortunately, there are already good examples for multilateral cooperation in this area. Among these is the Debt Service Suspension Initiative of the G20 countries, which offered to 73 countries – mainly in Sub-Saharan Africa – a temporary suspension of the debt service payments until at least the end of June 2021.

Laying the Foundations of the Future

An unprecedented crisis like the COVID-19 pandemic has the powers to magnify and accelerate trends that were already under way - changes that might have taken years, now happen in months. Among these changes are the digitalisation of our everyday life; the emergence of new work routines and practices; the technology-driven transformations of business models; and the reshuffling of supply chains. The crisis has also incited a reconsideration of many of our beliefs, which will have a long-lasting impact on the economy and society. These include the future of capitalism, the role of governments, and the perception of risks that affect us all and call for collective responsibility and action.

Without losing more time, we need to step up the preparations for the post-COVID-19 world. As we emerge from the pandemic, we have the opportunity to move away from the pre-crisis growth model and lay the foundations of our future. This task will be challenging, at best, as we need to address multiple pre-existing issues such as inequalities and climate change, build resilience against future shocks, and complete the transition towards a digital, green and inclusive economy. Yet, one thing is certain – governments will be the main protagonist in this endeavour. ISI

JOINT EFFORT OF GOVERNMENTS, CENTRAL BANKS IS NEEDED TO SPUR GROWTH AND PRESERVE LOW INTEREST RATES

02

Asia

WHAT DOES CHINA BUY ONLINE

Online retail sales proved resilient, but the pandemic disrupted shopping patterns

Top 10 Product Groups Purchased via Taobao and Tmall, RMB tn

34.7	WOMEN'S APPAREL AND ACCESSORY
24.1	RESIDENTIAL FURNITURE
17.5	MEN'S APPAREL
14.8	BEAUTY AND SKIN CARE, ESSENTIAL OILS
11.8	HARDWARE AND TOOLS
10.7	SNACKS AND NUTS
9.6	LARGE HOUSEHOLD ELECTRICAL APPLIANCES
8.6	WOMEN'S FOOTWEAR
8.2	UNDERWEAR, HOME APPAREL
7.2	MOBILE PHONES

Source: CEIC, Moojing Market Intelligence

The lockdown in Wuhan, Hubei's capital, the strict social distancing measures in response to the COVID-19 outbreak across China and the cautiousness of the society in terms of spending took their toll on consumption. However, online retail sales demonstrated resilience and did not post any negative change, year-to-date, compared to 2019. Actually they kept increasing. The total retail sales kept declining on an annual basis as of September 2020, albeit at a less steep rate each month.

Apparently and understandably, the least essential items - clothing - were the only component to suffer negative annual change, recovering only in August.

LOCKDOWN VS RECOVERY, CHINA

Retail Sales, ytd, y/y change

	FEB-20	OCT-2020
ONLINE	3%	16%
OVERALL	-20.5%	-5.9%

Source: CEIC, NBS

Online Retail Sales by Main Group, ytd, y/y change

	FEB-20	OCT-2020
FOOD	26.40%	34.30%
CLOTHING	-18.10%	5.6%
DAILY NECESSITIES	7.50%	17.40%

Source: CEIC, NBS

SHARE OF ONLINE RETAIL SALES OF CONSUMER GOODS

In a matter of seven years, the share of online retail sales in China grew almost four times.

2013	2020
6.9%	24.3%

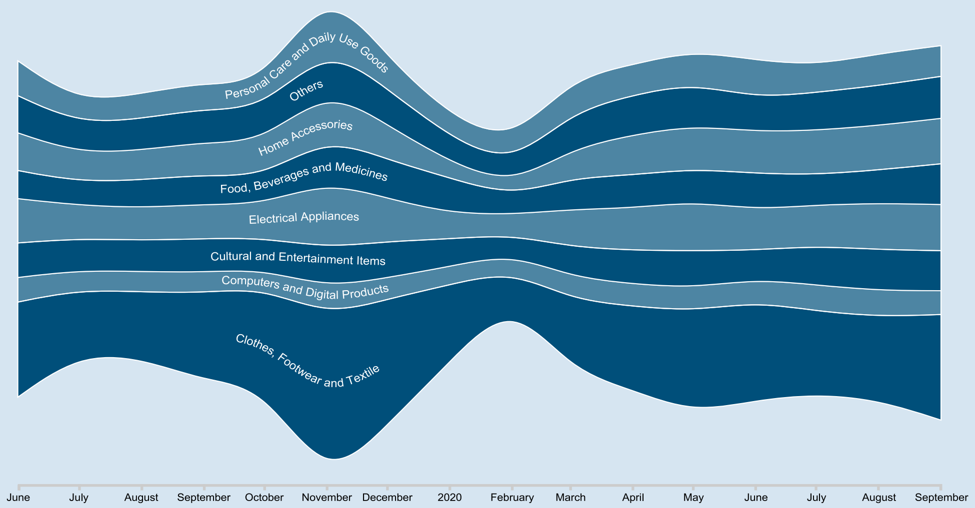
Source: CEIC, NBS

ONLINE RETAIL MARKET

As an absolute value the growth is sevenfold.

2013	2020
RMB 1.2TN	RMB 7.6TN

HOW THE PANDEMIC DISRUPTED ONLINE SHOPPING PATTERNS



Source: CEIC, Moojing Market Intelligence

Despite remaining relatively resilient compared to other sectors, online retail sales experienced change in the shopping patterns, evident from the February 2020 data, as many parts of China were subject of strict social distancing measures. The figures cover Taobao & Tmall, which are the most prominent online sales platforms, accounting for over 60% of the e-commerce market in China. ISI

RETHINKING CHINA'S GROWTH

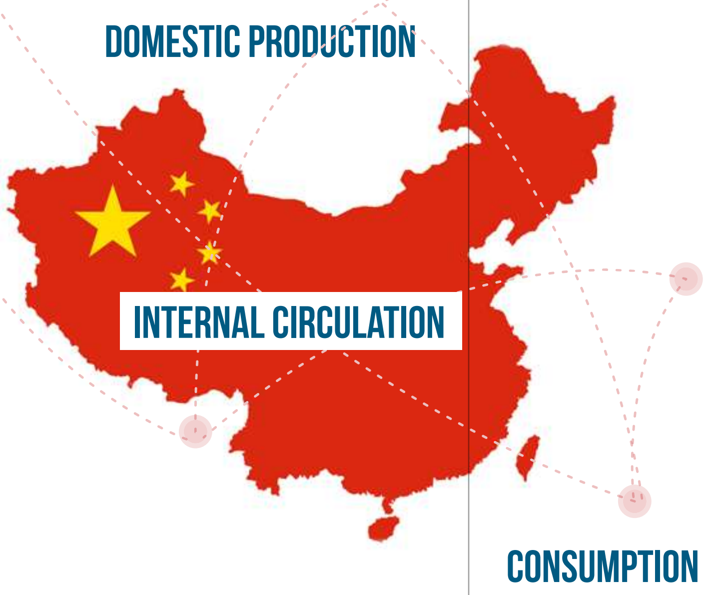
Yinglei Li, Industry Researcher, China

FOR DECADES CHINA'S EXPORT-ORIENTED MODEL HAS FUELLED AN UNPRECEDENTED ECONOMIC EXPANSION.

The 2008-2009 global crisis, however, has exposed the vulnerabilities of that model and the rising geopolitical tensions in recent years have shifted the focus, prompting Beijing to rethink growth strategies. Back in 2016 when China's real economic growth weakened to below 7% for the first time in two decades, the government centred its five-year plan on significantly raising the share of consumption in GDP. In the following years, however, the share of domestic consumption in total GDP remained unchanged at 55%. One of the underlying reasons is that the country had enormous external markets to absorb its output and sustain its growth. That situation changed abruptly in early 2020 when the spread of the COVID-19 pandemic disrupted global economic activity and trade flows in a way that reinforced China's self-reliance efforts.

55%

DOMESTIC CONSUMPTION SHARE IN GDP



GLOBAL TRADE

EXTERNAL CIRCULATION

FOREIGN INVESTMENT

10% of GDP

Transportation, Healthcare and Education Sectors

Dual Circulation Strategy

The dual circulation strategy concept was first floated by Chinese President Xi Jinping in May 2020. The strategy's goal is for the country to rely mainly on internal circulation, making domestic production and consumption the main engines of growth, supported by innovation and upgrades in the economy. External circulation will play a supporting role in boosting economic growth. The purpose of the model is to reduce China's dependence on foreign markets and it has been touted as a viable strategy to build up resilience to external shocks.

DUAL CIRCULATION STRATEGY TO IMPROVE CHINA RESILIENCE TO EXTERNAL SHOCKS

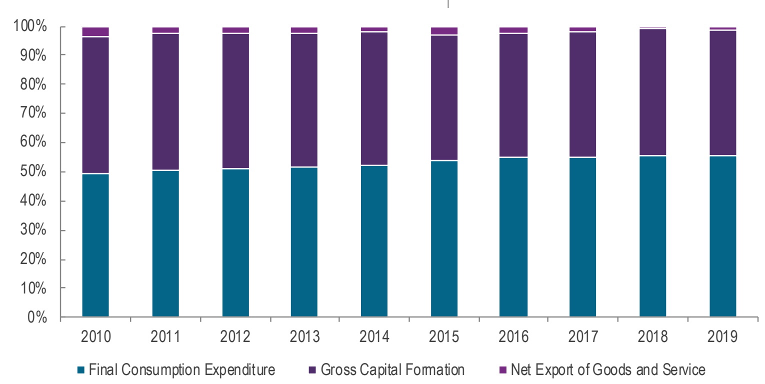
It comes in contrast with the "great international circulation" strategy adopted by former Chinese leader Deng Xiaoping in the 1990s that advocated for the opening of the economy.

Consumption in the Spotlight

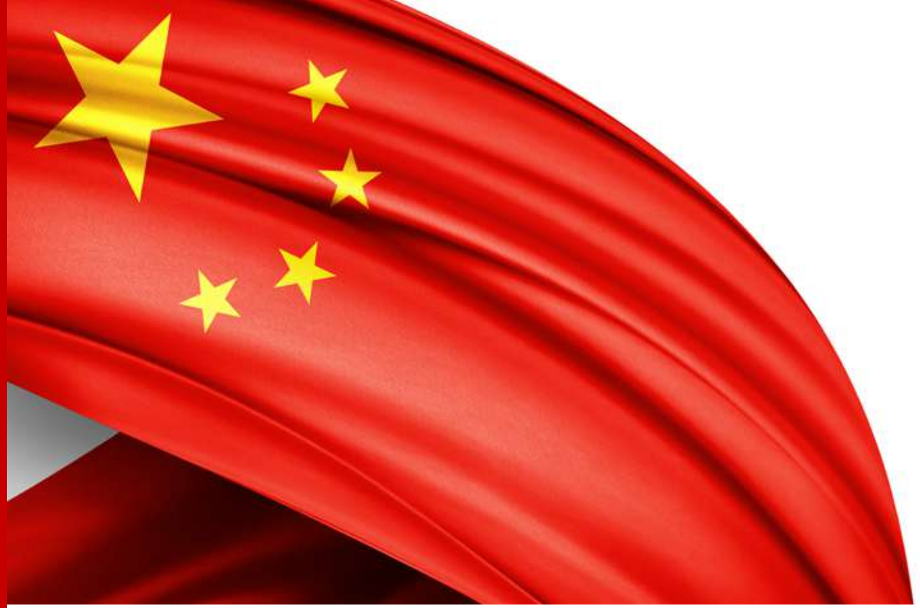
While investment and consumption are the two major domestic sources of economic growth, this time China firmly goes for consumption, believing that it is the strongest and most sustainable growth engine. To kick-start consumption the government is planning to accelerate investment in certain service sectors where demand is yet to be fulfilled. These include transportation, healthcare and education. These sectors together accounted for only 10% of China's GDP in 2018 based on data from the National Bureau of Statistics. The government now faces the question of how to effectively enhance these key sectors to expedite personal consumption expansion.

While the continuous construction of physical facilities, such as railways, highways, hospitals and schools, will certainly be required as before, the specificity of sector upgrades this time lies in the deep integration of digital and energy-saving technologies. And here comes the renewed focus on China's new infrastructure initiative. The initiative is not new – it was first unveiled in December 2018 when China set as its priority the development of artificial intelligence, industrial internet and the Internet of Things. Now, Beijing is positioning investments in new infrastructure as a key pillar of its post-pandemic recovery. The initiative is expected to mobilise investments of USD 2tn over the next five years in areas such as 5G base stations, high-voltage power grids, inter-city high speed railways and urban rail transit, charging piles for new energy vehicles (NEV), big data centres, artificial intelligence and industrial internet They are expected to become the technical foundation that will enable the transportation, healthcare and education sectors to awaken the dormant consumer demand.

CHINA'S GDP COMPONENTS



Source: China's National Bureau of Statistics, CEIC



KEY SECTORS IN CHINA'S USD 2TN NEW INFRASTRUCTURE PLAN

5G INFRASTRUCTURE

Construction of 5mn-5.5mn base stations by 2025 to ensure countrywide coverage

ARTIFICIAL INTELLIGENCE (AI)

Establishment of 20 AI innovative trial zones by 2023

BIG DATA CENTRES

Construction of a large number of big data centres, super-data centres and edge-computing data centres by 2025

INDUSTRIAL INTERNET

Launch of 3 to 5 world-class industrial internet platforms by 2025

ELECTRIC VEHICLES INFRASTRUCTURE

Construction of more than 36,000 electric vehicle charging stations by 2025

NEW INFRASTRUCTURE INVESTMENT INITIATIVE TO GENERATE USD 2TN IN INVESTMENTS

Transportation Sector

Transportation infrastructure, although having experienced intensive development in past decades, remains insufficient given the country's vast territory. For the purpose of driving domestic consumption in a low-carbon way the government is likely to continue supporting this sector through two independent strategies.

On the public transport side, regional railway is expected to become the top priority segment for expansion, given that the government has long accentuated the importance of regional collaboration and resource-sharing.

REGIONAL RAILWAY TO BECOME TOP PRIORITY

Different from the traditional long-distance railways, which serve cargo transportation better than passenger considering the low efficiency of cross-country travelling, the shorter distanced inter-city railways within a certain region are expected to mainly cater to people's demand for more time-saving and more frequent travels and thus to boost regional tourism.

Healthcare Sector

The healthcare sector in China took a heavy blow during the peak of the pandemic, when the critical issue of imbalanced allocation of medical resources became apparent. China's high-end medical resources have always been concentrated in urban areas. In 2019, a rural area resident spent an average RMB 1,421 on medical and healthcare, which is only 62% of the spending of urban residents, indicating that demand for medical services in rural areas has not been met. Considering that rural residents account for nearly 40% of China's total population based on 2019 data, the most urgent task in the healthcare sector must be to tackle this resource imbalance problem.

Fortunately, there is a solution that has been proven effective during the lockdown period – online healthcare services. When hospitals were largely closed for non-emergent patients in order to mobilise medical resources for COVID-19 treatment in Q1 2020, online medical platforms rose up to the challenge and shouldered some of the burden of traditional hospitals. The popularity of online healthcare remained high even after China successfully brought the epidemic under control. The major pioneers in this area, such as AliHealth and JD Health, are now not only providing online health consultancy services but are also utilising their developed e-commerce network to cooperate with offline hospitals and pharmacies to close the circle of online-offline medical services. With the support of 5G, big data, artificial intelligence and other new technologies, rural residents will finally be able to have access to high quality treatment services, at least to some extent.

Education Sector

China's education sector shares certain similarities with the healthcare sector in the sense of geographical imbalance of resources and proven feasibility of online practices. Hence, online education services are bound to expand in the years to come.

Although the government has largely made the nine-year compulsory education available to every child, the most prestigious higher education facilities are located in several first-tier cities, which limits equal access to high-end education services.

As the country suffered from an increasing unemployment rate due to the COVID-19 outbreak and its fallout, businesses turned to providing additional vocational trainings to increase employees' competences. Such continuous education programmes are likely to gain popularity among adults, stimulated by the increasingly competitive job market in China.

POPULARITY OF ONLINE EDUCATION SERVICES BOUND TO GROW

At the moment, only about 20% of all online retail sales come from the services segment, education included, implying that the online education business in China is at an early development stage. Nevertheless, as demand seems bound to increase, both traditional higher education and innovative out-of-school trainings are expected to provide more online programmes for the sake of reaching a wider audience.

ONLINE HEALTHCARE REMAINS POPULAR POST COVID-19 OUTBREAK

Next Five Years

The year 2021 will mark the start of China's 14th five-year plan period. Beijing's targets for that period are strengthening the domestic market and perfecting the economic structure. While investment in hardware infrastructure remains important, China's growth will be driven above all by domestic consumption, as the purchasing potential of the world's most populous nation is yet to be fully explored. The areas that are most likely to expand at a fast pace include transportation, healthcare and education. And this time, with the integration of digital technologies, the geographic restrictions traditionally inherent to the services industry will gradually be removed, granting people, wherever they are, more equal access to high quality services. ISI

02 Asia

CHINA

DIGITAL HEALTHCARE IN THE SPOTLIGHT

Xintong (Olivia) Wu, Macroeconomic Researcher, China

Imagine you are living in a city in China. One day you wake up feeling a bit unwell and decide to go see a physician. Although you are aware of the existence of community health centres and clinics, you still choose to go to the nearest top-tier public hospital because you want to get the most qualified help available. After waiting in line for hours, you finally get to meet the physician just to join later another queue in front of the hospital pharmacy. Thus, a regular doctor's appointment typically takes a whole day and is a most exhausting experience.

Riding the Wave of Change

This has long been the accepted norm for many patients in China. Even before the COVID-19 outbreak put a huge strain on China's healthcare services, the sector had been facing many challenges, the lack of resources being among the most serious ones. The development and deployment of internet and mobile technologies have granted an increasing number of patients access to online healthcare services.

DIGITAL TECHNOLOGIES GIVE MORE PEOPLE ACCESS TO QUALITY HEALTHCARE SERVICES

By simply downloading a mobile app, patients in China now have easier and quicker access to many experienced physicians across the country. Patients can choose between a one-time consultation via messages, a phone call with the physician, or long-term personalised advice.

Digital healthcare technologies also proved to be a critical tool in the fight against COVID-19. Artificial intelligence, robotics and information and communication technologies provide innovative and valuable solutions for patient treatment, frontline protection, risk reduction and improved quality of living. The pandemic forced the healthcare sector, which has traditionally been conservative in adopting modern technologies for reasons such as regulatory approval, patient privacy and interoperability, to embrace the wider adoption of digital healthcare services. An evidence of that is the Chinese government's decision to finally agree to pay for prescriptions ordered online.

The Background

The uneven development of China's healthcare system has been problematic for a long time. The number of China's hospitals has been growing steadily in recent years. In 2019, China had 34,354 hospitals, more than five times more than in the US. However, more than 60% of these hospitals are privately owned, meaning they are automatically not the first choices of people with social insurance plans. Only 1,516 out of the 11,930 public hospitals are rated as top-tier hospitals and their popularity compared to non-top-tier ones is enormous. People from rural areas as well as small cities and towns have limited access to high quality healthcare services as top-tier hospitals are mostly located in bigger cities and developed areas.

The Birth of Online Healthcare Platforms

The expansion of digital infrastructure provided a solid foundation for the boom of online healthcare services. Many online healthcare platforms appeared, of which the three biggest were set up by China's e-commerce and insurance giants JD.com, Alibaba and Ping An Insurance.

JD Health, launched in 2014 by JD.com, had a revenue of RMB 10.8bn in 2019, making it the country's biggest online healthcare platform as well as the biggest online pharmacy. From 2017 to 2019, JD Health's revenue grew rapidly and nearly doubled. JD Health is now seeking to raise USD 3bn in its Hong Kong IPO.

Ali Health, listed in Hong Kong, is the healthcare arm of e-commerce giant Alibaba Group and has a business model similar to that of JD Health, providing online drug sales and health consultations to digitally savvy Chinese consumers. Both JD Health and Ali Health benefit from the large number of active users and the solid logistic network of their parent companies.

Unlike JD Health and Ali Health, which specialise in online drug retail, Ping An Good Doctor, launched by insurance giant Ping An Insurance, is focused on online healthcare services. Ping An Good Doctor was listed in Hong Kong in 2018.

Before the COVID-19 outbreak, China had already been supporting public hospitals in the process of building capacity for online medical consultations and diagnosis. Private online healthcare platforms were also gaining popularity. However, the regulatory restrictions and the patient concerns about privacy were big obstacles that hindered the development of the industry. Prior to the pandemic, the use of digital healthcare services in China was rather low. A survey by Brian & Company published in March 2020 showed that only 24% of the Chinese had used telemedicine. Still, 97% expressed interest in digital health services, if the costs were covered by an insurance provider or employer, and 64% said they plan to use telemedicine within the next five years. The COVID-19 shock has greatly changed the market dynamics. In January 2020, a massive number of people resorted to online healthcare platforms to seek help when the whole country was under lockdown and people were afraid to go to the hospitals.

620MN

Number of Digital Healthcare Users

Challenges Ahead

However, China's online healthcare platforms are still at an early stage of development. Out of the three major platforms, JD Health is the only profitable one according to its 2019 financial report. Both Ali Health and Ping An Good Doctor reported losses in 2019. The services offered by these platforms are not yet met with unanimous approval and clients still complain about the quality of the consultations, especially on private healthcare platforms.

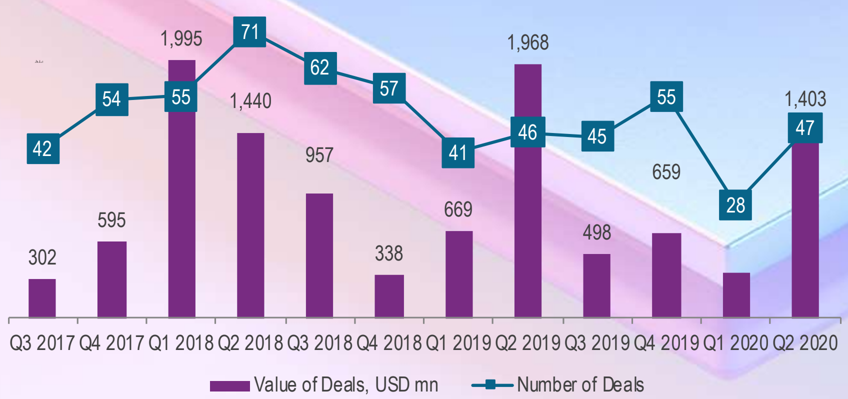
Besides, there are many limitations to online healthcare services. For example, China's traditional medicine hospitals rely heavily on personal interaction with the patients, with doctors depending on observation and palpation in order to diagnose - methods that are not applicable online. The development of the digital healthcare industry might also widen the existing gap between people with better access to the technology and the information and those without such access. On the regulatory side, the challenges are enormous. A regulatory scheme tailored to the digital healthcare industry needs to be set up from scratch. Unlike in online retail, where consumers can easily return products with subpar quality, the quality of healthcare services could be a huge risk to monitor.

The COVID-19 outbreak has provided a huge boost to the development of the online healthcare industry. With a constantly growing demand for healthcare services and an accelerating digital economy, China's online healthcare industry will certainly attract worldwide attention moving forward. The challenges are real, but the benefits will transform an entire generation. ISI

USD 1.8BN

Digital health funding in China in H1 2020

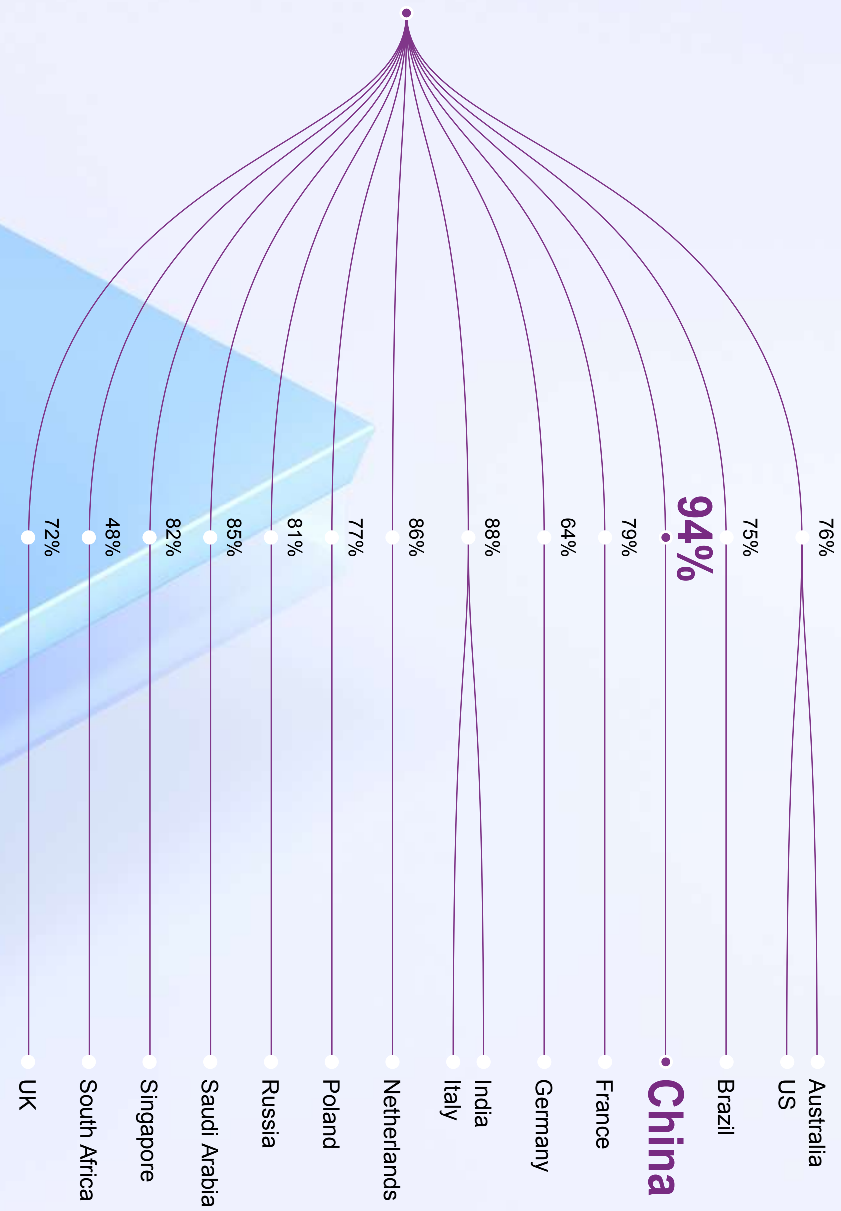
Digital Health Deals in China



Source: CB Insights

SHARE OF HEALTHCARE PROFESSIONALS WHO CURRENTLY USE ANY DIGITAL HEALTH TECHNOLOGY

China leads the world in the use of digital health technologies with the highest percentage of healthcare professionals who currently use any digital health technology or mobile health apps, a Philips survey has showed



Source: Philips' Future Health Index 2019

It's All in the Balance

Rohini Sanyal, Research Economist, India

The outbreak of COVID-19 and the subsequent lockdowns caused massive disruptions in global supply chains, and adversely impacted both consumer demand and the financial markets. The world economy is expected to decline by 4.4% y/y in 2020 and governments across the globe have rolled out fiscal stimulus packages in an attempt to provide short-term relief to people. India's economy was hit particularly hard by the pandemic and the consequences of the strict 40-day lockdown that was implemented in March 2020 were dire. While some exceptions were provided to essential activities, the overall economy came to a virtual standstill. Hence, the government rolled out a fiscal stimulus programme worth INR 20tn, or 10% of India's GDP.

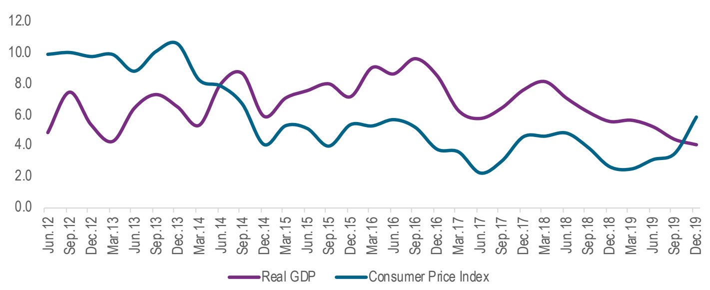
INR 20TN INDIA'S FISCAL STIMULUS PROGRAMME

The Reserve Bank of India (RBI), on the other hand, embarked upon a decisive expansionary monetary policy. Despite these measures, India's GDP is expected to decline by 10.3% in FY2021 (ending March 2021), which will have an impact on government tax collection and increase the fiscal deficit beyond the target of 3% of GDP by FY2021, set by the Fiscal Responsibility and Budget Management (FRBM) Act.

In this article we will analyse the interaction of fiscal and monetary policy and why it is so important for the ability of the state to withstand the shocks from the crisis and emerge stronger in the post-pandemic world.

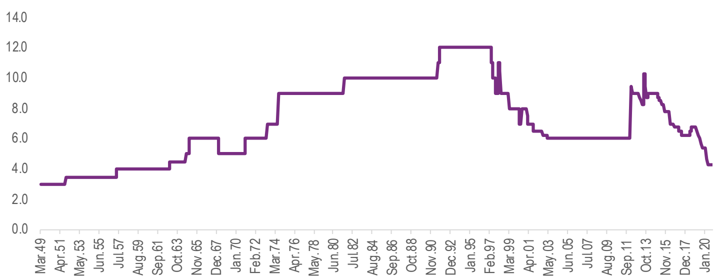
Fiscal policy can impact monetary policy through multiple channels. First, a dominant fiscal policy may lead to a large fiscal deficit, which is monetised by the government. This further leads to an expansionary monetary policy by the central bank that causes inflationary pressure and currency appreciation. If the deficit is financed through market borrowing, there is a risk of increasing the real interest rate that would eventually crowd out private investment. Also, if the deficit is financed with the help of foreign funds, there is a risk of exchange rate and even a balance of payment crisis. The increasing of indirect rather than of income taxes can translate into a wage-price spiral and cause inflationary pressures. Also, financing large budget deficits through borrowings can create the perception of increasing prices, which may lead to high inflation expectations, which can eventually result in an increase in the actual inflation. These situations may lead to financial market instability, may act as a destabilising factor on bond and foreign exchange markets, and may eventually cause a complete breakdown of the monetary regime.

India's GDP Growth and Inflation



Source: India's Central Statistics Office, CEIC

India's Bank Rate



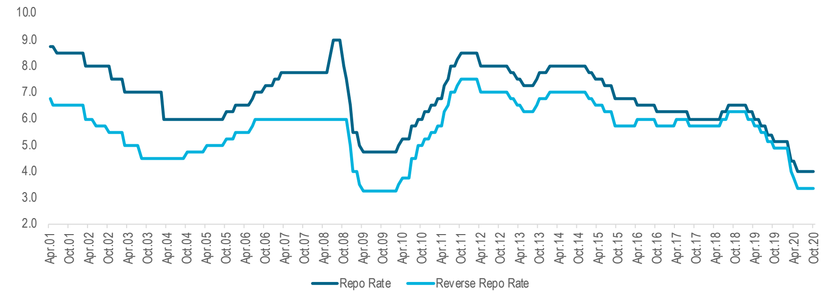
Source: India's Central Statistics Office, CEIC

Since the independence of the country in 1947 India's monetary policy has evolved substantially, moving from credit planning to inflation targeting.

While the evolution has been driven by the declining efficiency of policy instruments, it is the fiscal dominance that has undermined these instruments in most cases. After India's independence, the primary aim of monetary policy was to support the government's economic development plan. Between end-1960s and mid-1980s, RBI started using monetary policy instruments such as bank rate and open market operations to regulate credit growth, money supply and inflation in the country. However, government policies such as the nationalisation of banks in 1969 led to an influx of deposits from the public and increased credit availability in the economy. In addition, the period was marked by a host of external shocks - wars, oil price surges and droughts. As a result, monetary policy instruments proved inadequate. Although in 1985 India moved to a new policy regimen of monetary targeting with feedback that used broad money and reserve money as instruments, fiscal dominance increased further through the automatic monetisation of budget deficits using ad hoc treasury bills and a steady increase in statutory liquidity ratio. India's fiscal situation worsened substantially in the late 1980s, which caused the external balance position to deteriorate, eventually leading to the Balance of Payments Crisis of 1991 and a complete collapse of domestic growth. Consequently, the bank rate and cash reserve ratio (CRR) increased significantly and peaked in 1991. The monetisation of budget deficits was abolished in 1997, and replaced with a system of Ways and Means Advances, which was further replaced by a Multiple Indicators Approach (MIA) in 1998. The MIA model also lost significance owing to the global financial crisis of 2009. In addition, India's double-digit inflation between 2012 and 2013 paved the way for an inflation targeting framework, which was adopted formally by the RBI in 2015.

RBI ADOPTS INFLATION TARGETING FRAMEWORK IN 2015

India's Key Rates



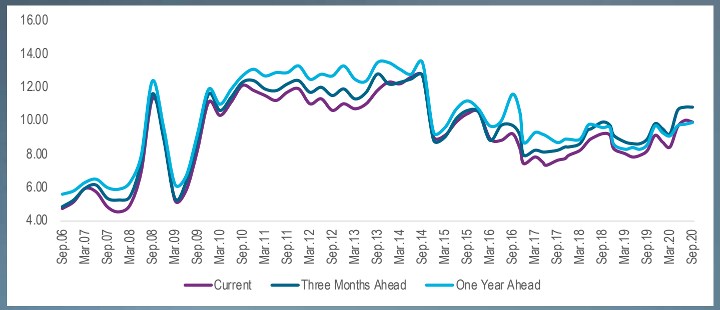
Source: Reserve Bank of India, CEIC

The COVID-19 pandemic and the ensuing lockdown pushed India into a phase of low growth and high inflation. This is seemingly temporary since high-frequency economic indicators are showing improvements. However, the main question that arises is why the monetary policy committee has not increased rates in spite of the expansionary fiscal policy and the widening fiscal deficit. On the contrary, the RBI decreased the repo rate by 80 bps in March 2020, and the CRR by 100 bps, even though consumer price inflation reached 6.6% y/y in February, 0.6 percentage points above the upper tolelance band. The answer to this question lies in the present monetary policy regimen of inflation targeting. A study by Eichengreen et al. in 2020 finds that the inflation targeting model provided a better anchor for inflation expectations, which in turn helped the central bank respond effectively to the COVID-19 situation.

INFLATION TARGETING MODEL HELPS CENTRAL BANK RESPOND EFFECTIVELY TO COVID-19 CRISIS

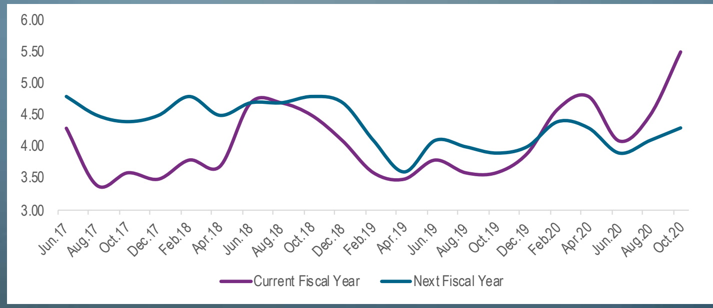
Even with a large fiscal stimulus, inflation expectations have increased but are yet far below their previous highs during crisis situations, such as the one in 2013. The government has also exercised precaution in rolling out the fiscal stimulus by making it a mix of short- and long-term policies. Cash transfers and wage increases were limited to the time of the lockdown, along with the provision of essential food items for the impoverished. Rather, the stimulus was aimed at increasing the productivity of the country by directing finances towards the development of infrastructure, agriculture, and micro and small and medium-sized enterprises. Even with a large fiscal stimulus, inflation expectations have increased but are yet far below their previous highs during crisis situations, such as the one in 2013. The government has also exercised precaution in rolling out the fiscal stimulus by making it a mix of short- and long-term policies. Cash transfers and wage increases were limited to the time of the lockdown, along with the provision of essential food items for the impoverished. Rather, the stimulus was aimed at increasing the productivity of the country by directing finances towards the development of infrastructure, agriculture, and micro and small and medium-sized enterprises. ISI

India's Inflation Expectations Survey of Households



Source: Reserve Bank of India, CEIC

India's Inflation Expectations - Professional Forecasters Survey

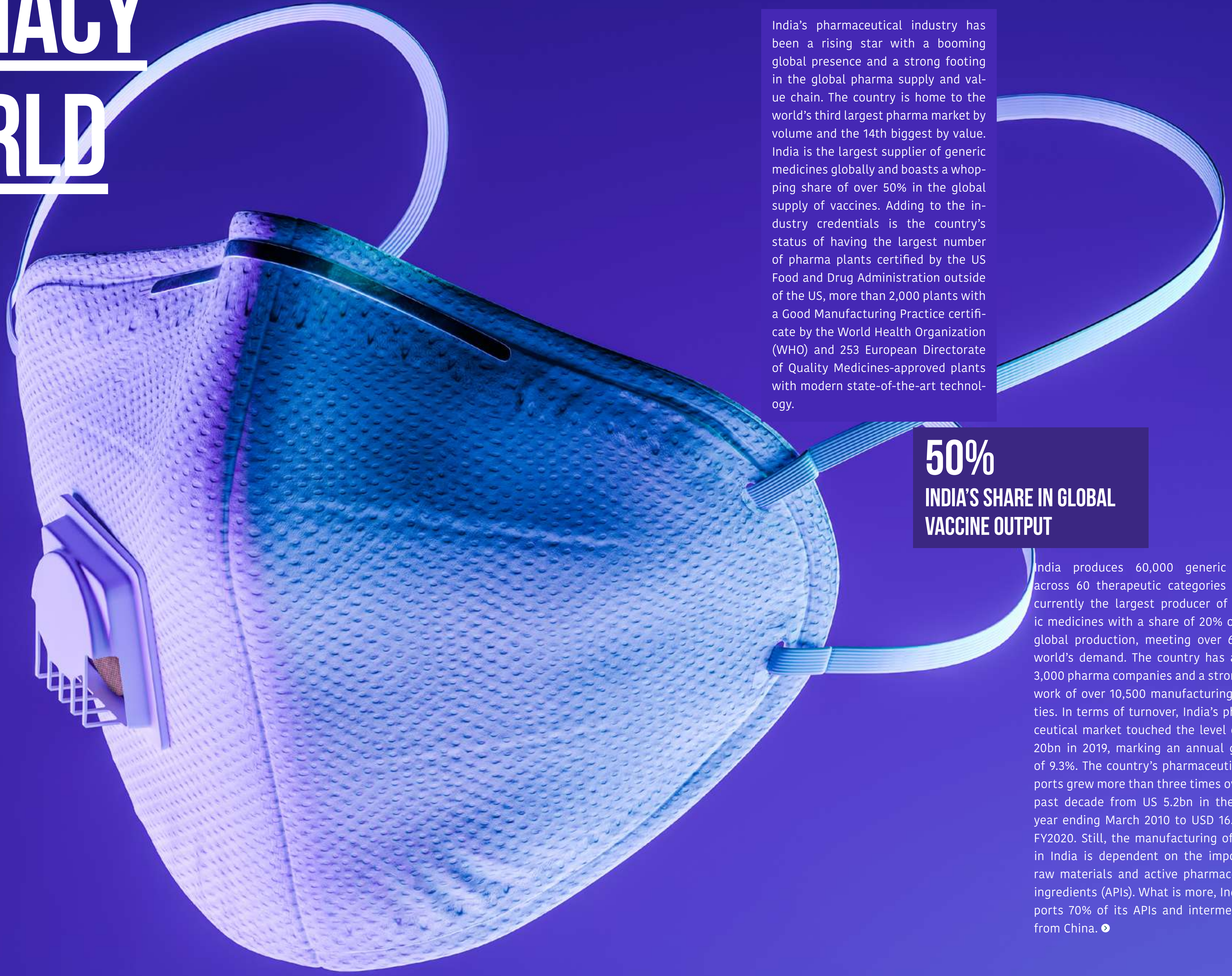


Source: Reserve Bank of India, CEIC

THE PHARMACY OF THE WORLD

Kritika Bhasin, Researcher, India

Producing more generic drugs than any other country and churning out more than half of the world's total vaccine supply, India has rightfully been dubbed the pharmacy of the world. With the onset of the COVID-19 pandemic that has pushed companies to diversify their supply chains, India is seeking to grow its presence and position itself as an alternative to China. The question is will India succeed, given its over-dependence on Chinese raw materials?



RISING STAR

India's pharmaceutical industry has been a rising star with a booming global presence and a strong footing in the global pharma supply and value chain. The country is home to the world's third largest pharma market by volume and the 14th biggest by value. India is the largest supplier of generic medicines globally and boasts a whopping share of over 50% in the global supply of vaccines. Adding to the industry credentials is the country's status of having the largest number of pharma plants certified by the US Food and Drug Administration outside of the US, more than 2,000 plants with a Good Manufacturing Practice certificate by the World Health Organization (WHO) and 253 European Directorate of Quality Medicines-approved plants with modern state-of-the-art technology.

50%

INDIA'S SHARE IN GLOBAL VACCINE OUTPUT

India produces 60,000 generic drugs across 60 therapeutic categories and is currently the largest producer of generic medicines with a share of 20% of total global production, meeting over 60% of world's demand. The country has around 3,000 pharma companies and a strong network of over 10,500 manufacturing facilities. In terms of turnover, India's pharmaceutical market touched the level of USD 20bn in 2019, marking an annual growth of 9.3%. The country's pharmaceutical exports grew more than three times over the past decade from US 5.2bn in the fiscal year ending March 2010 to USD 16.3bn in FY2020. Still, the manufacturing of drugs in India is dependent on the imports of raw materials and active pharmaceutical ingredients (APIs). What is more, India imports 70% of its APIs and intermediaries from China.

GROWING AMBITIONS

In pre-COVID times, the Indian pharma industry was undergoing a profound transformation and was at the threshold of an interesting phase. Local pharma companies were honing in on becoming a global manufacturing hub for low-cost drugs and on creating a whole pharma manufacturing ecosystem in the country. With the outburst of the COVID-19 pandemic, the importance of this vision has grown by leaps and bounds along with its urgency.

India's significance for the global pharma supply chain was proved once again as the country turned out to be manufacturing 70% of the world's supply of the hydroxychloroquine (HCQ), the anti-malarial drug touted as a game changer in the early days of the fight against COVID-19. The drug is not manufactured in developed nations where malaria is non-existent, whereas India has a monthly production capacity of 40 tonnes of HCQ. Once again, India's overreliance on imports became evident, as the API used to manufacture HCQ is imported from China.

20%

INDIA SHARE IN GLOBAL GENERIC DRUGS OUTPUT

FIGHTING OVERDEPENDENCE

The supply chain disruptions, export bans and the shortage of essential medical products in various countries caused by the COVID-19 pandemic have exposed the overdependence of the world on China. For instance, China is the world's largest producer of personal protective equipment (PPE). Initially, China imposed restrictions on PPE exports that were later lifted, but the country was not able to meet the sudden spike in global demand and on top of that it supplied poor quality and defective PPE to various countries. This revealed the weaknesses and vulnerabilities of the current global pharma supply chain and exposed the glaring necessity for an alternative to Chinese supplies. India has a chance to fill this void, however, there is a significant gap between this strategic goal and the realities of the pharma industry in the country.

If India is indeed willing to become a global pharma powerhouse, having full control on the availability of raw materials and APIs is of paramount importance. The COVID-19 pandemic has exposed India's over-the-board reliance on the imports of raw materials despite the fact that the country manufactures more than 500 APIs and its API industry is the third largest in the world.

TRUMP CARDS

- COST ADVANTAGE
- HIGH EXPORTS
- SKILLED MANPOWER
- RISING R&D SPENDING
- FAVOURABLE GOVERNMENT SUPPORT
- POTENTIAL OF COVID VACCINE MASS PRODUCTION

ISSUES

- HIGH IMPORTS OF RAW MATERIAL
- OVER DEPENDENCE ON
- PARTICULAR COUNTRIES
- QUALITY ISSUES
- COMPLEXITY IN SUPPLY CHAIN

INDIA HAS THE THIRD LARGEST ACTIVE PHARMACEUTICAL INGREDIENTS INDUSTRY IN THE WORLD

The good news is that a lot of work is in progress to reduce the dependency on imports and to ensure the creation of large clusters of API industry in India. In March 2020, the Indian government announced a US 140mn package, involving support for three bulk drugs parks as well as the manufacturing of 53 priority APIs as part of the efforts to reduce dependency on imports.

On the quality front, currently there exists a gap between the requirements of global regulatory agencies and those of domestic regulatory agencies. To tap into the opportunity of becoming a global pharma supplier, India has to work on harmonising these requirements. ISI

4 INDIAN COMPANIES ARE AMONG THE TOP 10 GLOBAL GENERIC PHARMA COMPANIES

EXPECT THE BEST, PLAN FOR THE WORST

HOMO POSTPANDEMICUS' PERSONAL FINANCIAL PLANNING

Rosita D'Cunha, Researcher, Southeast Asia

In our minds, 2020 will forever be the year of COVID-19, a disease of unprecedented magnitude and innumerable repercussions. For the Association of Southeast Asian Nations (ASEAN) region, where households are among the most indebted in the world, the disease highlighted the necessary precedence of good financial planning - comprising savings and insurance - over immediate consumption. COVID-19 also acted as a catalyst for an almost overnight and universal adoption of technology-assisted financial transactions, a goal which governments in the region have been aiming for, but have not been able to achieve for years.

COVID-19 HIGHLIGHTS IMPORTANCE OF FINANCIAL PLANNING

PANDEMIC JUMPSTARTS PAYMENT DIGITALISATION

Apart from payments, the nationwide lockdowns enforced in an effort to fight the spread of the pandemic helped entrench deeper the use of technology for purposes such as work from home, learning, financial management and online shopping. The sudden surfacing of many options for financial management made the vast majority of the population realise that, out of modesty of funds or immodesty of consumption, they had not prepared for a contingency of this scale, despite having successfully survived financial crises in the past.

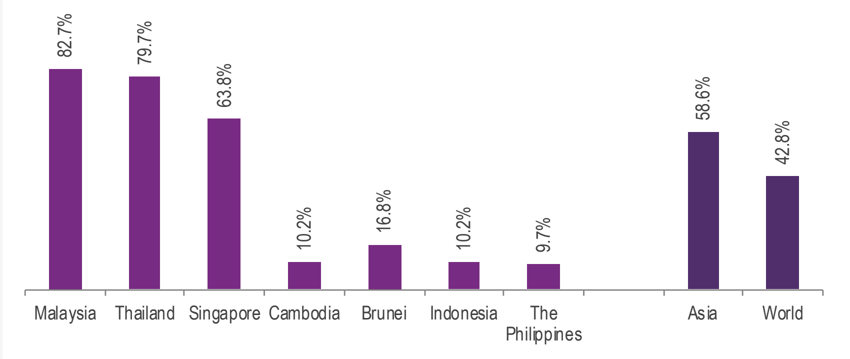
Financial Discipline for Financial Well-Being

This new awareness has also brought to the fore the validity of financial truisms that can be blithely disregarded at times of global economic prosperity. For instance, these are the necessity of having a good credit score so as to be eligible for financing at times of emergency, and of having rock-solid financial discipline assuring financial wellbeing. In the short-term, this is likely to reduce discretionary spending which is one of the main causes of financial distress for households. Likely consequences might range from buying smaller packages of food and cleaning/personal care items, putting off big-ticket purchases such as automobiles, giving up most travel, entertainment and recreation, and investing more in savings-cum-health insurance financial products that are yet to reach their full potential in the region.

Emergency Funds - More Important Than Ever

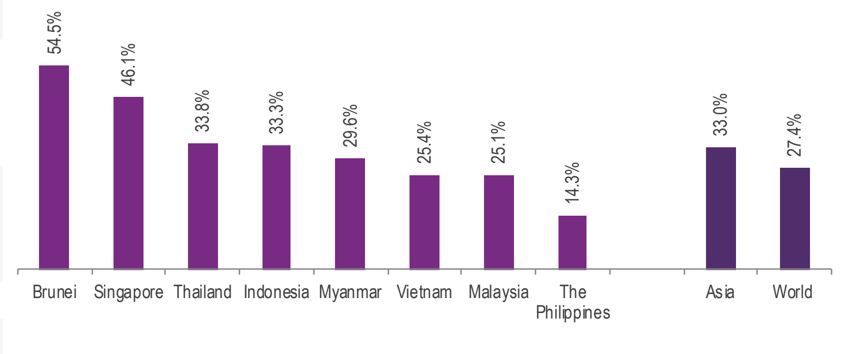
Prior to the COVID-19 crisis, savings in countries such as Malaysia and Thailand have generally been on a downward trajectory and debt was on the rise, on account of increasing consumerism and a low interest rate environment. In a reality which reduces the attractiveness of savings and encourages spending, any financial emergency was expected to be met through a loan or a credit card. However, the COVID-19 pandemic has completely busted the myth of the non-importance of savings because it has brought about an unanticipated disruption in the income source of many, thus making them ineligible for a loan. This reality is particularly harsh in the ASEAN region where social security is inadequate or non-existent, and health insurance coverage is neglected. Consequently, in the short-term at least, COVID-19 as an income disruptor is likely to affect the liquidity of banks, making them the repositories of household savings but limiting their possibility to extend consumer loans.

Household Debt, % of GDP, 2019



Source: CEIC, National Statistics Offices

Gross Domestic Savings, % of GDP, 2019



Source: CEIC, National Statistics Offices

Limited Social Security Highlights Need for Private Action

ASEAN countries allocate a relatively small share, i.e. 6% of GDP, towards social protection programmes as compared to 25% for Western Europe and 12.5% for Latin America, thus highlighting the inadequate support from the governments in the region, the OECD said in a policy insight titled Enterprise Policy Responses to COVID-19 in ASEAN. While governments all over the world have stretched their resources to support the masses due to the unprecedented nature of the current crisis, in Asia, with the exception of Malaysia, the stimuli in countries such as India, Vietnam, the Philippines, Indonesia, and to some extent Thailand, have been widely inadequate. What is more, the vast informal economy in the ASEAN region means that the policy support measures announced may in effect be inaccessible.

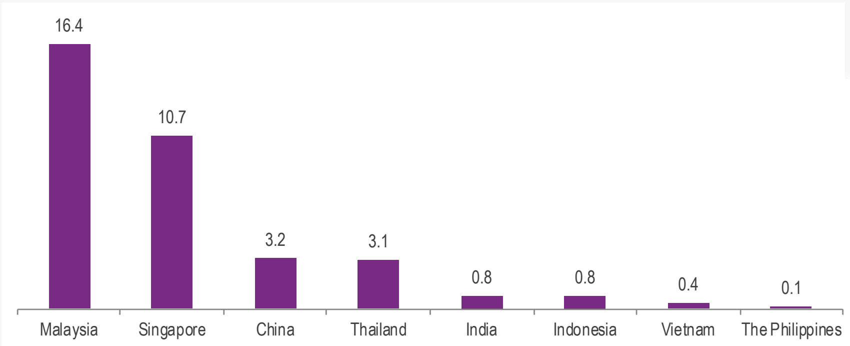
INFORMAL ECONOMY MAKES SUPPORT MEASURES INACCESSIBLE

This unfortunate situation highlights all the more the paramount importance savings are likely to play in post-COVID-19 ASEAN.

6% OF GDP

Allocated for social programmes in ASEAN

Government Fiscal Stimulus Pledges in Selected Asian Countries, % of GDP

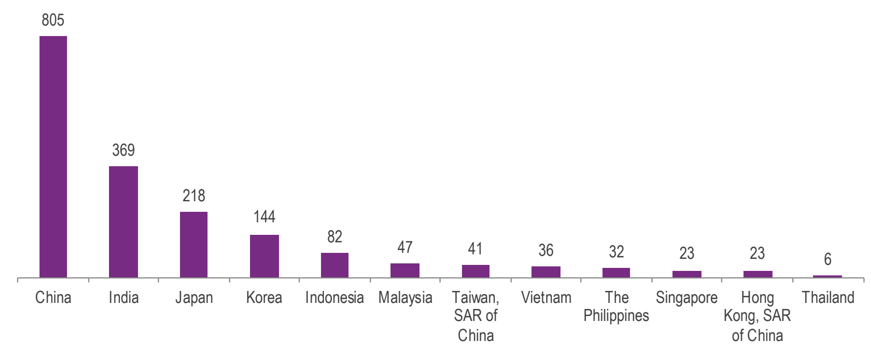


Source: L.E.K. Research and Analysis, Government Press Releases, Aseanbriefing

Health and Medical Insurance – The Next Big Thing

In the ASEAN region, health insurance is often tied to employment and hence having a personal medical insurance plan is often neglected. However, the coverage of the employment-related health insurance can be inadequate, and it is unfortunately lost with the termination of the labour contract. The COVID-19 pandemic has thus helped reinforce another principle of financially provident behaviour, namely that it is important to have personal health insurance to cover unforeseen medical exigencies and provide access to private healthcare. Government spending on healthcare in Indonesia, Malaysia, Philippines and Vietnam varied from 1.1% to 3.8% of GDP in 2019. Despite it being higher for Singapore and Thailand at 4.9% and 3.8% of the GDP, respectively, it was still lower than the global average of 6%. High out-of-pocket medical expenses as a share of total medical expenses can cause substantial financial distress. It amounted to 53% for Philippines, 37.9% for Malaysia, 34.6% for Indonesia, 32.1% for Singapore and 11.1% for Thailand in 2017, highlighting the insurance gap.

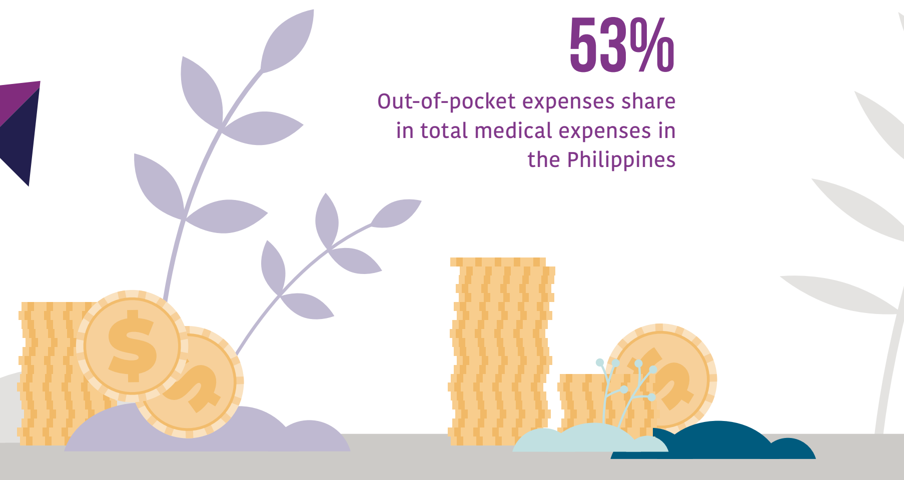
Chart 4. Health Protection Gap in Asia, USD bn, 2017



Source: Swiss Re Institute

53%

Out-of-pocket expenses share in total medical expenses in the Philippines



Fast-Paced Digitalisation - a Boon for Personal Finance

China became Asia's leader in contactless payments in the aftermath of the 2003 Severe Acute Respiratory Syndrome (SARS) epidemic, with the introduction of online payment systems such as Alipay. As of 2020, the QR code payment mode, where payment is made by scanning a QR code from a mobile app, is the leading payment mode in the country. India commenced its digital journey in 2016, when demonetisation forced people to opt for alternative modes of payment. Demonetisation, which withdrew some 90% of the cash in circulation, resulted in cash shortage and higher use of payment technology for everyday transactions.

In a similar way, the COVID-19 pandemic has propelled the adoption of contactless payments in the ASEAN region. Since the beginning of the pandemic, the usage of cash has declined by 64% in Malaysia and the Philippines and 59% in Thailand. The Philippines has been slow to adopt electronic payments, but since the start of the COVID-19 pandemic, the country has seen a surge in the use of mobile and e-wallets. The CEO of e-payment company TendoPay has predicted that the country would skip the phase of credit cards altogether and e-commerce would be the key driver. In May, 2020, G-Cash, the biggest e-payment platform in the Philippines, reported an eight-fold increase in transactions as compared to the previous year. These emerging trends across the region in response to restrictions imposed by the pandemic will become the 'new normal' and are likely to stay.

A report published by Facebook and Bain & Company and titled Digital Consumers of Tomorrow, Here Today studies how fast paced the shift to the online economy has been. A prediction in 2019 estimated that Southeast Asia would have 310mn digital consumers by 2025, and now it is estimated that his milestone will be surpassed by the end of 2020 alone. Financial institutions have also risen to the challenge by creating digital solutions eliminating the need for physical transactions. For example, Indian insurance companies have enabled the online purchasing of insurance where prospective clients upload all required documents and pay though a digital banking platform. In the Philippines, insurance companies have forged partnerships with e-commerce firms to generate online offerings.

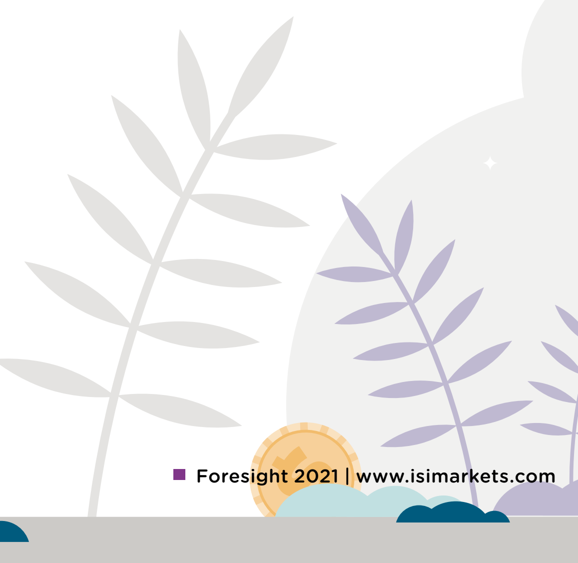
A major advantage of technology-aided cashless transactions is that they aid budgeting by making tracking payments and expenses easier. All these benefits suggest that the digital and contactless modes of payment are not a fad but a reality that is here to stay.

CASHLESS TRANSACTIONS BOOST TRANSPARENCY

The Way Ahead

The COVID-19 pandemic has brought along much pain and death. However, it has also highlighted the distinction between the important and the superfluous in many aspects of our economic, financial, and social lives. The reality of job losses and uncertain incomes has helped bring to the fore the traditional values of saving and financial planning, and has affirmed the importance of medical and other insurance, often disregarded in the pursuit of higher consumption. In the post-COVID-19 reality, people in the ASEAN region are likely to start laying their financial eggs in more than one (digital) basket, in an effort to provide for a more predictable future. ISI

CASH USE IN MALAYSIA DOWN BY 64% SINCE START OF PANDEMIC



Learning Lessons
Southeast Asia's COVID Experience

U-Ming Lee, Researcher, Southeast Asia

The first known case of COVID-19 recorded outside China was in Thailand in January 2020, when a Chinese tourist from Wuhan tested positive for the virus.Southeast Asia's reliance on international tourists, especially those from China, began to increasingly look like a burden for the region when most of these countries started recording COVID-19 cases in their tourist population. These initial cases provided the world with some inkling that humanity was dealing with a viral outbreak with pandemic potential.

In this article, we take the opportunity to briefly review some of the lessons learned on the anniversary of the emergence of the first COVID-19 case in Wuhan, in November 2019. The availability and sophistication of healthcare systems and public healthcare governance differ considerably between countries. So, we think that Southeast Asia is a useful microcosm to understand which of the various strategies applied to deal with the pandemic have been successful.

JAN 2020
First known COVID-19 case outside China

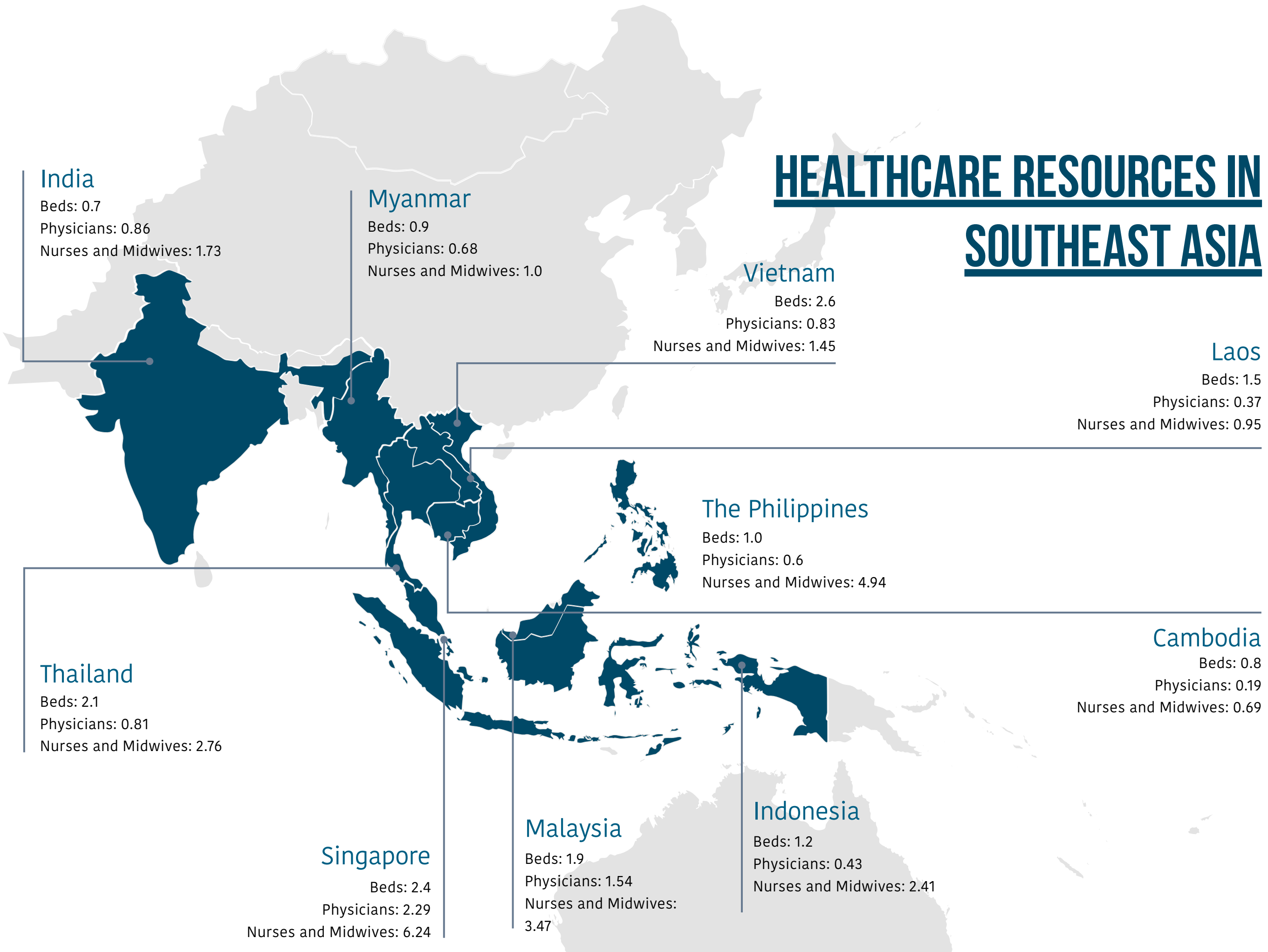
EMIS Insights' analysis into the ability of Southeast Asian nations' ability to control their respective outbreaks reveals the two major factors:

1. Central government control over public healthcare has been key to controlling the COVID-19 epidemic in Southeast Asia.
2. Extensive migration, both internationally and internally, severely taxed governments' ability to curtail the COVID-19 outbreak.

GOVERNMENT-CONTROLLED PUBLIC HEALTHCARE KEY TO OUTBREAK CONTROL

One thing that is common for Southeast Asian countries is that healthcare remains in inadequate supply throughout most of the region. Although the availability of healthcare resources differs considerably between countries, in general, the Southeast Asian countries tend to have fewer healthcare resources available to them compared with the global average.

HEALTHCARE RESOURCES IN SOUTHEAST ASIA



A notable difference between these countries is the degree to which their healthcare systems have been decentralised.

Source: World Bank

Who's in Charge?

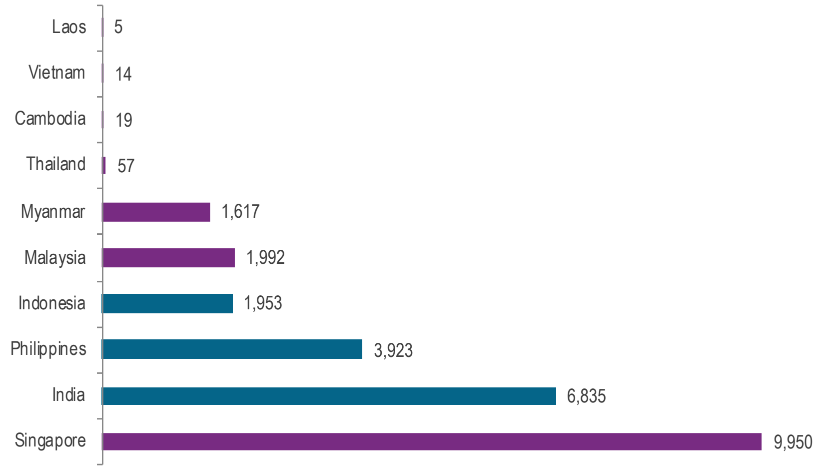
Most of the Southeast Asian countries achieved their independence from colonial powers in the 20th century, except for Thailand. Healthcare decentralisation, in which responsibility for healthcare policy formation and delivery is devolved to local government units, has thus been promoted as a way of rapidly building modern healthcare systems to serve the needs of diverse populations.

Despite these efforts, healthcare decentralisation has been most advanced in the Philippines and Indonesia, both of which grappled with the impact of authoritarian regimes under Presidents Marcos and Soeharto, respectively. Under these regimes, government authority was concentrated in the hands of the president, and these regimes' overthrow stirred up a desire to devolve powers away from the centre. Primary healthcare services delivery in India is mainly devolved to the individual states and Union Territories. Still, significant COVID-19 testing capacity is centralised in a few key institutes.

One year after COVID-19 reared its ugly head, the evidence from Southeast Asia suggests that decentralisation has hampered efforts to control the disease's spread. The countries with the most decentralised healthcare systems - India, the Philippines and Indonesia - have tended to show the highest COVID-19 incidence rates. Notably, the healthcare systems of these three countries are under-resourced by most measures compared with the global average. These findings imply that that the process of healthcare decentralisation in these developing countries diminishes the capacity of their governments to coordinate the efforts needed to curb COVID-19's spread.

HEALTHCARE DECENTRALISATION HAMPERS DISEASE CONTROL

COVID-19 Cases in Southeast Asia, per million population (as of Nov 30, 2020)



Source: CB Insights

Nevertheless, Malaysia and Singapore appear to be outliers as both countries have experienced some of the most prevalent COVID-19 outbreaks in the region despite having the region's most advanced healthcare systems. The prevalence of migration is a crucial factor in influencing the government's ability to control the course of the disease.

Migration and Health

Southeast Asia is a region in transition, with millions of people moving from rural to urban areas, or between countries, to improve their lot in life. In better times, migration has helped to reduce poverty in Southeast Asia's populations. However, throughout this pandemic, the presence of a significant migrant population has complicated governments' efforts to control the spread of COVID-19.

Firstly, the mere announcement of lockdown measures led to a dramatic reverse of migratory flows - from urban to rural areas. In India, hundreds of thousands of people fled their jobs in the city - some on foot - when Prime Minister Narendra Modi announced a 21-day nationwide lockdown on March 24, 2020. Similarly, when in mid-March the Philippines announced lockdown measures on its capital, Metro Manila, there was an exodus from the capital to the other provinces in the Philippines.

LOCKDOWN MEASURES REVERSE MIGRATORY FLOWS

In Singapore's case, international migration has contributed to the country's high COVID-19 incidence, at 9,895 cases per million. Singapore's 5.1mn-strong population includes 1.3mn foreign workers. Due to the expensive cost of living in the city-state, many of Singapore's lower-paid foreign workers lived in densely populated worker dormitories, which proved to be hotbeds of COVID-19 transmission. In this context, Singapore's strategy to control the outbreak centred on separating these foreign workers from the rest of the population, and employing targeted strategies for both segments to reduce the incidence and the severity of the outbreak. As at the time of writing (early November 2020), Singapore has managed to control its COVID-19 outbreak, with the number of new daily cases in the single digits.

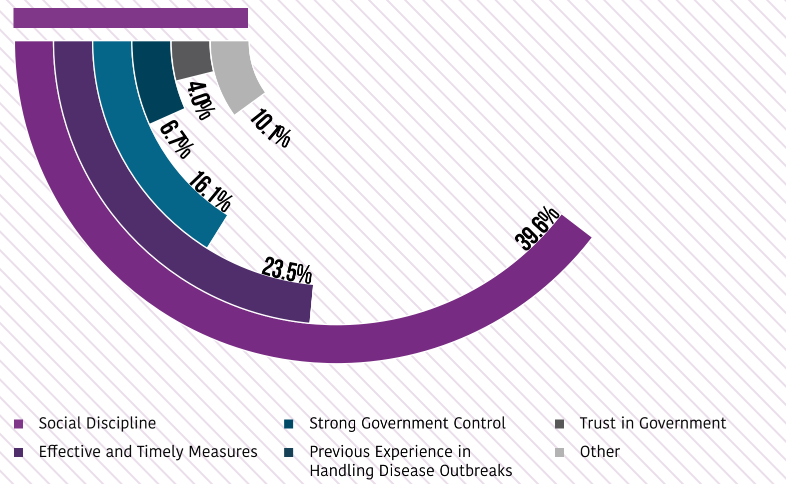
A high prevalence of migration is also an essential contributor to Malaysia's outsized COVID-19 incidence despite the country's highly centralised healthcare system. Nearly half of all Malaysia's cases are found in a single state - Sabah - on the northern portion of Borneo. Sabah shares a land border with the North Kalimantan Province in Indonesia and is geographically proximate to the Bangsamoro Autonomous Region in Muslim Mindanao in the Philippines, and immigrants from these countries -- legal or otherwise -- comprise up to a third of Sabah's 3.9 million people. The loosely controlled movement of people between these regions has undermined the Malaysian Ministry of Health's ability to conduct contact tracing activities in Sabah. This limitation had contributed to a third COVID-19 wave when cases from Sabah started spreading to the rest of the country after the conclusion of Sabah's state elections in September 2020.

Wrapping Up

Southeast Asia has been relatively successful in its efforts to contain COVID-19, despite many countries in the region having under-resourced healthcare systems. However, Southeast Asia's experience shows how deficiencies in other government capabilities – notably, immigration and inter-departmental communications – can seriously undermine public healthcare systems' ability to contain the spread of COVID-19. The takeaway lesson from this experience is that it will take a whole-of-government response, combined with societal trust to comply with the tough measures imposed on broad swathes of the population, to bring these outbreaks under control. ISI

ISI FORESIGHT SURVEY

In your opinion, what factors were behind the generally successful handling of the pandemic in Asia Pacific countries?



RATTLING SOUTHEAST ASIA'S SUPPLY CHAIN

Aaron Dayle Cruz, Researcher, Southeast Asia

SOUTHEAST ASIA TO PLAY PIVOTAL ROLE IN SUPPLY CHAINS OF TOMORROW

Southeast Asia had been through many challenging times – the 1997 Asian financial crisis, the 2008 global financial crisis, the 2002 SARS outbreak and numerous natural disasters to name but a few – but the region has always been able to recover from these large-scale crises and even to tally promising growth rates shortly after. However, the magnitude of COVID-19's impact seems to be unprecedented, with the IMF even describing it as a "crisis like no other". Supply chains were particularly vulnerable to the ill effects of the pandemic, given how interconnected the region's trade flows are. The pandemic has proved how much the global supply chain is dependent on China, prompting companies around the world to rethink strategies and reshore value chains to other destinations. Rising geopolitical tensions and tariffs introduced during the US-China trade war have already pushed many manufacturers to actively plan ways of reducing their dependence on China, a trend that has been accelerated by the COVID-19 outbreak. Competitive costs, proximity to China and rising regional growth are positioning Southeast Asia in a good place to play a bigger role in the supply chains of tomorrow.

02 Asia

Reconnecting Broken Chains

The pandemic exposed not only the extent to which multinationals depend on China but also how much most of the Southeast Asian countries rely on their big neighbour for intermediate goods and migrant workers. Indonesia, for instance, has about 30,000 Chinese workers employed in various plants and businesses in the country. What is more, there are companies entirely relying on Chinese workers. An Indonesian nickel and zinc smelter faced huge losses during the outbreak in China, when strict lockdowns and people movement restrictions prevented migrant workers from returning to Indonesia, since only Chinese employees were trained to operate the ore smelters, This Week in Asia reported in February 2020. A Vietnamese firm reported that it could not export goods or import raw materials as the majority of the electronic components it uses in manufacturing come from China. In the Philippines, the total volume of containers loaded with raw materials coming from China dropped by over 60% in February 2020.

Yet, the question remains to what extent countries can actually diversify their sourcing, given that China is the top supplier of intermediate goods for many of them. Vietnam sources half of its imports from China, South Korea and Japan; China accounts for over 20% of Malaysia's imports, and nearly half of South Korea's imports come from China, Japan and the US.

Given the impact of the pandemic on the supply chains, Baker McKenzie reports that many companies will likely reconsider their strategies, especially in terms of diversification and digitalisation. Manufacturers who are reliant on one or few sources of raw materials or intermediate goods have realised the importance of diversification, which could have minimised disruptions, and of digitalisation, which could have helped quickly identify potential bottlenecks and risks in the entire supply chain. In addition to diversification, however, manufacturers may also resort to ending outsourcing agreements in an effort to be more in control of their supply chain, thus contributing to deglobalisation.

Trade War – Opportunity or Threat?

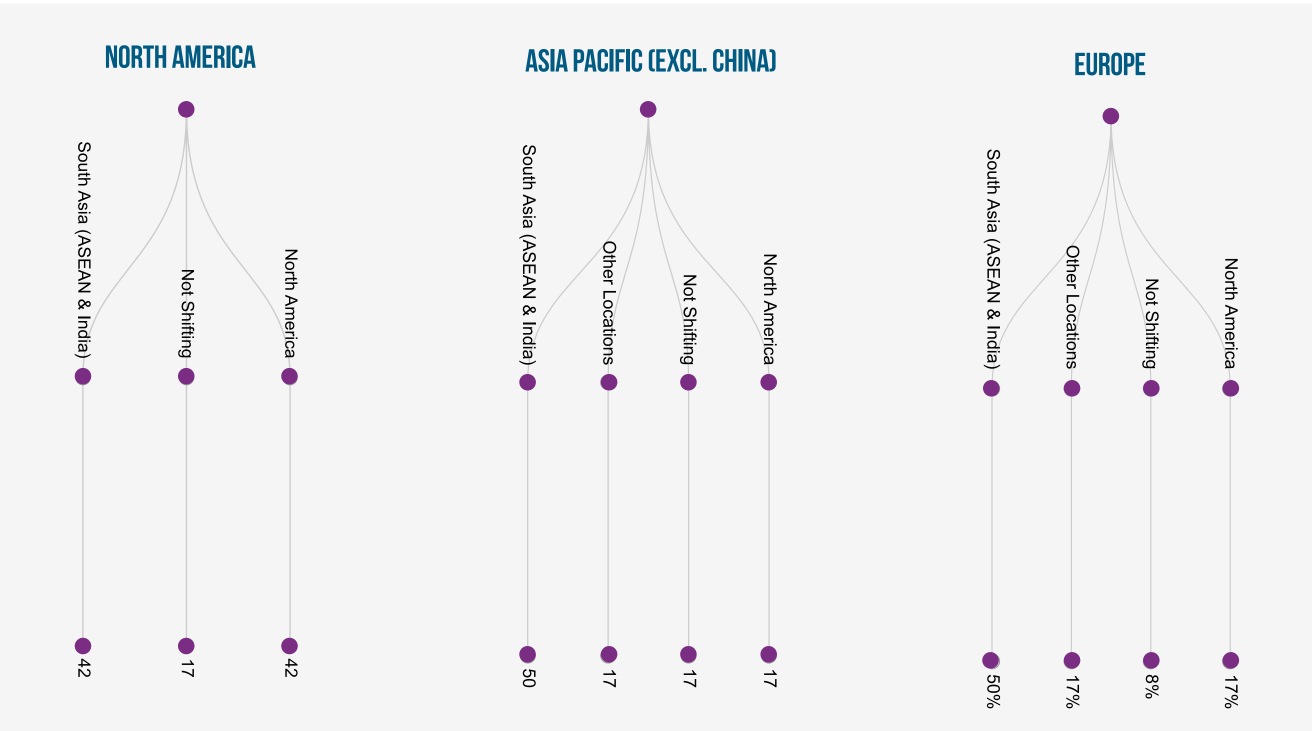
A few years before the pandemic hit the region, the trade war between the US and China had already started causing disruptions to the supply chains. China is a major export destination for many intermediate goods manufactured in Southeast Asia. These are used as inputs for final goods assembled in China and then exported to other countries including the US. This implies that any trade-related disruption between China and the US has repercussions for exporting firms in Southeast Asia.

US-CHINA TRADE WAR DISRUPTED SUPPLY CHAINS YEARS BEFORE COVID-19

However, apart from a cause of disruption, the US-China trade war can be viewed as an opportunity too. With protectionist policies in place, the investment flows can divert from China to Southeast Asia, especially when firms believe that the trade conflict will be a long-standing one. In fact, even before the trade war, China's increasing labour costs and tougher regulations have already made Southeast Asia a viable prospect for relocation of manufacturing facilities.

A survey published by BofA Global Research in February 2020 suggests that Southeast Asia will be one of the biggest beneficiaries of the realignment of supply chains, as companies perceive it to be a viable alternative to China. Most companies have suffered supply chain disruptions during the pandemic and more and more are now widening the scope of their reshoring plans.

Companies' Preferred Choice for Relocation



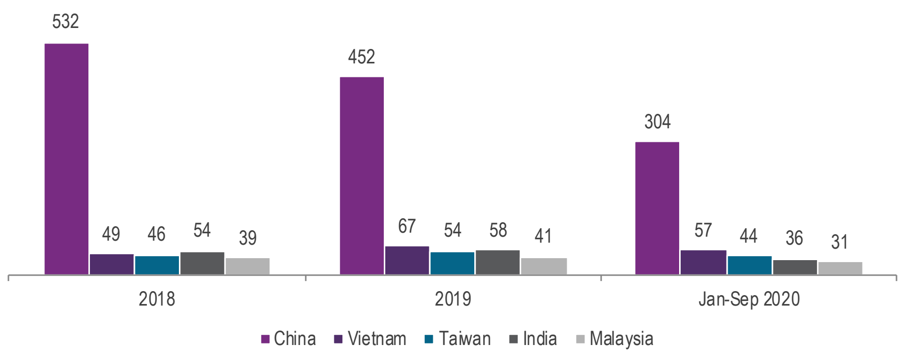
Source: BofA Global Research

In 2019, more than 50 multinational companies including Nintendo and Apple, relocated their production out of China to avoid the 25% trade tariffs that have been slapped on over USD 200bn worth of Chinese imports to the US since 2017, according to the Nikkei Asian Review.

50 MULTINATIONALS RELOCATE PRODUCTION OUT OF CHINA IN 2019

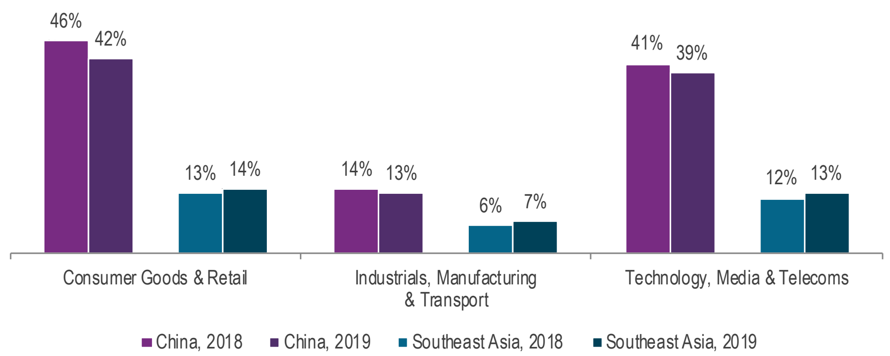
Trial production of Apple's AirPods has already started in Vietnam and Dell and HP are considering shifting 30% of their notebook production from China to Southeast Asia and elsewhere. Other multinationals to follow suit include Google, Microsoft, Amazon, Nintendo and Sony. The spill-over effects of this trend are already visible in the US' external trade with US imports from China on a steady decline, while imports from Vietnam, India and Malaysia have been on the rise. Additionally, figures from Silk Road Associates showed that between 2018 and 2019 China's global export market share declined, while that of Southeast Asia increased.

US Imports from Selected Asian Countries, USDbn



Source: US Census Bureau

China and Southeast Asia Global Export Market Shares



Source: Silk Road Associates, Baker McKenzie

SOUTHEAST ASIA SHOULD IMPROVE CAPACITY, HUMAN CAPITAL, INFRASTRUCTURE, DIGITAL INNOVATIONS

The textile, consumer goods, and automotive industries have seen probably the most significant relocation from China with Vietnam, Cambodia, and Bangladesh being the biggest beneficiaries. Thailand, Malaysia and India are also poised to benefit from the US-China trade war, especially in the automotive and electronics industry. Taiwan's electronic manufacturers Foxconn, Quanta and Pegatron have been moving production out of China to new plants in Taiwan, Vietnam and India in a bid to reduce costs and avoid US tariffs. In August 2020, Foxconn – one of the largest electronics contract manufacturer that employs more than a million people in China assembling iPhones for Apple, servers for Dell and electronic games for Nintendo – said it plans to move more of its production outside China with India, Southeast Asia or the Americas as possible destinations.

To take full advantage of the opportunities, Southeast Asian countries must urgently and significantly improve their production capacity and complement it with increased competitiveness through investments in human capital, infrastructure, and digital innovations. Even so, China will undoubtedly remain the region's economic heavyweight and preferred manufacturing hub since Southeast Asian countries simply lack the infrastructure bandwidth to compete with China, which rebounded from the COVID-19 crisis much more quickly than other countries.

Rethinking Supply Chains in Southeast Asia

The common denominator for the COVID-19 outbreak and the US-China trade war is that they both triggered a rethinking of the supply chain systems of many Southeast Asian manufacturers, especially of those who are heavily reliant on raw material imports and on demand from other countries. Diversification is going to be a key to the future of supply chains as Southeast Asian manufacturers will try to diversify their sources of raw materials. Manufacturers might also opt for nearshoring, which would shorten supply chains and reduce risks. If these trends remain resilient in the long term, they might put the start of a fully-fledged deglobalisation process. Digitalisation is another key factor to better identify bottlenecks and risks in the entire supply chain. The widespread adoption of technology is going to be important especially as Southeast Asia plans to attract more investors and to make the region a manufacturing powerhouse. ISI

14%

Southeast Asia's Global Export Share in Consumer Goods

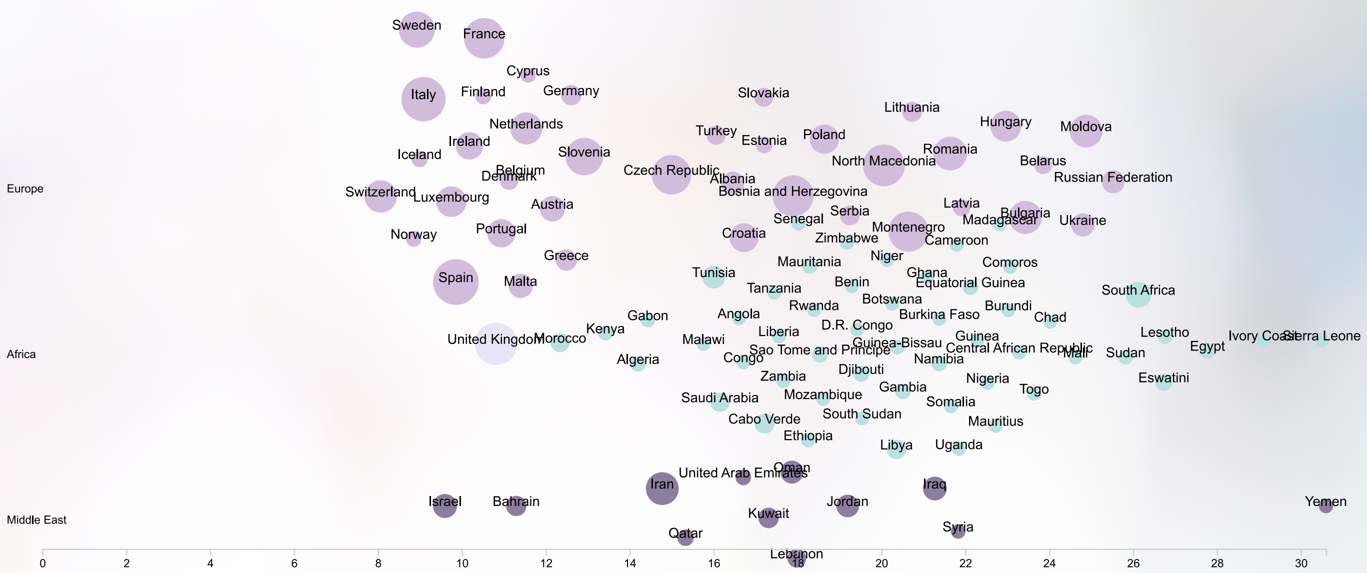
03

EMEA

03 EMEA

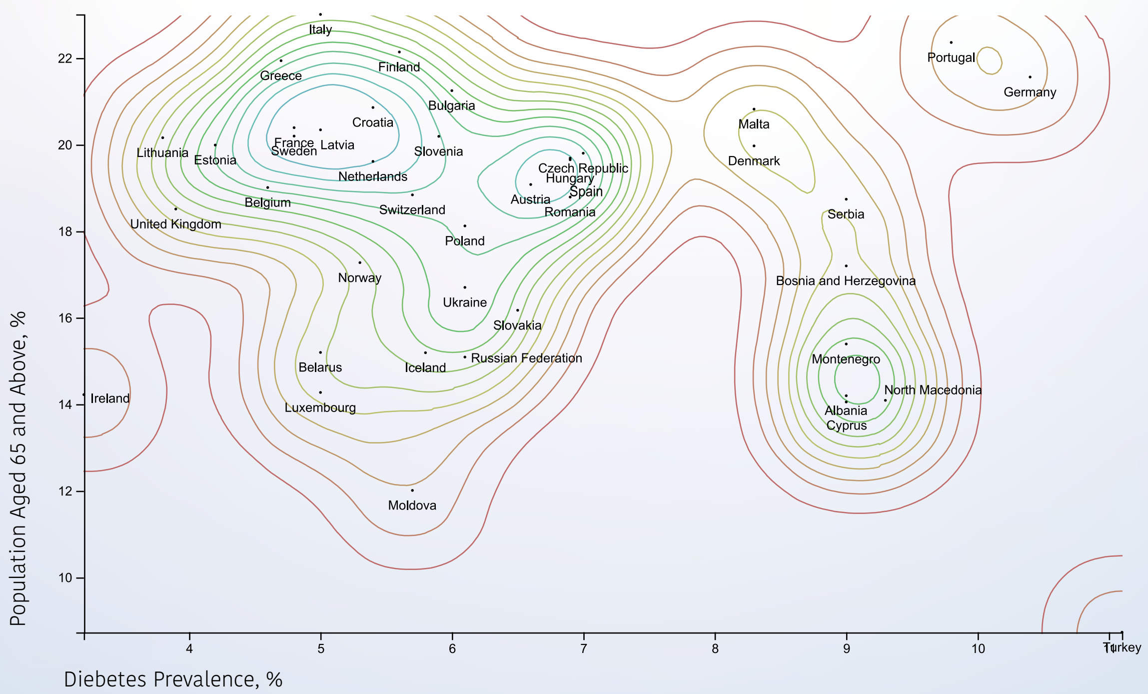
IN SICKNESS AND IN HEALTH

COVID-19 RELATED DEATHS AND PRE-EXISTING CONDITIONS



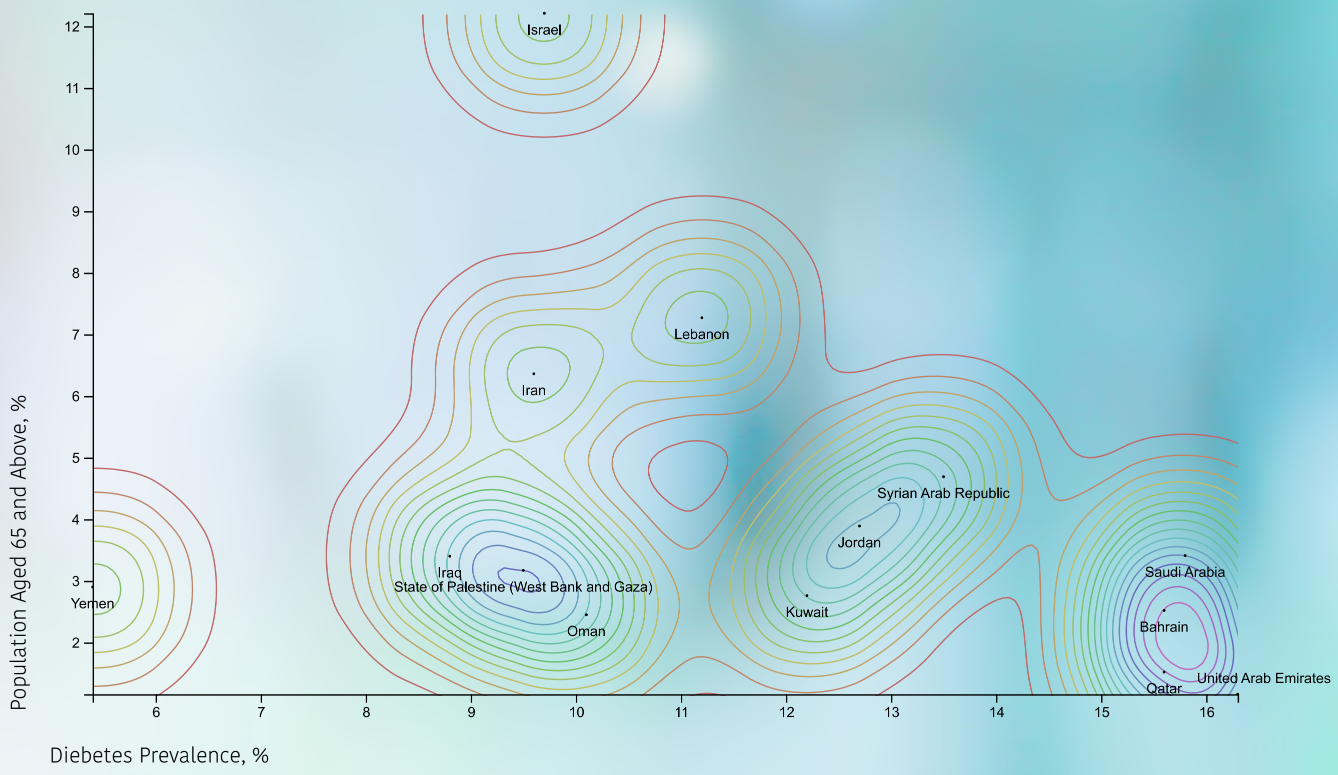
Pre-existing conditions, per 100 000 people
Note: Bubble size reflects COVID-19 related deaths per 1mn people

HEALTH RISK FACTORS IN EUROPE

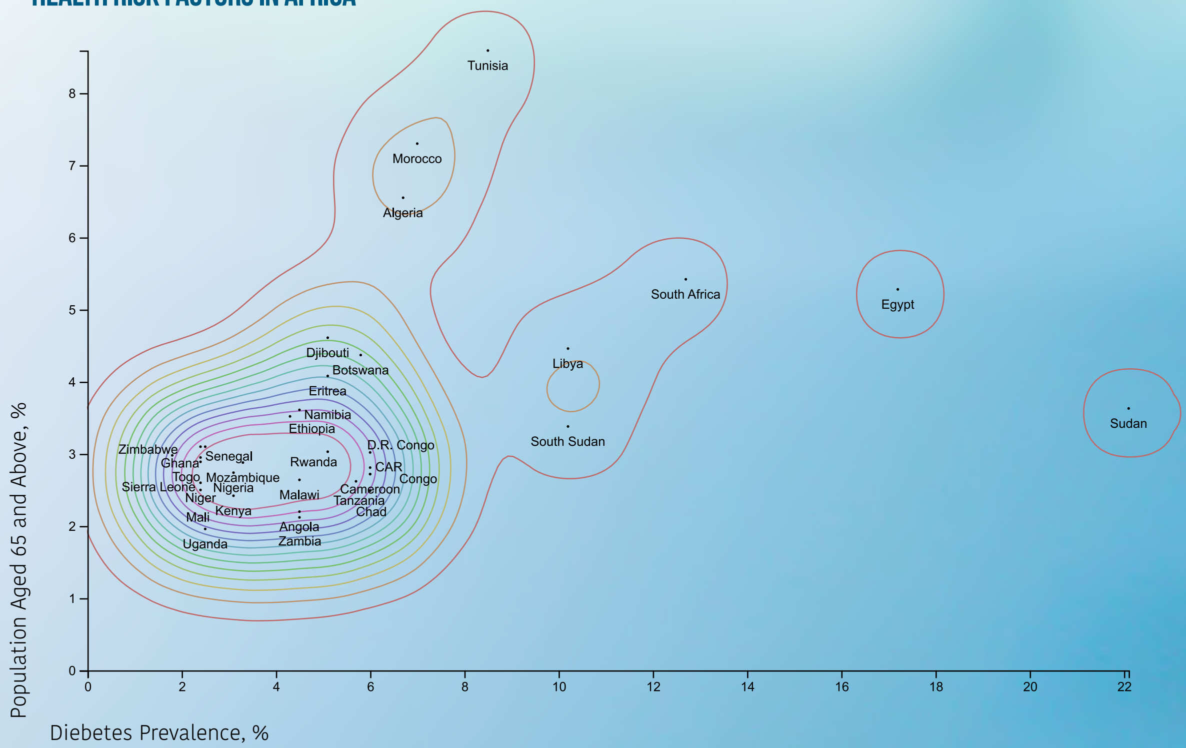


Source: CEIC, World Bank

HEALTH RISK FACTORS IN THE MIDDLE EAST



HEALTH RISK FACTORS IN AFRICA



RECOVERY ON HOLD

Antonia Dobreva, Researcher, EMEA

When governments across Europe started to ease lockdown measures in mid-May 2020, allowing businesses to re-open and people to travel, hopes that life might go back to normal were if not high then at least alive. And for a while things did seem to get better. The number of new COVID-19 cases had been declining and countries on the continent seemed to have succeeded in keeping the pandemic under control.

After the severe shock Europe's economy suffered in the first half of the year, activity rebounded in the third quarter as the continent profited from a summer period with few social restrictions. The EU's GDP expanded by 11.6% in the third quarter of 2020 compared to the previous three months. The increase – the sharpest-ever on record – came after an 11.4% q/q contraction in the second quarter. The GDP growth for the eurozone was even stronger – a record 12.6% q/q rise in July-September 2020 that followed a drop of 11.8% q/q in April-June.

Dashing Hopes

However, with the arrival of autumn a second wave engulfed Europe with a large number of countries reporting a spike in COVID-19 cases. By late-October the vast majority of European countries were declaring more cases each day than they were during the first wave earlier in 2020. Italy, Spain, France, Germany, Poland, the Netherlands, Croatia and Slovakia were among the many that were reporting record new cases for days, raising fears that Europe is running out of chances to get a grip on the COVID-19 pandemic. To reign in the resurgence of infections, governments responded by bringing back measures that had been relaxed over the summer – curfews, travel restrictions, closure of bars and restaurants, and tightening of mask-wearing rules were among the most widely introduced measures.

Hopes that the summer's fragile recovery would gather momentum have been dashed by fears of what the winter might bring. That pessimism is shared by the European Commission. When in early November the EU's executive arm announced its regular economic forecast for the 27-nation bloc and the 19 countries sharing the euro currency it said that the rebound expected in 2021 will be smaller than initially thought and that the EU's economy would not reach pre-pandemic levels until 2023

EU ECONOMY NOT TO REACH PRE-PANDEMIC LEVELS UNTIL 2023

The Autumn 2020 Economic Forecast sees growth of just 4.2% for the eurozone in 2021, down from the earlier forecast of 6.1% predicted in July 2020.

The tentative recovery would take place after an unprecedented 7.8% recession forecast for 2020. The 2021 forecast for the EU economy was also lowered from 5.8% in July to 4.1%. Growth would follow a 7.4% contraction in 2020. The mid-term outlook is also a bit gloomy with growth both for the eurozone and the EU seen easing to 3%. The commission also warns that the forecasts are subject to an extremely high degree of uncertainty given the unpredictability surrounding the spread of the virus. Spain, Italy, France and Portugal will be the hardest hit developed EU economies with their GDP expected to shrink by over 9% in 2020. Of the new EU members, Croatia, Slovakia and Slovenia are the ones to witness the sharpest contraction in economic activity in 2020.

COVID-19 has put the EU's labour market under a severe strain but the decline in employment was much more contained than the drop in economic activity thanks to a number of ambitious policy measures such as short-time work schemes and other support policies that helped avoid mass lay-offs and large income losses.

EU MANAGED TO CONTAIN EMPLOYMENT DROP WITH POLICY MEASURES

However, the pandemic will take a huge toll on public finances, according to the European Commission. The Euro Area governments are expected to go deeper into the red than ever before, accumulating an aggregated budget deficit of nearly EUR 1bn, or 8.8% of the GDP in 2020. The gap is said to narrow to 6.4% in 2021 and to 4.7% in 2022.

On the upside, the progress in the development of vaccines against COVID-19 raises hopes for a quicker return to a more normal economic situation. By late-November, the European Commission had approved six contracts with pharmaceutical companies for the purchase of COVID-19 vaccines. Another supportive factor is the Next Generation EU – the coronavirus recovery package - that will provide a much-anticipated strong boost to the EU economy over the next few years.

In July 2020, the leaders of the 27 EU countries agreed on the largest stimulus package ever financed through the bloc's budget at their first in-person meeting in five months. Alongside the EUR 1.1tn seven-year budget for 2021-2027, the EU approved a EUR 750bn coronavirus pandemic recovery fund, Next Generation EU, to help countries weather the painful recession triggered by the coronavirus. Next Generation EU will be composed of EUR 390bn in grants and EUR 360bn in loans. The European Commission will borrow the money from financial markets. The EU's executive arm has a triple-A credit rating, which it says will give it access to very favourable loan terms and moderate interest rates. Repayments would start after 2028, with the full amount due after 30 years. The money is intended for projects spanning 2021-2024, though absorption could be extended into 2025-2026.

The aim of the programme is to help prepare the European countries to better address any COVID-19-related challenges and also to set the stage for the long-term recovery of Europe and help in building its resilience in the face of future risks. The plan is also closely linked with the launch two new social and health programmes – the Recovery and Resilience Facility (rescEU) and EU4Health. Through the EU4Health programme the EU plans to invest EUR 9.4bn to strengthen the resilience of EU's healthcare systems and promote innovation in the healthcare sector. This new programme will also fill the gaps revealed by the crisis and ensure that the EU's healthcare systems are resilient enough to face any potential new health threats.

NEXT GENERATION EU PACKAGE TO SUPPORT THE BLOC'S ECONOMY IN THE NEXT FEW YEARS

EUR 1BN

Eurozone budget deficit in 2020

One of the biggest lessons the pandemic has taught us is how important digital technologies have been in keeping us connected to work, school and family. For that reason, the EU is accelerating investments in digital transformation.

EU TO ACCELERATE INVESTMENT IN DIGITAL TRANSFORMATION

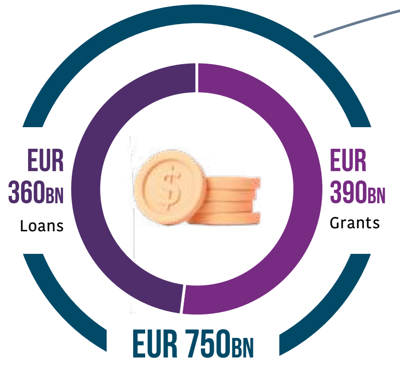
At least 20% of the funds under rescEU will be made available for digital transition, including for SMEs. These funds should help advance objectives such as fostering the development of the next generation of digital technologies, including supercomputers, quantum computing, blockchain and human-centric artificial intelligence; developing capacities in strategic digital value chains, especially microprocessors; accelerating the deployment of very high capacity and secure network infrastructures including fibre and 5G all over the EU; enhancing the EU's ability to protect itself against cyber threats; unleashing the full potential of digital technologies to achieve the EU's ambitious environmental and climate action objectives; and upgrading digital capacities in education systems.

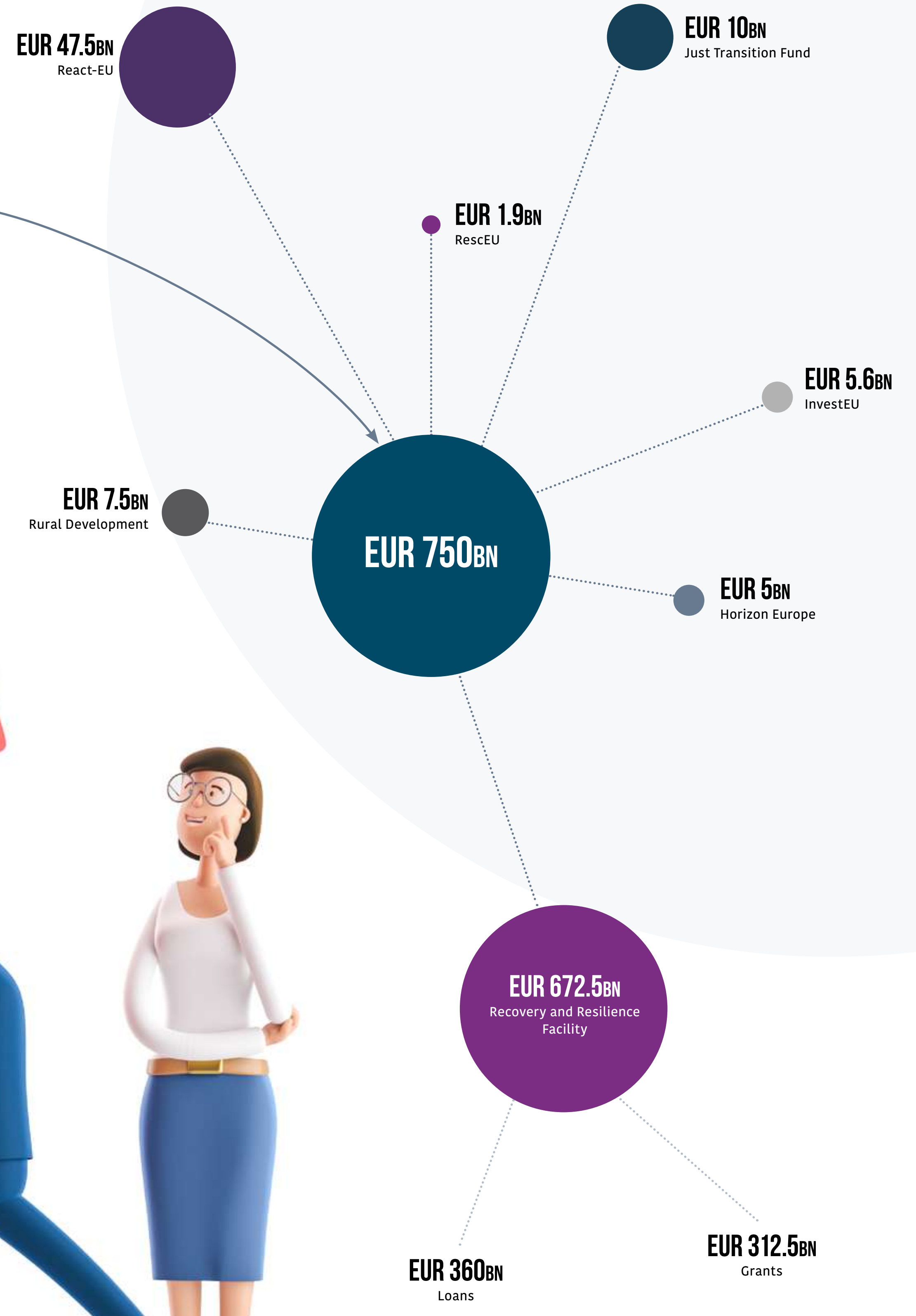
That is why the EU's increased focus on digital transformation might be the real game changer in preparing the union for future crises. ISI

NEXT GENERATION EU

COVID-19 RECOVERY PACKAGE

- Capital Raised on Financial Markets
- Repayment Period until 2058

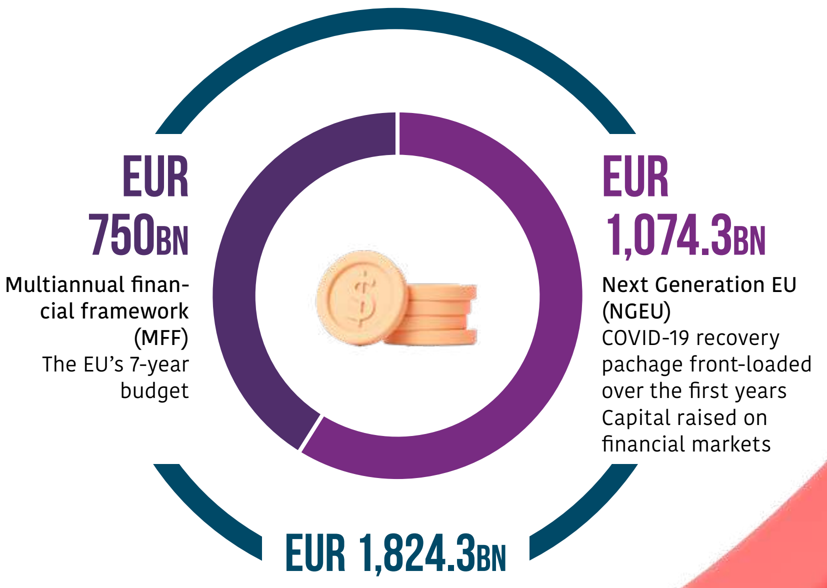




EU BUDGET 2021-2027 AND RECOVERY PLAN

EU EXPENDITURE 2021-2027

The EU recovery plan and long-term budget for 2021-2027 support the recovery from the COVID-19 pandemic and investment in the green and digital transitions.



03 EMEA

REWRITING RETAIL RULES

Malgorzata Wrzesinska, Researcher, Poland

Like in almost every country around the world, online sales in Poland surged in 2020, boosted by the COVID-19 outbreak as stay-at-home orders pushed shoppers to shift from brick-and-mortar retailers to e-stores. Even before the pandemic, brick-and-mortar retailers had been fighting a fierce battle against e-commerce players. These challenges have now been accelerated at a stunning pace. Poland's online sales are rising at a record speed and the number of new e-stores has never been this high. A clear evidence for the growing popularity of e-commerce has been the successful market debut of Poland's online retailer Allegro. Launched two decades ago as a home-grown competitor to eBay and Amazon, Allegro raised EUR 2.01bn in its October initial public offering, making it Warsaw's largest-ever listing and Europe's third largest in 2020.

ONLINE RETAILER ALLEGRO RAISES EUR 2BN IN WARSAW IPO

Online retail in Poland has been growing at a double-digit rate in recent years. Researcher PMR estimates the market at PLN 61.1bn in 2019 and forecasts a 26% annual growth for 2020, the strongest expansion in nearly a decade. High internet usage and smartphone penetration have been among the main growth engines. Figures from the EU's statistics office Eurostat show that 87% of the Polish households had internet access in 2019. The smartphone penetration rate stands at 83%. That is above Europe's average of 76% in 2019, according to data published by the mobile communications industry body GSMA.

Another important driver has been the well-developed innovative payment system in Poland that offers a variety of safe payments options. The implementation of the mobile payment standard BLIK revolutionised Poles' shopping habits. Launched in 2015, it allows smartphone users to make instant payments using a six-digit code generated in their banking app. In 2019, BLIK had 8mn users in Poland and registered a record-high of 218mn transactions. It is available in 11 banks in the country and covers over 90% of all financial institutions' clients in Poland.

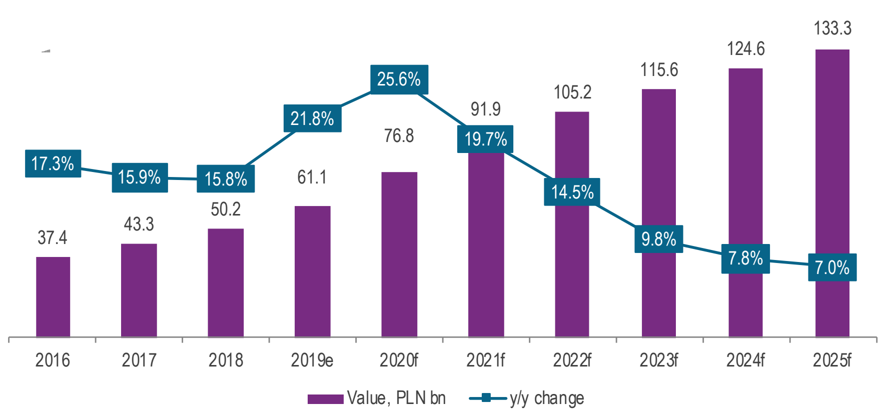
BLIK MOBILE PAYMENT STANDARD REVOLUTIONISES POLISH RETAIL

The shortage of convenient and affordable delivery options had been a major reason that impeded Poles from buying online. The undisputable game-changer was the creation of a network of parcel lockers by postal company inPost. Currently, there are 9,000 self-service parcel dispatch and collection points, open 24/7. The network allows 98% of the products ordered online to be delivered the next day. A survey by PostNord showed that Polish consumers have high expectations regarding delivery. A quarter of the respondents said they expect to receive the goods purchased online within one to two days, which is the second shortest among the 12 European countries surveyed by PostNord study.

26%

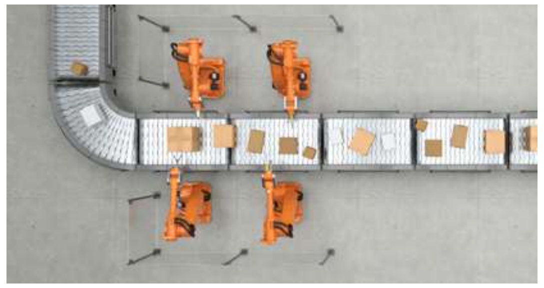
Expected annual growth of e-sales in 2020

Poland's Online Retail Sales



Source: PMR

Poles enjoy quick dispatch also due to the fact that several e-retailers, including Amazon and Zalando, have large logistics centres in Poland, thanks to the country's favourable location at the heart of Europe, the proximity to the German market, and its relatively low wage levels.



NUMBER OF E-GROCERIES IN POLAND INCREASED BY 18% FROM JANUARY 2019 TO MARCH 2020.

Undoubtedly, the introduction of the Sunday shopping ban in 2018 was one of the factors that also helped Poles' shift towards online shopping and prompted retailers to transfer their activities to the internet. At present, there are about 42,100 registered online stores, which makes Poland one of the largest, and certainly the most dynamically developing e-commerce markets in Europe. In the first half of 2020 alone, the number of e-commerce shops increased by 3,400.

42,100 REGISTERED ONLINE STORES IN POLAND

The pandemic has not only prompted people to buy more online but also to buy products they never bought before. Traditionally, apparel retail was the largest segment of the online retail sector in Poland, accounting for 25.3% of the sector's total value with e-grocery responsible for a mere 4.6% in 2018 according to Marketline. E-grocery was the least popular online retail category and a niche to be filled. The COVID-19 outbreak provided the needed impulse. The number of e-groceries increased by 18% in the period from January 2019 to March 2020. Moreover, many retail chains launched online orders and even if they were not able to quickly launch delivery options, they offered customers the option to order products online and collect them in the store or in special zones next to the stores.

The pandemic is rapidly changing customer preferences toward online channels and the longer it lasts, the more permanent this change will become. The growth trend is likely to stick in the post-pandemic world. PMR estimates that by 2025 the value of the Polish e-commerce market may reach as much as PLN 133.3bn. At nearly 11%, the share of online sales in the total retail trade in Poland is still relatively low compared to Western European countries. The large potential for growth suggests that the share may reach almost 20% by 2025, according to PMR.

RETAIL BLOOM AND GLOOM

CONSUMER CONFIDENCE AND SHOPPING IN EMERGING EUROPE IN 2020

The COVID-19 pandemic has found Emerging Europe unprepared and lacking experience. The high number of cases has put an unprecedented strain on the healthcare systems of the individual countries, pushing medical personnel to the brink of their physical and professional resilience. At the same time, the restrictions on movement and social gatherings alongside the higher government interference in all aspects of life have attacked the widely-defined European culture at its foundations. Thus, although they have been globally validated as effective in containing the spread of the coronavirus, in emerging Europe these measures were largely neglected with the onset of summer, and the attempts at their reinstallment have triggered anti-lockdown protests in many countries. Moreover, the tension induced by COVID-19 and the governments' ways of handling the pandemic, has added fuel to the fire of festering social problems, e.g. perceived violations of human rights, academic freedom, and personal data protection in the region. Further, the pandemic has turned the spotlight on the vulnerable social and financial status, alongside the ageing demographic profile, of healthcare and teaching professionals in emerging Europe.

Mail order and online retail was the biggest winner at times when most industries suffered from national movement restriction orders. In emerging Europe, the highest increase was observed in Turkey and the lowest in the Czech Republic, reflecting the low and high base for online trade in these two countries, respectively, before the COVID-19 pandemic.

RETAIL SALES VOLUME INDEX, MAIL ORDER AND ONLINE RETAIL, 2015=100

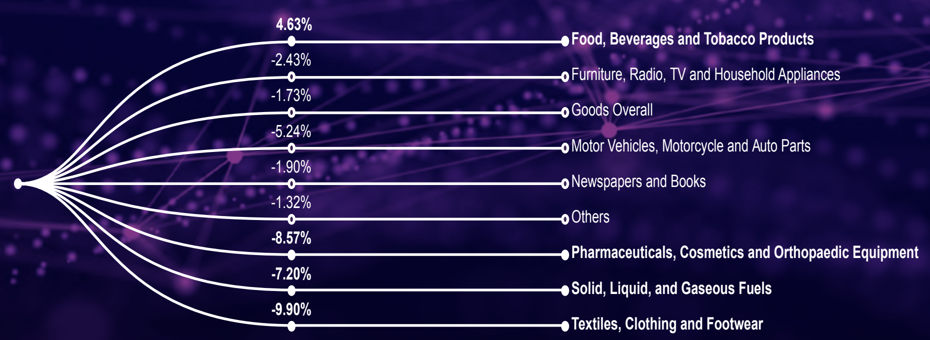
	Sep.17	Sep.18	Sep.19	Sep.20
Turkey	111.83	138.21	205.51	397.52
y/y%		**23.59%**	**48.7%**	**93.43%**
Romania	173.70	188.6	201.6	294.0
y/y%		**23.59%**	**48.7%**	**93.43%**
Hungary	181.7	237.0	341.3	448.6
y/y%		**8.58%**	**6.89%**	**45.83%**
Czech Republic	136.04	158.26	198.97	238.25
y/y%		**16.34%**	**25.72%**	**19.74%**

Source: National Institute of Statistics Romania, Turkish Statistical Institute, Czech Statistical Office, Hungarian Central Statistical Office, CEIC

POLAND

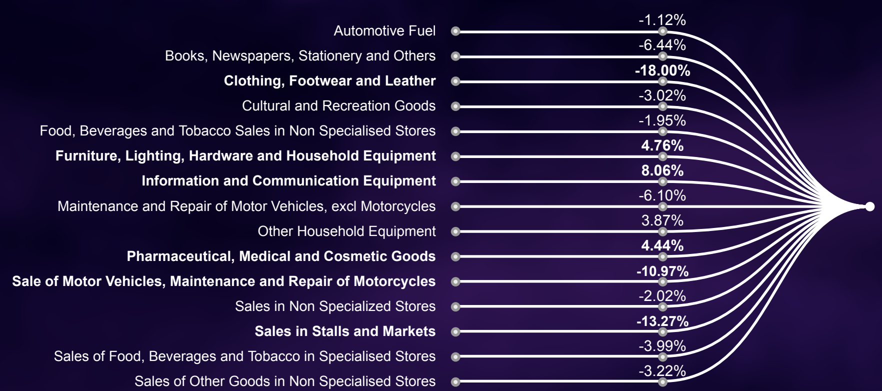
In October 2018, Poland became the first country from the former Soviet bloc to be graded as a developed economy. The grading was provided by FTSE, a London-based provider of economic and financial data. In the country, only F&B sales went up during the pandemic, reflecting the negative attitude of Polish consumers to the way their country was controlling the outbreak.

RETAIL SALES INDEX POLAND, % Y/Y CHANGE, SEPT 2020/SEPT 2019



Source: Central Statistical Office Poland, CEIC

CZECH REPUBLIC



Source: Czech Statistical Office, CEIC

ROMANIA

Romanians, in turn, seem to have engaged in a COVID-19-propelled shopping spree for furniture and other non-food items to make their quarantine time at home more pleasurable.

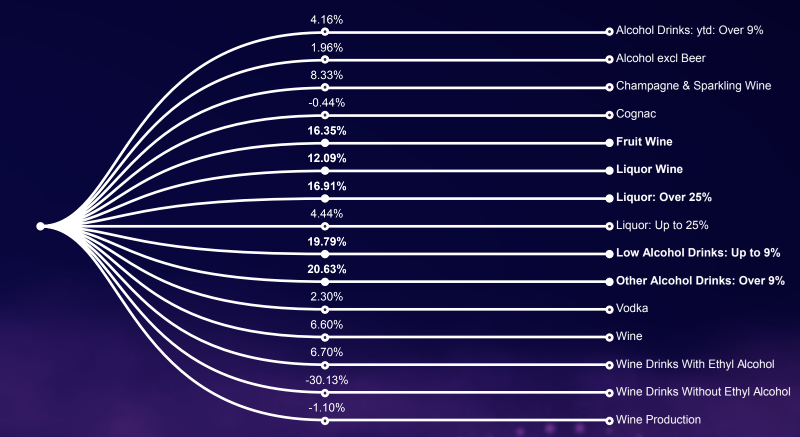
RETAIL SALES IN ROMANIA, % Y/Y CHANGE, SEPT 2020/SEPT 2019

Source: Source: National Institute of Statistics Romania, CEIC

RUSSIA

Russians, on the other hand, went in lockdown only for three months, between April and June, but increased home consumption of both low and high alcohol drinks by nearly one-fifth in September 2020 compared the previous year.

RETAIL SALES IN RUSSIA, % Y/Y CHANGE, SEPT 2020/SEPT 2019

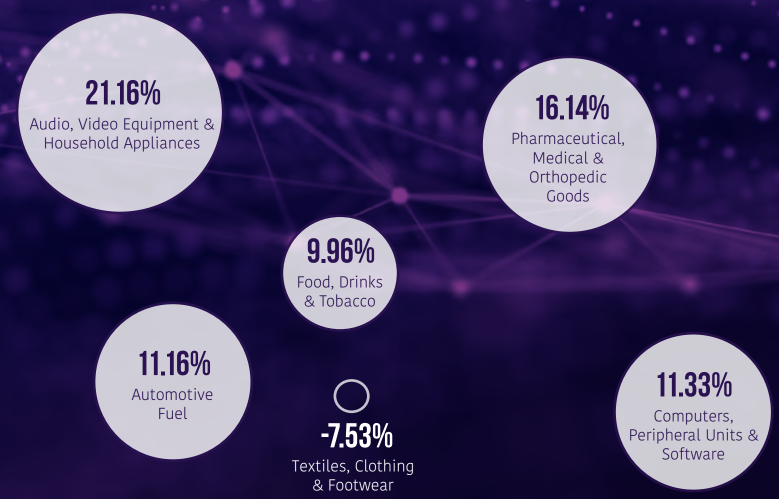


Source: Federal State Statistics Service, Russian Federation, CEIC

TURKEY

During the pandemic, the Turks seem to have been in need of more of everything, except clothing.

TURKEY'S RETAIL SALES VOLUME INDEX, 2015=100, Y/Y CHANGE IN %, SEPT 2020/SEPT 2019



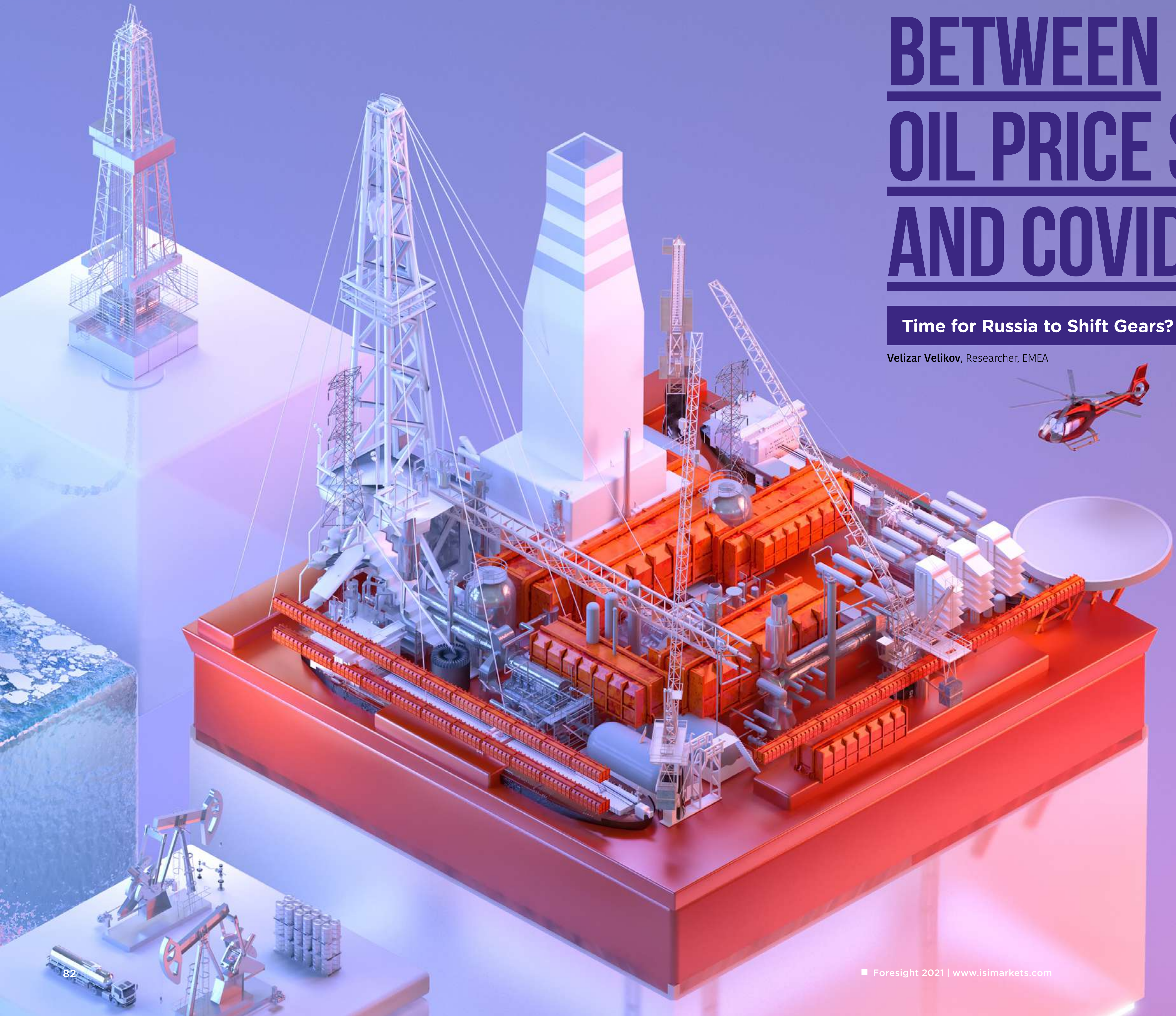
Source: Turkish Statistical Institute, CEIC

Big losers in Hungary, and no big winners in Czechia either. Sales at most retail shops in Hungary have declined or have barely increased since the onset of the pandemic. In Poland, Hungary, and the Czech Repubic alike, the clothing and footwear industry has faced the sharpest decline in retail sales during pandemic until September 2020. To meet the challenges of working and studying from home, some Czechs upgraded their information and communication equipment as well as furniture. On the other end of the spectrum were the Poles and the Hungarians who adopted a more reserved attitude.

HUNGARY

Source: Hungarian Central Statistical Office, CEIC

03 EMEA



BETWEEN OIL PRICE SHOCKS AND COVID

Time for Russia to Shift Gears?

Velizar Velikov, Researcher, EMEA

In 2020, the Russian government faced an uphill task to cushion the double whammy of COVID-19 and the crash of oil prices. First, the economy nosedived into a recession triggered by the two-month nationwide lockdown introduced in April to reign in the spread of the virus. Second, the slump in energy prices because of slowing global demand emptied the state coffers, which rely on the oil and gas sector for almost half of their revenues.

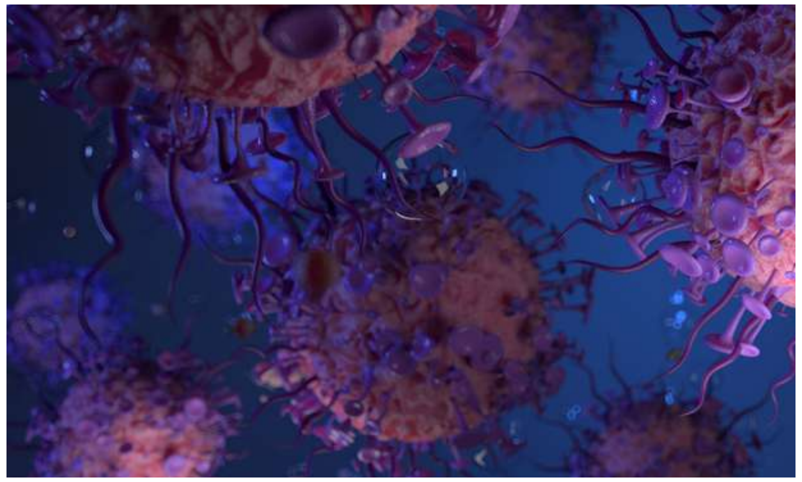
The Russian economy was well-positioned to respond to the COVID-19 crisis with hefty forex reserves, low unemployment rate and a robust financial sector. Thanks to the fiscal consolidation adopted since the 2014-2015 crisis, public finances were in a decent shape. The public debt stood at just 12% of GDP, while the National Welfare Fund (NWF) amounted to some 12% of national output. In the climax of the spring coronavirus outbreak, when oil prices plunged after OPEC's failure to strike a deal with its allies to limit production, the fund was reported to have sufficient reserves to last until 2024, if oil prices remain low. As for the banking system, after a continued clean-up, lenders were enjoying high profitability with sufficient capital buffers and liquidity in the eve of the coronavirus outbreak. The banks' capital adequacy ratio stood at 12.7%, while the bad loans, although at above 9%, were well provisioned.

03 EMEA

Russia's strong and timely fiscal and monetary response softened the economic fallout from the pandemic and resulted in a relatively mild downturn, especially when compared to the steep economic contraction in most other G20 countries. The vast set of measures included income support for households such as expanded social and unemployment benefits and corporate support such as tax deferrals, tax reductions and subsidised loans, among others. Also, public investment in projects deemed systematically important for the economy remained broadly intact and they were excluded from the lockdown. According to IMF estimates, the fiscal stimulus package amounted to about 3.5% of GDP, or some 4.5% if off-budget measures are also included.

COVID-19 FISCAL STIMULUS PACKAGE AT 3.5% OF GDP

On the monetary side, the Bank of Russia slashed its key interest rate by 200 bp to a record low 4.25% and introduced new tools to provide additional liquidity. In the first months of the pandemic, the central bank's accommodative policy was supported by below-target inflation and a rise in the value of the Russian rouble. As a result, lending to the real economy picked up by almost 12% in the first eight months of 2020.



Buoyed by the well-targeted anti-crisis measures, the economy saw a lower-than-expected contraction of 3.6% y/y in the third quarter of 2020. That followed an 8% drop in the previous three months, the deepest since 2009. The improvement could be partly explained with the structural characteristics of the Russian economy. Small and medium-sized enterprises, which have been hit the hardest by the COVID-19 crisis, contribute just around 20% to Russia's GDP or half the share in emerging economies.

But just as the Russian economy was looking to be gaining traction, a resurgence in COVID-19 cases in October sparkled new lockdowns across Europe, weighing on oil demand and sending Brent Crude prices down to levels not seen since the summer. Additionally, the threat of new sanctions against Russia following the alleged poisoning of opposition politician Alexei Navalny and especially after the election of Joe Biden as the new US president has put additional pressure on the rouble, sending it close to the four-year lows last seen in March.

SECOND COVID-19 WAVE, THREAT OF NEW SANCTIONS EXPOSE VULNERABILITIES OF RUSSIAN ECONOMY

Once again, the ongoing health crisis and the growing geopolitical risks have exposed the vulnerabilities of the Russian economy, putting forth plans to reshape its current commoditised model. In preceding years, the country witnessed a sluggish GDP growth and a decline of per capita income compared to that of new EU member states. In 2018, in order to address the medium-term potential growth and diversify its economy away from energy and mineral resources, Russia introduced 13 strategic goals, known as national projects, which envisage RUB 25.7tn (USD 400bn) of public and private spending in key areas from infrastructure and digitalisation to healthcare and education. The ambitions economic and social policy goals include raising GDP growth above the global average, cutting poverty in half, and extending the life expectancy, among others. In January Mikhail Mishustin, the head of Federal Tax Service, who successfully reformed the agency during his 10-year tenure in office, was appointed Russia' prime minister with the task to accelerate work on the national projects, which should have been completed by 2024.

However, the pandemic has dealt a serious setback to the planned spending package, mostly financed with tax increases, and forced the government to push back the deadline of the objectives to 2030 due to tighter budget constraints.

In the meantime, in June Mishustin unveiled a new RUB 5tn (USD 73bn) plan to jump-start the economy while admitting that the national projects require certain adjustments. The new plan will run until 2024 and is aligned with the national goals, which are currently under revision. It consists of around 500 specific support measures that will simultaneously target to raise household income and employment, bringing long-term structural reforms to the economy.

Around RUB 4bn of the earmarked funds, amounting to 3.9% of GDP, have already been spent to curb the immediate impact of pandemic. In 2021, as a second stage of the plan, the government will be looking to support the growth of consumer spending, private investment and exports to archive a GDP growth of 3.3% while reducing federal spending due to the withdrawal of anti-crisis programmes.

It remains to be seen how effective it will be in improving the business climate, increasing competition and ensuring strong private participation in line with the structural policies.

The IMF and the World Bank forecast that Russian economy will contract by between 4% and 5% in 2020 before returning to a growth trajectory with real GDP bouncing back by 2.8% y/y in 2021. It will take at least three years for the economy to fully recover, if a second countrywide lockdown is avoided. The longer-term prospects for the Russian economy are not bright either – at just 1.8% the GDP growth forecast for 2025 puts Russia well below almost all emerging countries, according to the IMF's World Economic Outlook released in October 2020. Reforming the heavily commoditised Russian economy will certainly help in securing a stronger and more sustainable growth. Still, Russia does not seem eager to diversify its economy. Most oil exporting nations have over the past decades invested in diversifying their economies to rely less on oil and gas and prepare for the time when oil runs out. Russia, however, has been lagging in these efforts.

RUSSIA STILL RELIES ON OIL AND GAS

Moreover, its dependence on oil and gas has increased. New data published by the country's statistics office showed that the share of oil and gas in Russia's industrial production increased to 38.9% in 2018 from 34.1% in 2010. That fact alone suggests that for now Russia's guiding motto is to take as much out of the ground as possible, for as long as it can. Yet, it will have to sooner or later embrace the new reality – demand for fossil fuels will continue to decline as more and more countries announce carbon neutrality targets. And it better be sooner than later if Russia wants to move forward to the low-carbon world.

2.8%
Russia's GDP growth expected in 2021

GOVERNMENT TO SUPPORT CONSUMER SPENDING, PRIVATE INVESTMENT, EXPORTS TO ACHIEVE 3.3% GDP GROWTH IN 2021

03 EMEA

AFRICA REIMAGINED

Maagatha Kalavadakken, Researcher, Africa

Although Africa's reported COVID-19 cases are inexpiably low compared to global figures, the socio-economic impacts of the pandemic on the continent are yet to be fully quantified. The pandemic laid bare Africa's existing structural problems and is expected to reverse a lot of developmental achievements, exacerbate the levels of inequality and highlight the importance of creating a strong local production capacity and bringing to light the informal economy, whose large share has made it extremely difficult for regulators to intervene during the pandemic.

Adopting Technology

On the upside, the measures implemented by various African governments have accentuated the adoption of digital economy as a tool to accelerate financial inclusion, e-learning and digital payments, and to forge new ways to integrate the dual economy that exists within many of the 54 countries on the continent. If some of these measures remain after the pandemic, they have the potential to benefit education, banking, e-commerce and agri-business.

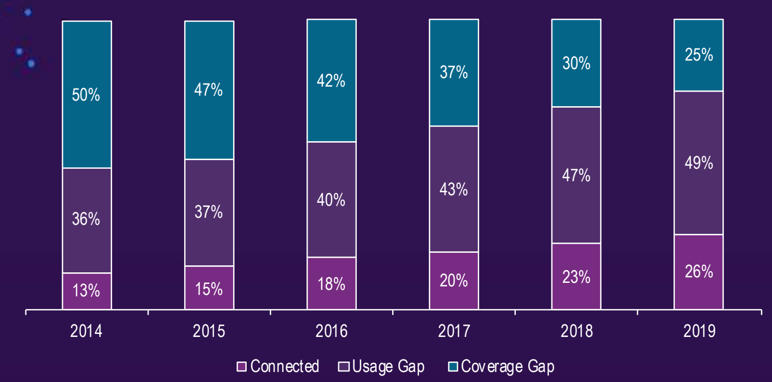
SPURRED BY THE PANDEMIC, AFRICA ACCENTUATES THE ADOPTION OF DIGITAL ECONOMY

Since so much of the online industry is dependent on the strength and accessibility of ICT, various countries such as Kenya, South Africa and Nigeria issued a temporary increase in spectrum, zero-rated websites and reduced data prices. South Africa also explored the use of white noise spaces to increase internet access in rural areas by tapping into the high TV per household ownership in the country. While increased spectrum may require additional infrastructure spending from telcos, it could boost the number of subscribers, pushing prices down and making internet access more affordable. However, more is still required to make digital technologies inclusive and accessible to all. Currently only 26% of the Sub-Saharan Africa population has access to mobile data (3G or more advanced) compared to a global average of 49% and the prices of fixed-line broadband packages in the region are among the highest in the world.

26%

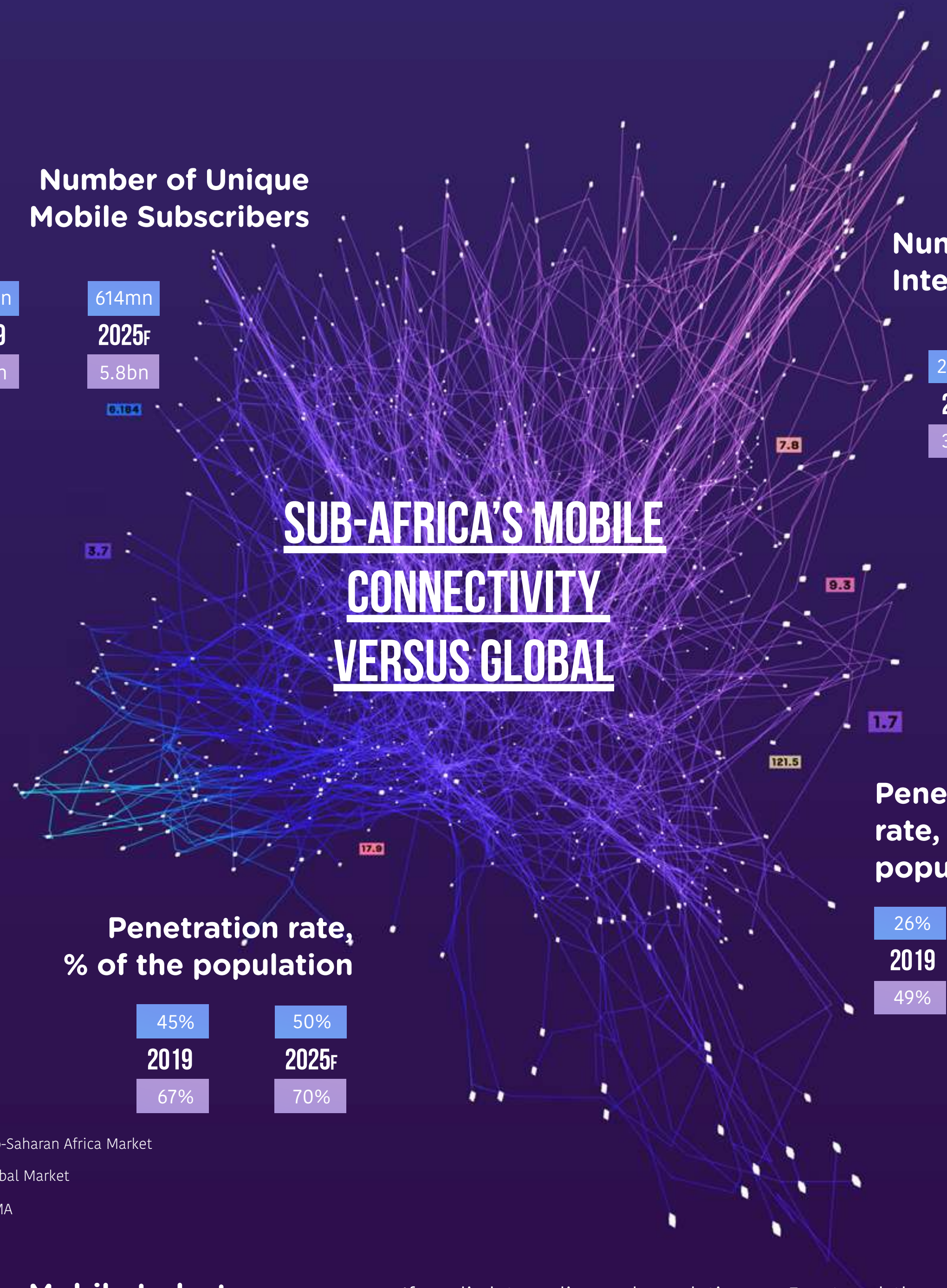
Share of Sub-Saharan Africa population with access to mobile data

Mobile Internet Users in Sub-Saharan Africa, % of Population



Note: Usage gap refers to populations that live within the footprint of a mobile broadband network but who are not using mobile internet. Coverage gap refers to populations that do not live within the footprint of a mobile broadband network (3G or above).
Source: GSMA Intelligence

SUB-AFRICA'S MOBILE CONNECTIVITY VERSUS GLOBAL



Number of Unique Mobile Subscribers

	2019	2025F
Sub-Saharan Africa Market	477mn	614mn
Global Market	5.2bn	5.8bn

Penetration rate, % of the population

	2019	2025F
Sub-Saharan Africa Market	45%	50%
Global Market	67%	70%

Number of Mobile Internet Users

	2019	2024F
Sub-Saharan Africa Market	272mn	475mn
Global Market	3.8bn	5.0bn

Penetration rate, % of the population

	2019	2024F
Sub-Saharan Africa Market	26%	39%
Global Market	49%	61%

Sub-Saharan Africa Market
Global Market
Source: GSMA

Mobile Industry Contribution to GDP

	Sub-Saharan Africa Market	Global Market
2019	USD 155bn	USD 4.1tn
2024F	USD 184bn	USD 4.9tn

Sub-Saharan Africa Market
Global Market
Source: GSMA

If applied to policy and regulations, the quick and decisive approach that African governments took to boost the adoption of digital technologies might eliminate the costly bureaucratic red tape that often makes doing business in Africa difficult. In addition, this agile approach is the best when implementing out-of-the-box solutions that are unique to African challenges.

Africa remains a cash-based economy, heavily reliant on remittances. During the COVID-19 outbreak, in order to encourage the use of basic banking services and support social distancing, countries like South Africa, Kenya, and Egypt and the members of the West African Monetary Union have put in place a number of measures such as simplifying procedures for onboarding new clients. A wavering of transaction fees and an increase in daily transaction limits were implemented in South Africa, Kenya, Senegal and Rwanda. Among the most important interventions is the relaxation of know your customer regulations. In the long run they will improve the gender gap in financial inclusion in Africa, where over 53% of women and youth are financially excluded.

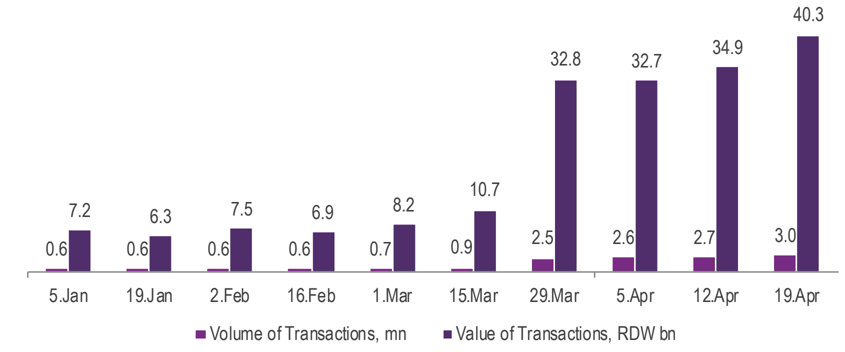
Wiring Money

As the majority of these supportive measures are phased down with the easing of the lockdowns, mobile money transfer charges are gradually being restored. However, the relaxed requirements have already resulted in a wider pool of new clients, thus leading to higher financial inclusion and less use of cash.

From a customer perspective, these measures offer an opportunity to test products that customers might otherwise think untrustworthy, while for the mobile money players they offer a way to move further into the digital field. In Rwanda, for example, the value of person-to-person (P2P) transfers rose five times from the pre-pandemic levels.

Data collected by Rwanda's telecommunication regulator and South African think-tank Cenfri showed that the number of mobile-money transfers in Rwanda doubled in the week after a lockdown was imposed on March 22. By late April users were making 3mn transactions a week, versus the pre-pandemic norm of just 600,000 weekly transfers. The pandemic has had a similar catalytic effect as the unrest that followed the disputed 2007 elections, when many people stayed in home afraid of the violent clashes on the streets and started sending money to each other by phone – a habit that stuck until today.

P2P Weekly Transfers in Rwanda



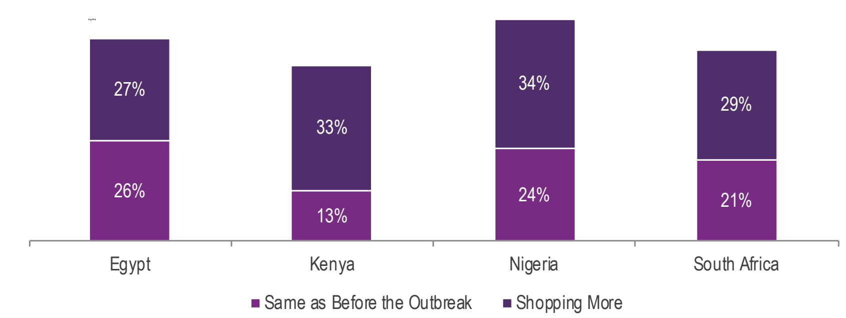
Source: Rwandan Utilities Regulation Authority, Cenfri

Online Boom

Similarly, e-commerce has become more popular during the COVID-19 outbreak. Even before the pandemic, the sector was growing steadily, but national lockdowns and stay-at-home orders have seen customers rushing to online stores that have since been struggling to keep up with demand. While e-commerce thrived, brick-and-mortar shops saw a decline in revenue. Figures published by market researcher Nielsen South Africa in May 2020 showed that 65% of South Africans have reduced visits to physical supermarkets despite the population's heavy dependence on informal trade outlets. On the contrary, 29% of South African consumers are shopping more online now than before the pandemic. Other African countries included in the survey are Egypt, Nigeria and Kenya. Of them, Nigerians seem to be the ones with highest preference for online shopping as 70% of them said they shop less in supermarkets after the COVID-19 outbreak and 34% said they have increased online purchases.

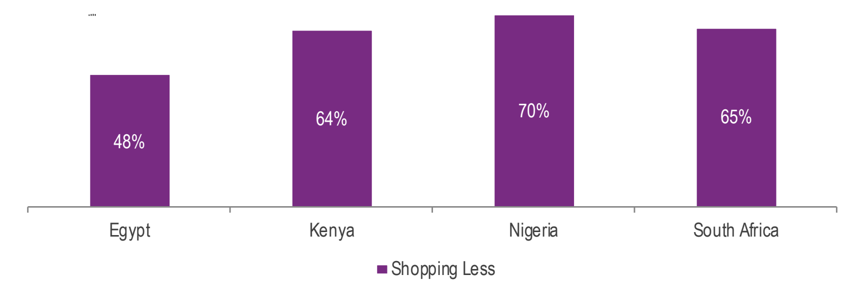
Nonetheless, it is no secret that Sub-Saharan Africa's e-commerce industry still faces numerous challenges such as low trust levels, low bank card penetration, underdeveloped transport infrastructure, and a lack of proper address systems. Still, there is room for pioneer innovations and coming up with solutions unique to Africa.

Impact on Online Shopping During COVID-19



Source: Nielsen Consumer Insights Survey

Impact on Supermarket Shopping During COVID-19



Source: Nielsen Consumer Insights Survey

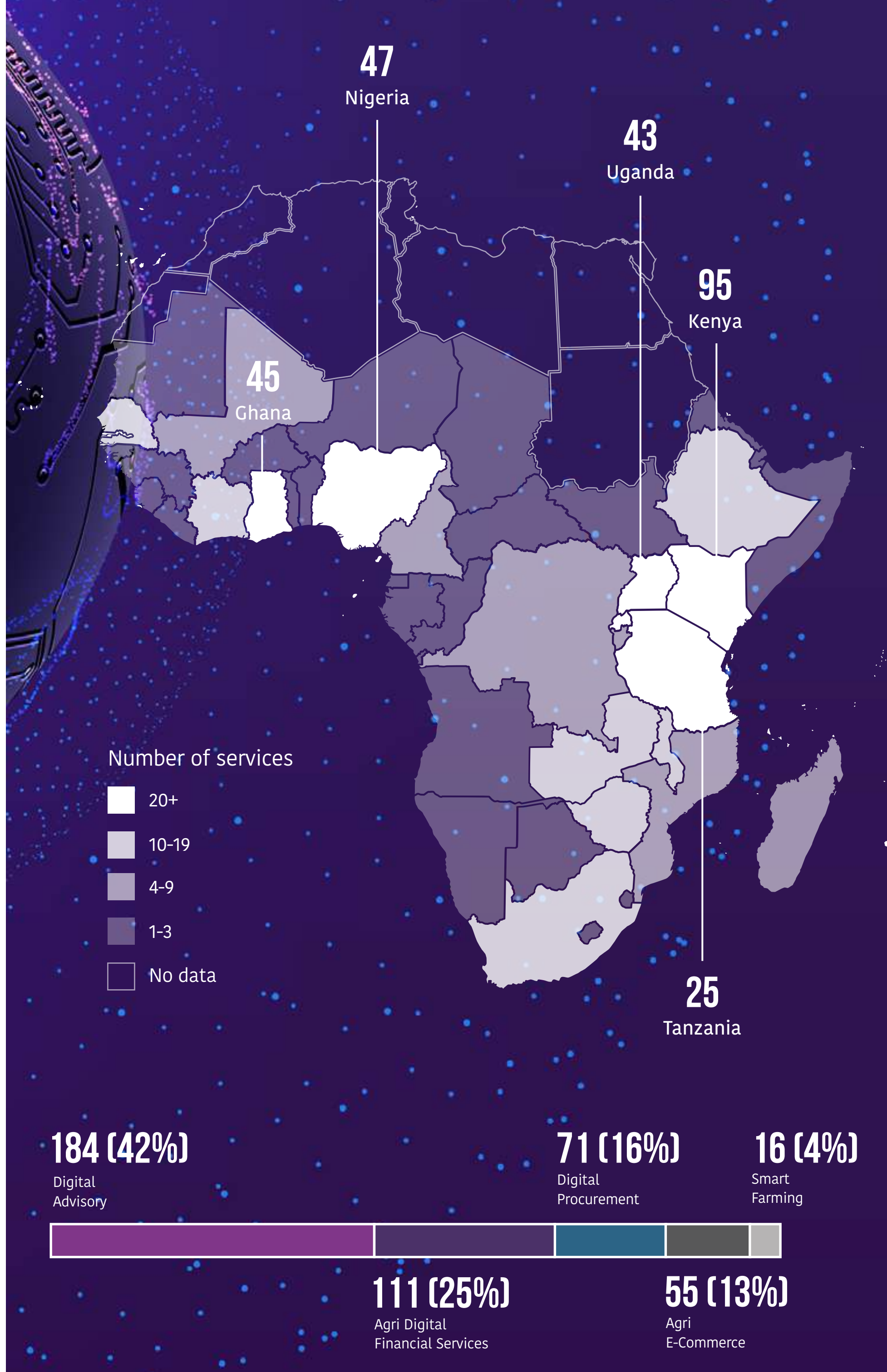
Digital Platforms for Small Farmers

One of the main challenges before the agriculture sector is the difficult access to markets, which pushes the prices of agricultural goods higher and kicks small farmers out of the game. A digital infrastructure that links the informal sector to the market can thus offer opportunities to over 60mn urban farms in Africa. A number of African governments have already stepped in to offer solutions. Togo, Senegal and Nigeria have created platforms linking informal operators to established marketplaces helping out-of-reach households to get in touch with market vendors, using local transport solutions. Other African governments have facilitated partnerships between the larger existing digital platforms to create more opportunities for collaboration with the informal sector. These digital platforms can also boost agricultural productivity through prompt payments for produce, information sharing and agro-industrial activities.

Although most e-commerce start-ups in Sub-Saharan Africa are still small, dependent on donor funding and in the pilot stage, some major players have been emerging such as Twiga Foods in Kenya, which connects fruit and vegetable farmers to urban retailers, and AgroTrade in Ghana, which connects farmers in the staple food value chain to large off-takers, according to data published in GSMA Agri-Tech Digital Report 2020. The report also shows that the number of agri e-commerce platforms in low and middle-income countries has grown exponentially, from six in 2009 to 126 in 2019, 71 of which are in Sub-Saharan Africa. Agriculture adds about 16.2% of GDP in Sub-Saharan Africa and employs over 80% of its population.

AFRICAN GOVERNMENTS STEP IN TO OFFER DIGITAL SOLUTIONS TO SMALL FARMERS

ACTIVE DIGITAL AGRICULTURE SERVICES IN SUB-SAHARAN AFRICA, JANUARY 2020



Source: GSMA Digital Agriculture Maps

E-Learning Opportunities

Another sector that has changed dramatically during COVID-19 is education. Like elsewhere, the pandemic has forced schools and universities in Africa to shut doors and students to shift to remote learning. But while digital e-learning platforms have come to the fore in most continents around the world, radio and television have remained the largest sources of information in Africa mainly due to the low internet connectivity and expensive data. Data from a report published by UNESCO in 2020 showed that 89% of learners in Africa do not have access to household computers while 82% lack internet access. Faced with national lockdowns, governments across Africa made use of radio and television to continue to deliver education. They also partnered with telecoms and schools to offer zero-rated websites and apps for learning.

RADIO, TV REMAIN LARGEST SOURCES OF INFORMATION DUE TO LOW INTERNET CONNECTIVITY

Before COVID-19 over 60mn children did not attend any form of school in Africa. To meet its Millennium Development Goal for Universal Primary Education, a report by the United Nations suggests Africa would need up to USD 8bn of investments a year. A combined usage of radio, television, internet and mobile phone apps presents a multitude of opportunities in Africa's education sector once the pandemic is over. Whatsapp and telegram became the dominantly used form of communication for learners, teachers and parents during the pandemic. Digital connections enable a two-way communication, real-time interaction, and feedback for learners and educators.

The global e-learning market is set to exceed USD 375bn by 2026, according to a report by Global Market Insights, with Africa's e-learning market expanding by 14% between 2011 and 2018. It is now expected to reach USD 1.8bn by 2024.

COVID-19 has enticed innovation in this space across Africa. Although most of the e-learning solutions are still at a nascent stage, once adopted these new technologies could be a game changer for the sector. For example, Nigeria as a tech hub in Africa boast a plethora of online learning platforms. Some like Krystal Digital and Quizac saw a rise in user numbers to 65,000 and 100,000, respectively, during the COVID-19 outbreak. Bigger players like Tanzania's Ubongo that boasts 17mn TV viewers in 30 countries use a combined model of TV programmes, YouTube and web resources for its users. This diverse offer allows users to access information via a channel that is most readily available to them.

In South Africa, AI platform Ms Zora, a collaboration between the department of Basic Education, Africa Teen Geeks and Apodytes, was initially rolled out to over 200 schools in 2019 and plans are to cover the whole country in the future. Other solutions, such as Mtabe, target the segment of population that has no access to mobile data. Mtabe is an artificial intelligence-powered SMS platform that can answer students' most pressing questions by text.

As the continent, which has weathered many natural disasters and disease outbreaks, is going through the pandemic and trying to evaluate its future impact, the measures and policies taken during the outbreak will not only play a critical role in recovery but will also serve as pillars for sustainable growth in the future and for creating a reimagined Africa. ISI

AFRICA'S E-LEARNING MARKET TO REACH USD 1.8BN BY 2024

03 EMEA

AFRICA'S INFRASTRUCTURE WOES

Mfundo Hadebe, Researcher, Africa

Infrastructure investments have been rising steadily in Africa over the past decade with both local government and international investors having the appetite and funds to spend much more. Yet, of the estimated USD 130bn-170bn a year that the continent needs to bring its infrastructure up to par, it manages to attract just half. On top of that, the short-term investment outlook is clouded by the COVID-19 outbreak with many infrastructure projects delayed as governments are prioritising their spending commitment in the light of the pandemic with a focus on recurrent expenditure. With many of Africa's 54 countries heading for an economic contraction, all eyes will likely again turn east to China – the region's top trade partner, the leading investor and most importantly the biggest financier of Africa's infrastructure.

WITH LOOMING GDP CONTRACTION IN AFRICA, ALL EYES TURN TO CHINA

Bridging the Infrastructure Gap

Most of Africa lags behind the rest of the world in key infrastructure metrics including energy, road and rail transportation, and water supply. It is estimated that this constrains productivity by up to 40% and reduces Africa's GDP by about 2% per year. Take electricity for example - nearly 600mn people in Sub-Saharan Africa do not have access to grid electricity and they make up over two-thirds of the global population without electric power. Bridging the infrastructure gap will undoubtedly make a great difference for Africa's economic development. In fact, infrastructure development has played a pivotal role towards the enablement of productivity and economic growth in Africa. According to the African Development Bank Group (AfDB), investment in infrastructure accounts for over half of the recent improvement in economic growth in Africa and has the potential to achieve even more. Continuous infrastructure improvements in services such as electricity, transport, sanitation and sewerage systems enhance productivity and stimulate regional integration and trade.

AfDB estimates that infrastructure needs for the African region amount to USD 130bn-170bn a year, with a financing gap of USD 68bn-108bn.

AFRICA NEEDS USD 130BN-170BN IN ANNUAL INFRASTRUCTURE INVESTMENT

This estimated infrastructure gap coupled with dire needs in health, education, administrative capacity and security, means the region is challenged with finding ways to attract private investments to speed up the building of critical infrastructure needed to unleash its potential.

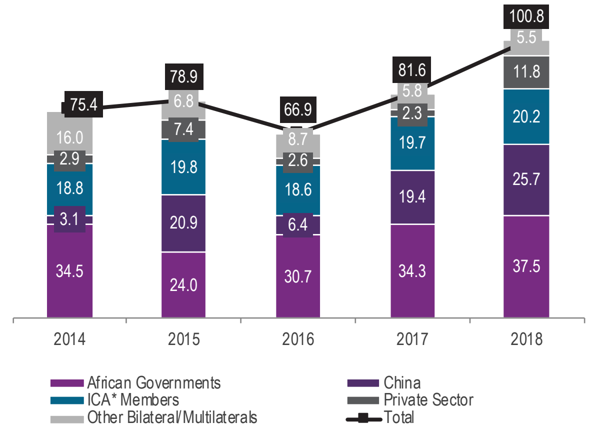
Who Funds Infrastructure?

Africa relies heavily on national governments to finance the continent's infrastructure development. A report by the Infrastructure Consortium for Africa (ICA) found that governments accounted for 40% of total funding for infrastructure in the 2014-2018 period.

In 2018 alone, total spending on African infrastructure amounted to USD 100.8bn, an increase of 24% over the total commitments reported for 2017 and an increase of 33% over the 2015-2017 average. This was the first time that the level of commitments passed the USD 100bn mark.

African governments were the largest source of infrastructure financing, with commitments of USD 37.5bn (37% of total), followed by China, which committed USD 25.7bn (25%), ICA members (USD 20.2bn, 20%), the private sector (USD 11.8bn, 12%), and other sources (USD 5.6bn, 6%).

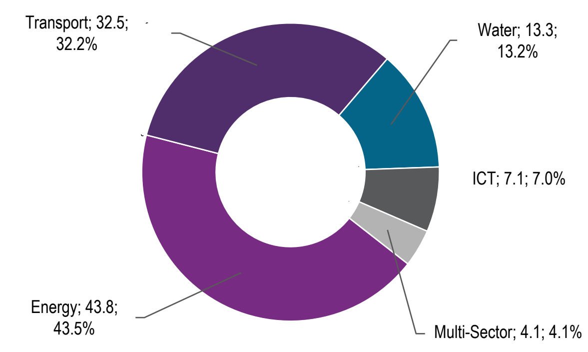
Africa's Infrastructure Investment Commitments, USD bn



Source: ICA

*ICA Members - The Infrastructure Consortium for Africa is a tripartite relationship between bilateral donors, multilateral agencies and African institutions.

Africa Infrastructure Investments by Sector, USD bn, 2018



Source: ICA

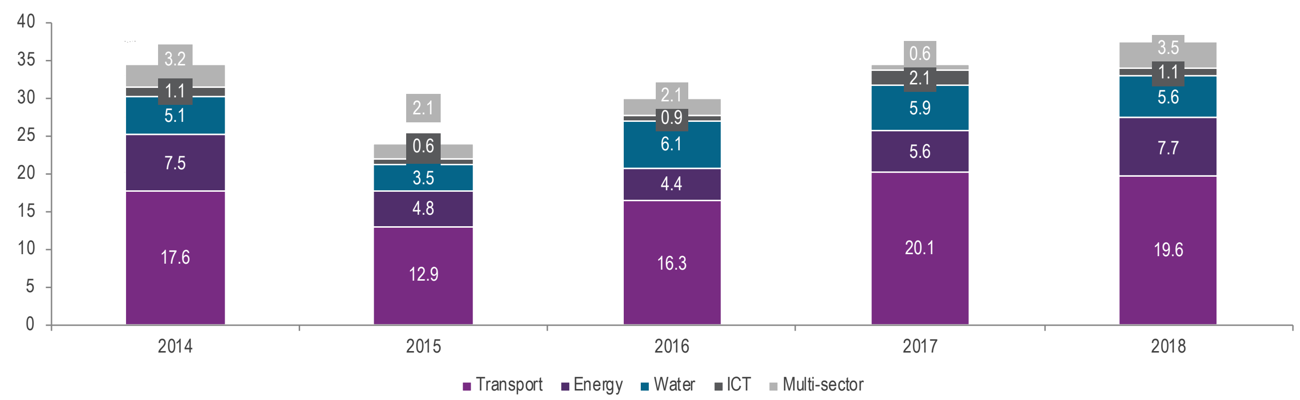
40%
GOVERNMENT SHARE IN TOTAL INFRASTRUCTURE FUNDING IN AFRICA

African national governments' commitment towards infrastructure development has been increasing every year. The year 2018 saw 48 African national governments commit USD 37.5bn towards their own infrastructure projects and programmes. This represents a 9% growth from the previous year's USD 34.3bn commitment from 47 African countries and a 22% growth from 2016's USD 30.7bn for 49 countries. When it comes to key focus sectors, transport, water & sanitation and energy sectors account for the lion's share of national governments' infrastructure budgets in Africa.

TRANSPORT, ENERGY AND WATER ATTRACT MOST INVESTMENTS

3.0%
Expected Economic Contraction in Sub-Sahara Africa in 2020

African Governments Commitments, Breakdown by Sectors, USD bn



Source: ICA

Gloomy Economy

The COVID-19 pandemic, however, will weigh significantly on African governments' ability to finance big infrastructure projects at least in the short term. A June 2020 report by AfDB projects Africa's GDP to contract by 1.7% in the best or by 3.4% in the worst case scenario as a result of the pandemic. A partial recovery of about 3% is projected for 2021 but it would not make up for an estimated cumulative loss to Africa's GDP of USD 173.1bn–236.7bn for both 2020 and 2021, the AfDB says. The IMF is even more pessimistic projecting a record 3% economic contraction for Sub-Saharan Africa in 2020 and a 5.1% GDP fall for the Middle East and North Africa, the fund said in its October 2020 Global Economic Outlook.

3.1% GDP GROWTH IN SUB-SAHARAN AFRICA IN 2021

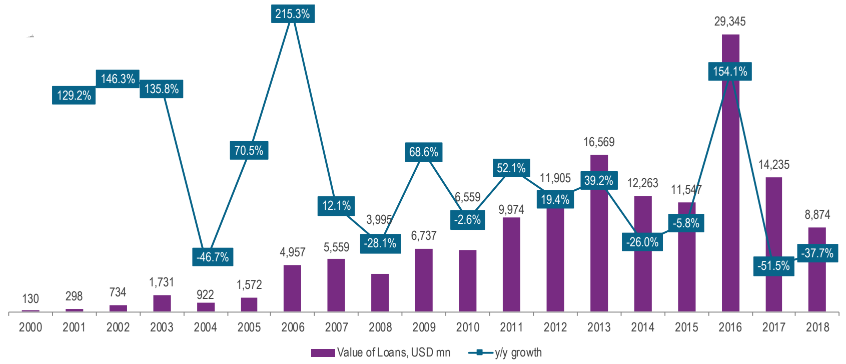
Looking forward, a recovery is expected for 2021, when Sub-Saharan Africa should see a 3.1% GDP growth. This is a smaller expansion than expected in much of the rest of the world, partly reflecting the region's relatively limited policy space within which to sustain a fiscal expansion, the IMF notes. Growth in the Middle East and North Africa is forecast at 3.2% in 2021. At such tough times could the region's second biggest infrastructure financier lend a helping hand?

A Look to the East

China has gradually become a central player in Africa's infrastructure development push. China funds one in every five projects across Africa, making it the second-largest funding source after African governments. In 2018, China invested USD 25.7bn in infrastructure projects and programmes in Africa, 32% higher than in the previous year. Over 2014-2018, China had committed to invest USD 75bn in infrastructure projects in Africa, more than half of which (57%) going to energy projects and a third (30.1%) to transport projects.

ANGOLA IS THE LARGEST RECIPIENT OF CHINESE LOANS WITH USD 43.2BN IN NEARLY TWO DECADES

China's Loans to Africa



Source: ICA

The ambitious projects and the desire for fast results might have led to African countries biting more than they could chew as the bills started piling up. The lending spree over the past two decades has propelled China to the top of Africa's creditor list. China's government, banks and companies lent some USD 148bn to Africa between 2000 and 2018, larger than any OECD lender, and near-matching the World Bank's loans in Africa, according to data from Johns Hopkins University.

USD 148BN CHINESE LOANS TO AFRICA, 2000-2018

CHINA FUNDS ONE IN EVERY FIVE PROJECTS ACROSS AFRICA

Saddled with a pile of debts, some of the poorer African countries have been struggling to pay their dues even before the pandemic made things even worse, sending some on the brink of default. Zambia became the first African nation to default on its debt in the COVID-19 era. On a positive note, the G20 countries agreed to suspend debt service for African countries until at least mid-2021 and sketched out rules for restructuring their government debt to help fend off the risk of default in the wake of the COVID-19 crisis. Yet, these plans provide just a near-term breathing room for African countries, raising concerns of more defaults on the way.

And here comes the reasonable question – will China continue to support Africa's infrastructure development or will Beijing change its course of action and be more selective in its investment activities abroad. A November 2020 report by German insurer Allianz and Euler Hermes suggests that over the 2021-2025 period China will cut its funding abroad, thus depriving South Africa of USD 10.7bn, Kenya of USD 6.6bn, Angola of USD 5.2bn, Ethiopia of USD 4.7bn, Egypt of USD 1.3bn, Zambia of USD 1.1bn and Ghana of USD 0.9bn. Overall, the seven African countries might lose USD 30.5bn in potential Chinese funding over the five-year period. The authors of the report identify two reasons for China's withdrawal. The first is the recently unveiled dual circulation strategy that would help steer the Chinese economy towards greater self-reliance and lower its dependence on overseas markets. The second reason is the expected slowdown in Chinese economic growth that will further strain Beijing's overseas lending and investment activities.

AFRICAN COUNTRIES AT RISK OF LOSING USD 30.5BN IN POTENTIAL CHINESE FUNDING

One thing is sure though - Beijing's relationship with its African partners is changing and it remains to be seen whether this would mean fewer investments or whether China will seek to further strengthen its position in the resource-rich continent.

In Need for Private Investment

Securing private investments for large-scale infrastructure projects has always been a challenge for many African countries. One significant hurdle is the lack of sound policies and regulatory frameworks in order to spur private infrastructure investment in the continent. Some of the inadequacies include regulatory uncertainties, bureaucracy and widespread bribery. Estimates by OECD show that 10%-30% of investments in publicly funded infrastructure projects are likely to be lost as a result of bribery or mismanagement of funds. Another constraint is the region's underdeveloped financial market coupled with regulatory barriers that impede the supply of long-term financing. The banking sectors in most African countries do not accommodate infrastructure financing and there are only six countries in the region that offer bank loans with long maturities (20-year loans). Even in the case of these six countries, the interest rates are too high - above 20% in three of these countries - making it close to impossible to consider using banks for financing infrastructure developments.

The continent of Africa is making strides towards achieving sustainable regional growth. The launch of the African Continental Free Trade Area (AfCFTA) in 2019 could potentially hold the key for the creation of a more integrated Africa. The effectiveness of the AfCFTA will require satisfactory infrastructure networks and countries across the continent will have to join forces in investing in roads, rail and power infrastructure. ISI

12%

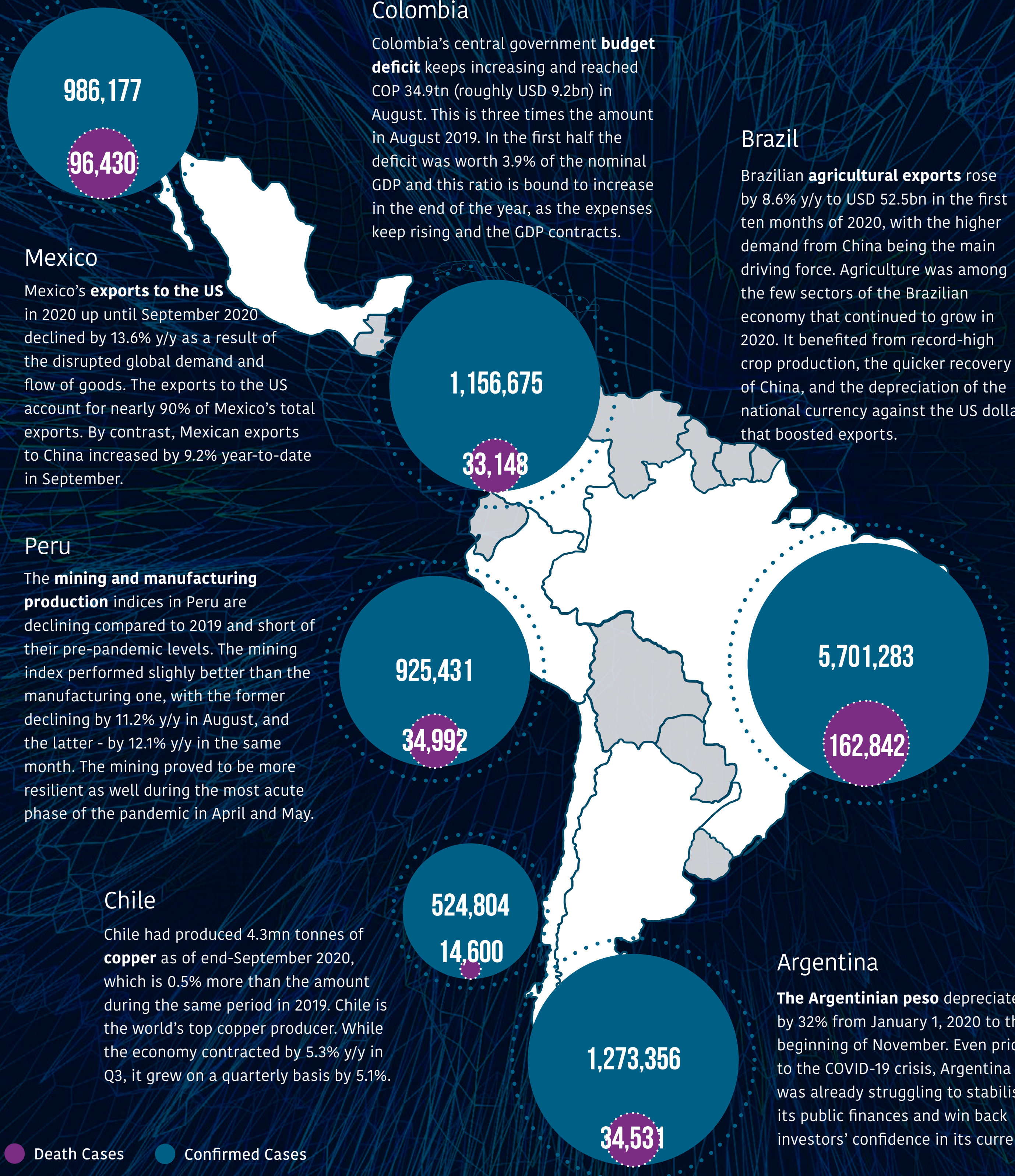
Private Sector Share in Infrastructure Funding

04

Latin America

ADJUST AND ADAPT

The COVID-19 outbreak shed light on both vulnerable spots and resilient areas in Latin America



Mexico

Mexico's **exports to the US** in 2020 up until September 2020 declined by 13.6% y/y as a result of the disrupted global demand and flow of goods. The exports to the US account for nearly 90% of Mexico's total exports. By contrast, Mexican exports to China increased by 9.2% year-to-date in September.

Colombia

Colombia's central government **budget deficit** keeps increasing and reached COP 34.9tn (roughly USD 9.2bn) in August. This is three times the amount in August 2019. In the first half the deficit was worth 3.9% of the nominal GDP and this ratio is bound to increase in the end of the year, as the expenses keep rising and the GDP contracts.

Brazil

Brazilian **agricultural exports** rose by 8.6% y/y to USD 52.5bn in the first ten months of 2020, with the higher demand from China being the main driving force. Agriculture was among the few sectors of the Brazilian economy that continued to grow in 2020. It benefited from record-high crop production, the quicker recovery of China, and the depreciation of the national currency against the US dollar that boosted exports.

Peru

The **mining and manufacturing production** indices in Peru are declining compared to 2019 and short of their pre-pandemic levels. The mining index performed slighly better than the manufacturing one, with the former declining by 11.2% y/y in August, and the latter - by 12.1% y/y in the same month. The mining proved to be more resilient as well during the most acute phase of the pandemic in April and May.

Chile

Chile had produced 4.3mn tonnes of **copper** as of end-September 2020, which is 0.5% more than the amount during the same period in 2019. Chile is the world's top copper producer. While the economy contracted by 5.3% y/y in Q3, it grew on a quarterly basis by 5.1%.

Argentina

The Argentinian peso depreciated by 32% from January 1, 2020 to the beginning of November. Even prior to the COVID-19 crisis, Argentina was already struggling to stabilise its public finances and win back investors' confidence in its currency.

Death Cases Confirmed Cases

Note: COVID-19 confirmed cases as of mid-November

Source: CEIC, MDIC/Comex Stat, Central Bank of Argentina, Bank of Mexico, National Institute of Statistics Chile, Central Bank of Colombia, National Institute of Statistics Peru

THE BUTTERFLY EFFECT IN BRAZIL

What were the (un)intended effects of government aid to vulnerable groups

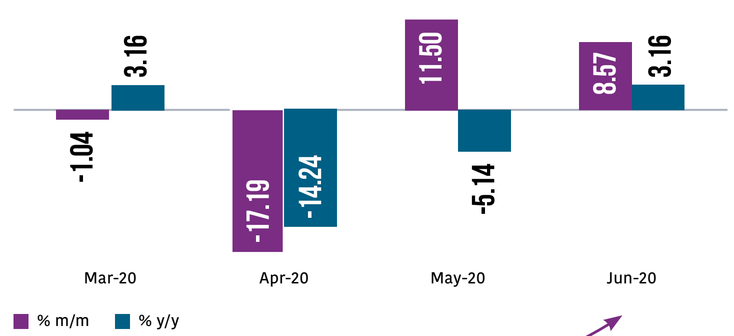
APR 2020

The government introduced a social programme for individuals and households affected financially by the pandemic. Monthly benefits of BRL 600 were given to unemployed workers from low-income households

MAY 2020

Monthly retail sales value growth turned again positive at 11.5%

Retail Sales in Brazil



Source: CEIC, Brazilian Institute of Geography and Statistics

JUN 2020

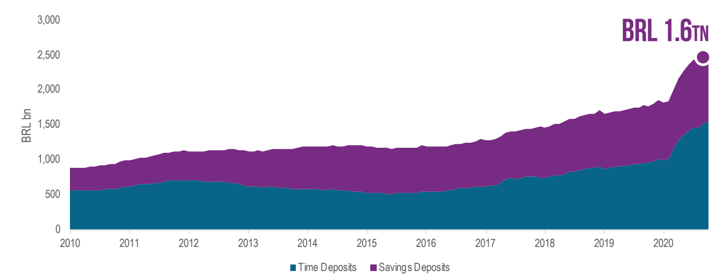
The emergency aid programme got extended but the monthly transfer was reduced to BRL 300

Annual retail sales growth followed the monthly dynamic and turned positive again at 3.2%

Getulio Vargas Foundation: The poverty line in Brazil fell to 21.7% in June 2020, a 16-year low, from 25.6% a year earlier.

Brazil's Gini coefficient fell below the 0.5 point mark for the first time ever

Time and Savings Deposits in Brazil



Source: CEIC, Central Bank of Brazil

AUG 2020

Over 66mn people participated in the programme

The programme has become the largest social expense of the Brazilian government, accounting for more than BRL 50bn per month

SEP 2020

Side effect: Brazilians start hoarding cash. Time deposits reached BRL 1.6tn (USD 306bn), a 55% y/y increase

Brazilians Working Remotely

Brazilians on Unpaid Leave or with Reduced Working Hours Due to Social Distancing Measures

May-20 Aug-20

Source: Brazilian Institute of Geography and Statistic

WEATHERING THE CORONAVIRUS STORM: ALL PAIN, NO GAIN?

Juan Manuel Costa, Researcher, Latin America

It took a while for COVID-19 to arrive in Latin America. But when it did, it hit hard. By late November 2020, Latin America accounted for eight of the world's 15 deadliest COVID-19 hotspots

IN NOVEMBER 2020 LATIN AMERICA WAS HOME TO 8 OF THE 15 DEADLIEST COVID-19 HOTSPOTS GLOBALLY

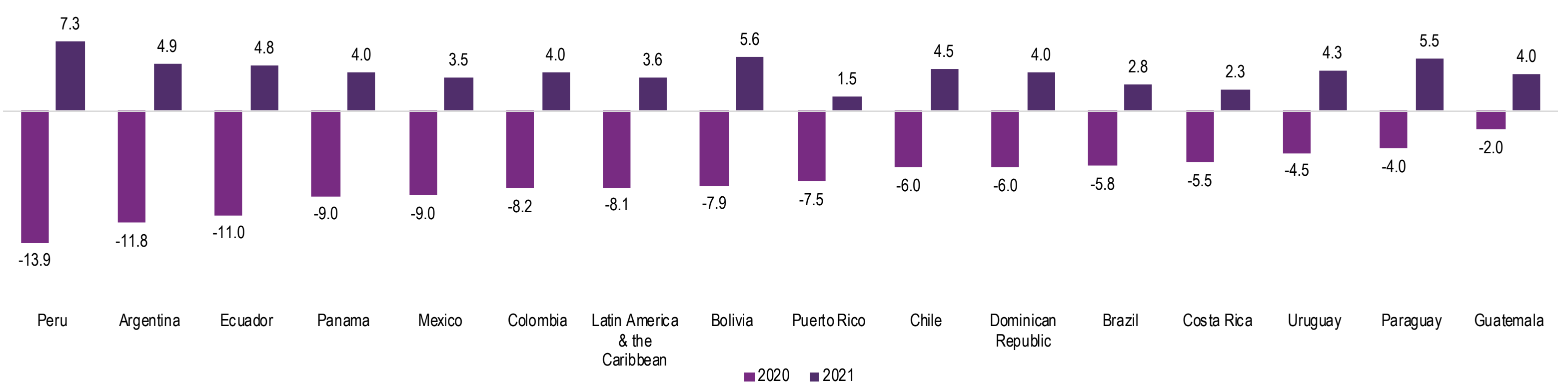
With 110 deaths per 100,000 population, Peru was in the lead of the grim statistics, followed by Argentina, Chile, Brazil, Mexico, Bolivia, Ecuador and Panama. Why has the pandemic affected the region so badly, both on the healthcare and the economic fronts? Why were some countries like Brazil and Mexico hit very early, while others such as Argentina seemed to be doing well initially only to end up as bad as the others? Was it all pain and no gain? These are some of the questions that we will try to answer in this article.

The Mother of All Shocks

Some experts believe that one of the main reasons for the failure to contain the COVID-19 outbreak in Latin America was the poor timing of the lockdown measures. On the one hand, there are countries such as Mexico and Brazil, which, for varying reasons, stalled the adoption of quarantine measures even in the face of an alarming growth in the number of COVID-19 cases and when such measures were finally adopted their scope was rather limited. In Brazil, the delayed introduction of restrictive measures was political in nature, as President Bolsonaro wanted to protect business interests and trade at all costs. Meanwhile, in Mexico, President Lopez Obrador, concerned by fragile public finances, stated that the government was in no shape to provide the massive social assistance that would have been needed as a result of a severe and lasting lockdown. Thus, the Mexican government opted for a mild nationwide quarantine in April and May and a rapid normalisation of economic activities afterwards. In contrast, other countries such as Argentina and Colombia, adopted severe lockdown measures at the beginning of the outbreak. This strategy proved efficient in mitigating the initial shocks of the pandemic, but at the cost of a strong negative impact on the economy, social tiredness and a massive spike in the number of cases once restrictions were lifted.

Another factor that reduced the capacity of governments in the region to control the pandemic was the insufficient testing capacity, with bottlenecks of all kinds. In Peru and Colombia, despite the preventive acquisition of materials for PCR testing, the lack of laboratories with adequate testing capabilities limited the effectiveness of diagnostic campaigns. Argentina, on the other hand, was too late to secure materials for PCR testing, which was the main limiting factor in the first months of the fight against COVID-19. A grand exception from this was Chile, with adequate testing infrastructure, innovative testing techniques and ample supply of materials. This allowed the South American country to run a much more precise and systematic tracking of the pandemic. Chile's key to success was a system of regional rather than national lockdowns, which proved quite effective and with less economic costs.

GDP Estimates



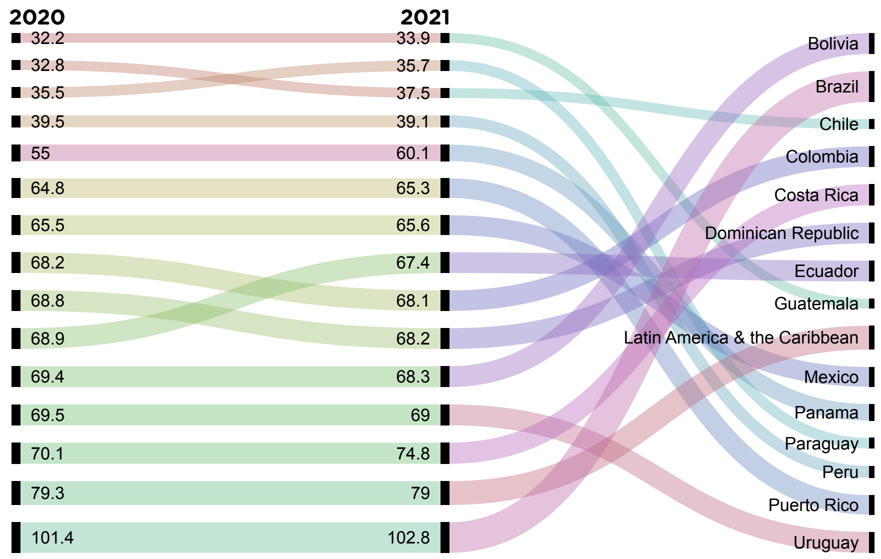
Source: IMF, World Economic Outlook October 2020

Aside from the hard factors – timing of lockdowns and testing capacity – the rapid evolution of the pandemic in the region was also due to soft factors such as the structure of the economy and social issues. High poverty, especially among the urban population, combined with high population density limited the effectiveness of lockdowns

HIGH POVERTY AND POPULATION DENSITY LIMITS LOCKDOWN EFFICIENCY

Although the governments in the region were fully aware of these issues and implemented household support programmes, targeting the most vulnerable layers of the population, fiscal restrictions downplayed the success of these measures. Some of these programmes were either too small right from the start – as in the case of Peru and Colombia – or more adequate but quite difficult to sustain in time, such as that in Argentina. Only two countries in Latin America – Brazil and Chile – performed a significant and sustained income support effort. However, only for Chile there is empirical evidence that the support was actually effective in keeping people at home and reducing the spread of the disease. In that regard, the size of the informal economy in Latin America is probably the single most important factor behind the inefficiency of such programmes, with informal workers still going to work, despite receiving government subsidies.

Budget Deficit-to-GDP Ratio



Source: IMF, World Economic Outlook October 2020

INFORMAL ECONOMY UNDERMINES GOVERNMENTS' INCOME SUPPORT PROGRAMMES

9.1%

Regional GDP contraction in 2020

In some countries, such as Peru, Paraguay, Ecuador and Colombia, the informal sector was larger than the formal economy, accounting for more than 50% of the total non-agricultural employment. Besides informality, the urgent need to invest in public health infrastructure, the highly regressive tax systems and the high income inequality all sabotaged government efforts to efficiently support those most in need.

In October 2020, The United Nations Economic Commission for Latin America and the Caribbean (ECLAC), one of the most prestigious think tanks on the continent, evaluated the extent of the economic damages from the COVID-19 pandemic. For ECLAC, the COVID-19 crisis is the worst regional economic crisis since the external debt crisis of the 1980s when most Latin American countries suffered severe GDP contractions and rampant inflation. Some 2020 figures are just staggering - regional GDP is expected to contract by 9.1% y/y, which is the worst decline since ECLAC started keeping record in 1900; unemployment might reach 13.5%; and poverty is seen rising by 7 pp to 37.7%.

According to ECLAC, one of the factors behind the huge economic contraction for the region in 2020 is the sharp decline in aggregate demand. A major drop in external demand for commodities also played a role in some – but not all – of these countries. The countries most affected by the plummeting external demand for commodities were those with relevant domestic production of oil and oil derivatives, such as Colombia and Mexico. Those specialised in agricultural commodities or metals, on the other hand, such as Brazil, Argentina, Peru and Chile, were less affected. The nosedive of inbound tourism revenues, however, had devastating consequences across the region, although again Colombia and Mexico suffered the most.

Budget deficits increased across Latin America, following the growing expenses on health and support programmes for households and businesses, and the sharp drop in revenues caused by the virtual paralysis of economic activity and the launch of tax relief initiatives in some countries. The region will end 2020 with an average public deficit of 8.4% of GDP according to ECLAC, the highest figure since at least 1950. Fortunately, ample international liquidity and historically low interest rates are helping most countries in Latin America to finance this huge deficit with debt issuances at a reasonable cost. The single exception from this is Argentina, which is in the middle of a severe debt crisis and is struggling to return to international debt markets. In this context of ample access to financing and subdued inflation, monetary policy in the region has mostly been highly accommodative, marked by record-low monetary policy rates in countries such as Chile, Peru and Brazil, which operate under inflation targeting regimes. In other countries with more conventional monetary aggregates targeting (e.g. Bolivia and Uruguay), there have been significant efforts to increase liquidity and reduce rates.

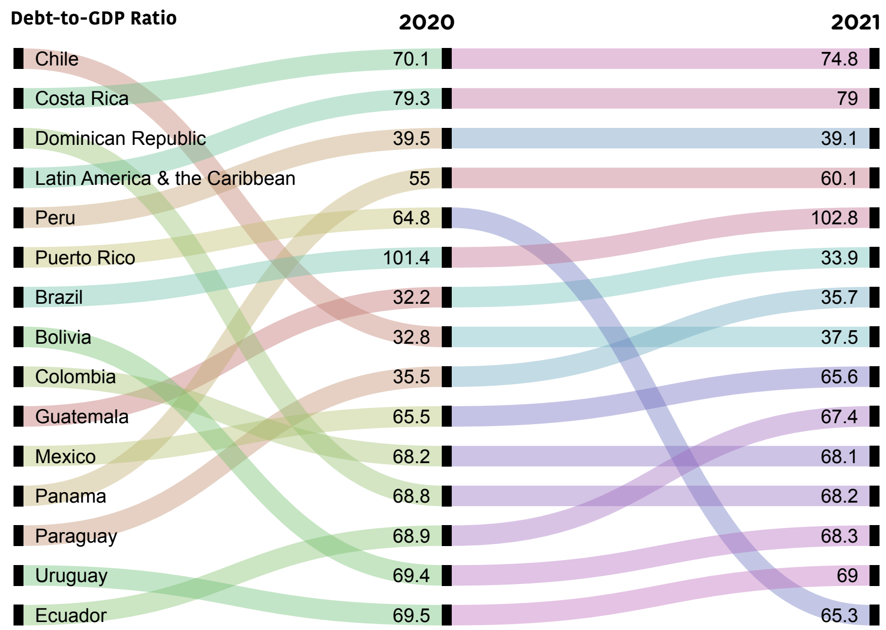
The New Normality

As 2020 is heading to a close, most countries in Latin America are in a state of new normality, with no national lockdowns in place, and relatively milder restrictive measures in spite of the ongoing pandemic. Moreover, in an effort to propel economic recovery, countries which had imposed bans on the entry of foreign tourists (e.g. Chile, Argentina and Peru), are planning to reopen their borders by no later than January 2021. Yet one question arises – how fast will Latin American economies bounce back from the crisis in this context of new normality? In October 2020, the IMF sparked some hope for the region, projecting an improved economic outlook in the last two months of 2020 and early 2021. This is supported by the good performance of the Chinese economy and the better-than-expected international demand for metal and agricultural commodities, which helps countries that depend on exports of these products (i.e. Chile, Peru, Brazil and Argentina) to rebound faster.

Still, the IMF expects the economy of Latin America to grow by just 3.6% y/y in 2021. This means that after registering the steepest contraction among the developing world in 2020 as per the IMF estimates, the region is also headed for one of the slowest recoveries in 2021.

AFTER THE STEEPEST CONTRACTION IN 2020, LATIN AMERICA IS HEADED FOR A SLOW RECOVERY

The economic rebound will largely depend on the ability of governments to sustain the programmes that support internal demand during the new normality phase, with many nations at risk of having to discontinue or curtail such programmes too early. Most countries in the region are still suffering from high unemployment, rising bankruptcies among SMEs, and structural transformations of sectors such as entertainment and physical retail, which slow down the return to the pre-pandemic reality. A prominent example is Argentina, which in 2020 will apply stimulus measures amounting to 3.5% of GDP. The country cannot afford to extend these measures in 2021, due to the need to put its public finances in order – in fact, Argentina suspended its main household support programme in September 2020. Ecuador is facing similar challenges – with debt at 68.9% of GDP in 2020, it needs to show fiscal discipline in order to lure back creditors. Another country with poor recovery prospects, but for entirely different reasons, is Mexico. The country faces no major international financial constraints for running a larger budget deficit. However, President Lopez Obrador's administration has adopted a fiscally conservative stance. This, coupled with the large share of the troubled oil and tourism sectors in the Mexican economy, shapes a slow and painful road to recovery.



Source: IMF, World Economic Outlook October 2020

Two Paths Ahead

Although Latin America had the luxury of time to prepare for the imminent threat, it was among the regions hardest-hit by the massive supply and demand shock that COVID-19 brought to the world. The pandemic also outlined multiple structural deficiencies of the economies in the region: underfunded healthcare systems, low levels of export diversification, regressive tax schemes, small or non-existent household support programmes, high labour informality, and political opportunism. Due to the extent of the economic damage in 2020, the outlook for 2021 indicates a sluggish recovery at best, even without considering a potential second wave of the pandemic. For those countries with fiscal space - Chile and Mexico in particular - higher public spending and public investment might be the best option to boost economic recovery. However, for other countries with relatively severe debt problems, such as Brazil, Ecuador and Argentina, the best – and, perhaps, the only pathway to economic recovery in 2021 – is to seize the export opportunities stemming from the robust demand for commodities by China and other countries in Asia. ISI

3.6%

Latin America's GDP growth in 2021

04 Latin America

START-UPS STEERING BRAZIL'S DIGITAL TRANSFORMATION

Adriano Morais, Research Economist, Brazil

As the COVID-19 pandemic continues to rage across the world, forcing many businesses to stay closed for months, digital technologies have come to the rescue of many. With online shopping, virtual meetings and digital services taking centre stage in the lives and livelihoods of people and companies around the globe, businesses that were quick to adopt digital technologies were the ones that managed to weather the crisis. In Brazil, start-ups proved to be the engine driving the digitalisation of the country's economy. Their reliance on digital technologies will help start-ups withstand the COVID-19 crisis and even emerge stronger.

The economic recession of 2015-2016 had a significant and long-lasting impact on the Brazilian labour market, provoking some skilled workers to venture out as entrepreneurs in unexplored segments with high growth opportunities. Not scared of uncertainty and having to think out of the box, these people formed innovative start-ups, for the majority of which digital technologies were the most obvious choice because of their low costs and high potential. Some technological start-ups have been very successful in providing efficient services, disrupting traditional business models, and adding new digital paradigms to the Brazilian business environment.

Growing Popularity

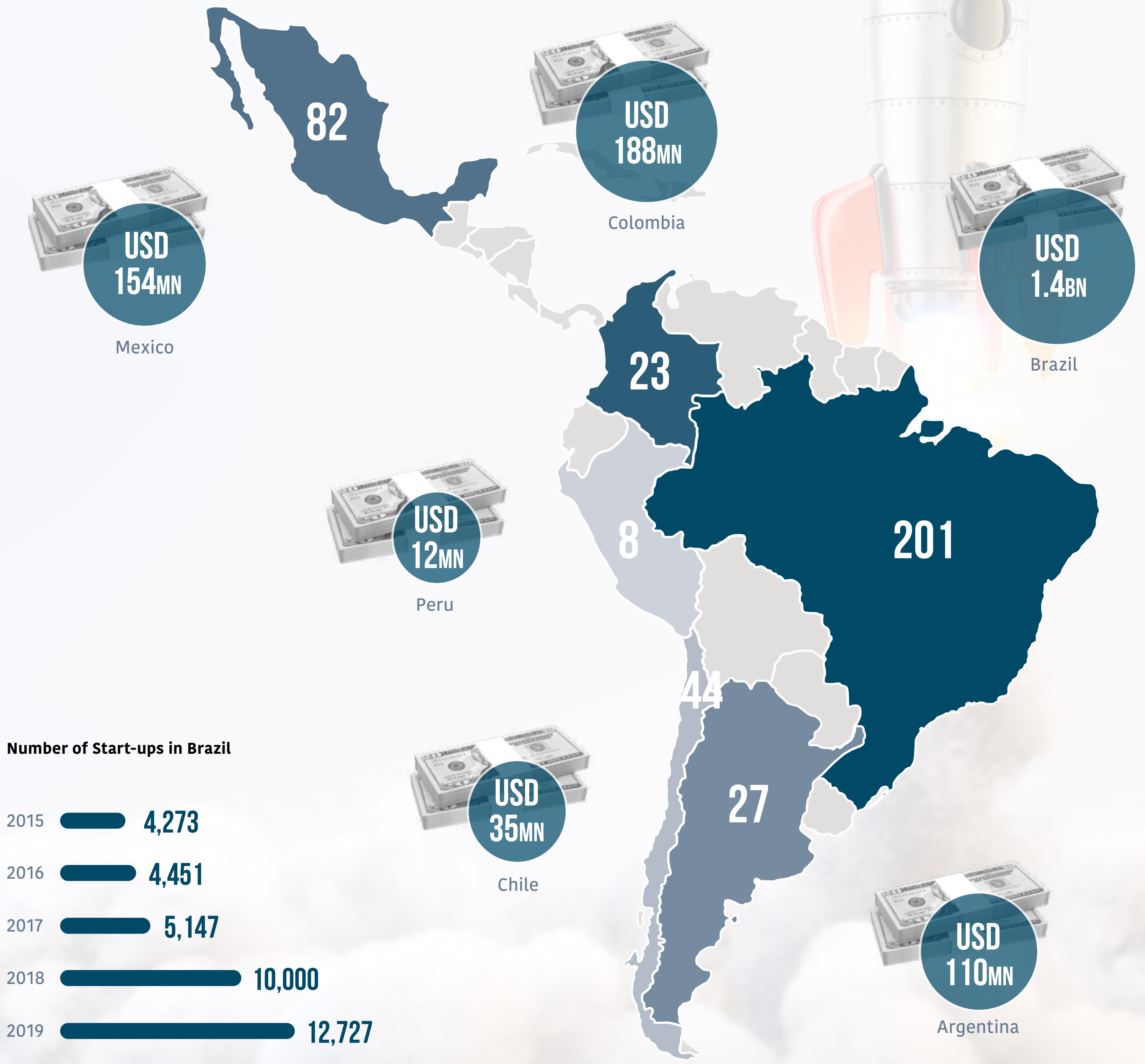
Between 2015 and 2019 the number of start-ups in Brazil grew by 186%. They have flourished in many industries and have attracted the attention of investment funds and large business groups, which see start-ups as a possibility to enter new markets and offer new products. Start-ups are perceived as lean and informal structures, not adverse to risk and open to new ideas. This often makes them lucrative investment targets for large companies willing to stimulate innovations in their internal processes. Some of these big firms even created start-up accelerators, which provide physical structure, mentorship programmes, financial resources and the possibility to make a contract with the sponsoring company. Start-ups attracted more than half of venture capital investments in Latin America in 2019, according to data published by The Association for Private Capital Investment in Latin America (LAVCA). Out of the USD 4.6bn invested in all sectors in Latin America in 2019, USD 2.6bn were allocated to start-ups. For comparison, in 2018 venture capital investments in Latin American start-ups totalled USD 2bn.

START-UPS ATTRACT OVER HALF OF VENTURE CAPITAL INVESTMENT IN LATAM IN 2019

PRIVATE CAPITAL INVESTMENTS IN LATIN AMERICA'S START-UPS, JAN 2017-JUN 2018

186%
Growth in number of start-ups in 2015-2019

Start-ups are so popular in Brazil that 26% of students said they wanted to start their career in start-ups or big tech companies, according to a June 2020 survey by venture capital firm Atlantico.



Number of Start-ups in Brazil

2015	4,273
2016	4,451
2017	5,147
2018	10,000
2019	12,727
2020*	13,344

*Until Nov 18, 2020
Note: Number of start-ups attracting investments in Jan 2017-Jun 2018

Source: Brazilian Association of Start-ups (ABSTARTUPS)

Agritechs

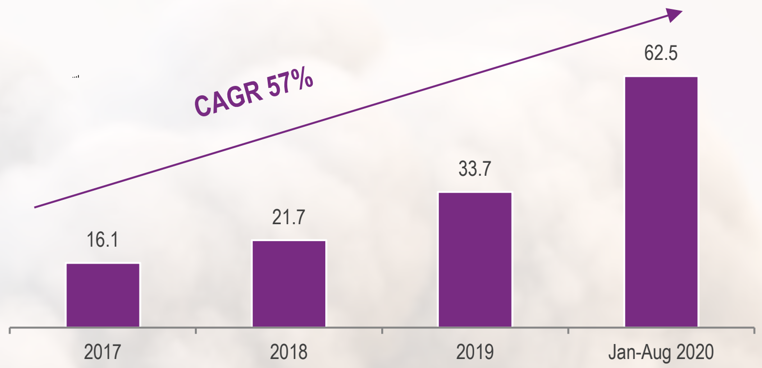
In the agriculture sector – one of the most traditional sectors of the Brazilian economy – agritech start-ups are implementing innovations in rural areas in the fields of precision agriculture, food traceability and farm management. One such company is NetWord Agro. Created in 2017, it offers a soil and crop monitoring technology that detects the need of irrigation and fertilisers and determines which plants have to receive pesticides, avoiding the application of the product on safe plants. Other agritech start-ups offer a variety of technologies of farm production monitoring, using satellites and drones integrated with meteorological data, sensors and cameras on tractors and combine harvesters, and even platforms with artificial intelligence to optimise farm activities.

Edtechs

In the education sector, edtech start-ups are creating innovative solutions to improve the learning process, such as software development, digital platforms and educational games. In addition, start-ups also offer online courses of professional and corporate education, preparatory exams for university entrance, and even price comparisons among different courses, private schools and universities. As an example, corporate education start-up Niduu, founded in 2017, uses technologies such as micro learning, data intelligence and mobile learning to develop gamified applications for training the client's employees. Another example is the platform Shapp, created in 2017, which connects students and private teachers for online or face-to-face classes. Amid the COVID-19 pandemic, from March to May 2020, the number of teachers registered on the Shapp platform doubled to 2,000. The success of education start-ups is also evident in the strong interest of investors – in the first eight months of 2020 venture capital raised by education start-ups in Brazil reached USD 62.5mn, nearly double the funding raised in full-2019, according to data published in Atlantico's Latin America Digital Transformation Report 2020.

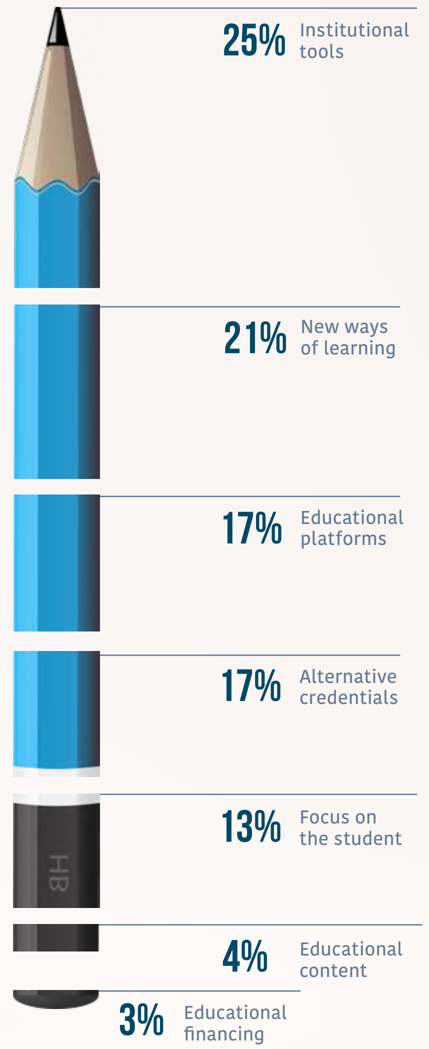
OF THE 1,864 VENTURE CAPITAL DEALS IN BRAZIL IN 2010-2019, 114 WERE WITH EDUCATION START-UPS

Venture Capital Raised by Education Start-ups in Brazil, USD mn



Source: Atlantico's Latin America Digital Transformation Report 2020, Distrito Edtech Report 2019, Pitchbook

BREAKDOWN OF EDUCATION START-UPS



Fintechs

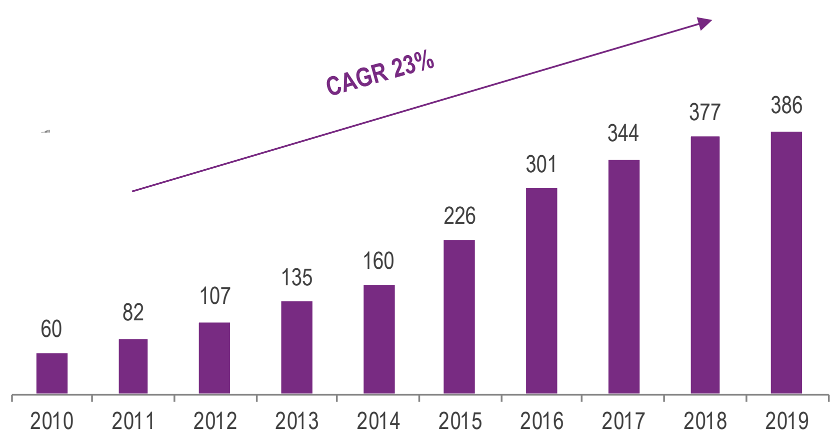
In the banking industry, fintech start-ups utilise digital platforms to offer financial services such as credit cards, loans, insurances and financial management. A prominent Brazilian fintech start-up is Rebel. Founded in 2016 and specialising in the provision of unsecured credit to middle class citizens in the country, Rebel has been listed as one of the 50 most innovative emerging fintechs in the world in a ranking compiled by consultancy KPMG and Australian venture capital firm H2 Ventures. Rebel uses a credit evaluation technology which scans the internet to find information about the borrowers, and infer their capacity to pay loans. The company has an artificial intelligence model which analyses up to 2,000 variables per applicant, such as the characteristics of their neighbourhood through photos on Google Street View. Rebel also has a financial education programme. The clients who watched videos and read information about financial education on the platform can earn points to improve their credit score. Many other fintechs use artificial intelligence and machine learning tools in segments other than loans, such as insurance, credit cards, financial planning and business accounting.

Healthtechs

In the healthcare sector, healthtec start-ups offer digital solutions to support medical prescriptions, diagnostics and the management of clinics and hospitals. Such companies are Conexa and Neomed. Conexa, founded in 2016, is a telemedicine platform that connects patients and doctors. It offers an integrated system of scheduling, patient monitoring, electronic medical records and digital receipts. Neomed, which was established in 2017, offers a marketplace that connects doctors and laboratories to speed up the process of medical exam reports. The registered doctors can work remotely to write reports for exams, reducing costs for laboratories and clinics, and delivering the reports faster. The doctors can also count on an artificial intelligence algorithm to make a previous screening of each exam and help them to make the diagnostics. The number of healthcare start-ups increased at a CAGR of 23% over the 2010-2019 period.

NUMBER OF HEALTHCARE START-UPS RISES AT CAGR OF 23% IN 2010-2019

Number of Healthcare Start-ups in Brazil



Source: Atlantico's Latin America Digital Transformation Report 2020, Distrito Edtech Report 2019, Pitchbook

The success of digital platforms and their flexibility allowed them to diversify their services during the pandemic and explore new market segments. An interesting case is the taxi and mobility app 99. Founded in 2012, the company has become Brazil's first unicorn – a privately held start-up company valued at over USD 1bn. The company was strongly affected by the social distancing measures during the pandemic, and started to allocate idle drivers to deliver packages purchased online. Even before the COVID-19 outbreak, the company had already started to diversify by offering loans and other financial services to drivers, who could pay back with a share of their revenues. Brazilian food delivery app iFood also opted for some diversification of its operations with the acquisition of online grocery marketplace platform provider SiteMercado in September 2020. SiteMercado is a white-label platform that helps grocery stores digitise their operations to work as an e-commerce business. The acquisition is expected to accelerate the expansion of iFood's grocery delivery business. iFood, one of Brazil's most innovative foodtech companies, is a leader in online food delivery in Latin America with more than 45mn monthly orders in Brazil from more than 200,000 restaurants in 1,000+ cities.

Another example of a high growth start-up is former credit card issuer Nubank, founded in 2013, which became the second Brazilian unicorn in 2018, and since then has diversified its activities to include many financial services such as loans and bank accounts. In September 2020, amid the pandemic, Nubank acquired one of the ten biggest stockbrokers of the country, EasyInvest, to start offering investment products on its platform.

The pandemic has accelerated demand for digital solutions in the Brazilian economy as a whole and has provided a boost to the business of many technological start-ups and digital platforms. Many changes brought by the pandemic will surely continue to play an increasing role in our lives, such as the higher use of e-commerce, e-learning, and telemedicine, as people tend to cut down on face-to-face interactions and try to avoid workplaces, restaurants, schools and medical offices. Therefore, start-ups in Brazil will likely remain on an upbeat trend in the next years as a powerful tool to explore new markets, ensure more efficiency for consumers and businesses, and implement innovations in traditional companies in a challenging scenario. ISI

Brazil's Unicorn Start-ups

	Start-up	Founded in	Sector	Unicorn since	First core business
1	99	2012	Transportation	2018	Digital platform
2	Nubank	2013	Financial	2018	Credit card issuance
3	Arco	2017	Education	2018	Softwares for schools
4	Stone	2012	Financial	2018	Payments
5	iFood	2011	Food delivery	2018	Digital platform
6	Gympass	2012	Physical Activity	2019	Digital platform
7	Loggi	2013	Delivery	2019	Digital platform
8	Quinto Andar	2013	Real Estate	2019	Digital platform
9	Ebanx	2012	Financial	2019	Payments
10	Wildlife	2011	Games	2019	Software
11	Loft BR	2017	Real Estate	2020	Digital platform
12	Vtex	2000	IT	2020	E-commerce solutions

Source: Folha, Company Data

04 Latin America

Mining in the Time of PANDEMIC

Nikoleta Slavcheva, Industry Researcher, Brazil

THE MINERAL EXTRACTION INDUSTRY IS A KEY ECONOMIC GROWTH DRIVER FOR MANY COUNTRIES IN LATIN AMERICA.

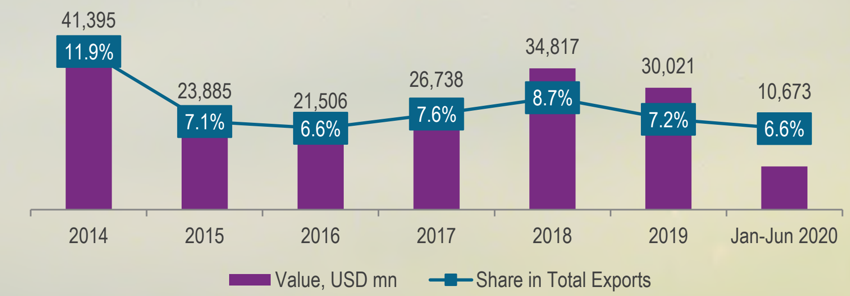
The region is a leading producer and exporter of coal, oil, iron, copper, nickel and precious metals. Thus, it is not a surprise that when the COVID-induced global economic shock sent prices of mineral commodities reeling, the finances of many countries in the region came under heavy pressure.

Given the importance of the industry for public finances and the urgency to capture revenues to fund the galloping expenses during a pandemic, governments in the region were quick to put in place measures to support the mining sector. But they differ significantly from country to country. Below we will discuss the dynamics in Mexico and Colombia, and how the decisions of the two governments may impact the post-pandemic prospects of their mineral extraction sectors.

Essential, Non-Essential

Latin America's second biggest oil and gas producer, Mexico, is also a leading producer of silver, copper and lead. It ranks among the world's top ten producers of gold and molybdenum, too. Yet, mining was not classified as an essential activity for the economy and when the government announced a two-month lockdown at end-March 2020 to contain the spread of the virus, mines were ordered to close. In mid-May, however, the government changed its stance, following pressure from the industry which claimed that the closure of mines breaches the requirements of the free trade agreement Mexico has with the US and Canada. The agreement mandates that a member country cannot delay the production of any component, if this affects the value chain of the other countries. After mining was reclassified as an essential sector, mines started to gradually resume operations. According to August 2020 estimates by Mexico's mining chamber CAMIMEX, the sector lost USD 2bn in production value and USD 2.8bn in exports as a result of the suspension of activities in April and May 2020.

Mexico's Extractive Industry Exports



Source: INEGI

Government Darling

And while the mining sector as a whole might not have felt the full support of the government, there was one segment that was unconditionally backed by the state – oil exploration and production. The administration of President Andres Manuel Lopez Obrador is determined to continue supporting Petroleos Mexicanos (PEMEX), pouring billions of US dollars into the indebted and loss-making state oil champion.

MEXICO IS DETERMINED TO SUPPORT PEMEX AT ALL COSTS

Back in the 1990s and the beginning of the 2000s, PEMEX pumped more oil than any other Latin American company, and was also the leading exporter of crude oil in the Americas. Yet, years of underinvestment in exploration, in addition to depletion of the country's principal producing areas – the shallow waters Ku-Maloob-Zaap and Cantarell complexes – have sent crude production in a constant decline since 2005. As a result, PEMEX' contribution to the federal budget nosedived from 34.5% of total tax revenue in 2011 to only 7.7% in 2019. To counter these trends, the government enacted a constitutional amendment in 2013 to open up the sector and end PEMEX' 75-year monopoly. The reform was expected to give Mexico the opportunity to unlock massive oil reserves in the Gulf of Mexico and allow PEMEX the access to capital, technology and know-how needed to boost its long-term prospects. In 2016, for the first time since Mexico nationalised the oil industry in 1938, other companies than PEMEX were allowed to import, distribute and sell fuels. Ever since, the country has seen oil majors such as Royal Dutch Shell, BP, Chevron and Exxon Mobil building thousands of petrol stations. However, the election of leftist Obrador as president in 2018 has set the stage for significant changes. A harsh critic of the energy reform, Obrador has vowed to restore the national oil company to its former glory by helping it recover the oil production, modernise its refineries and fertiliser plants, and build a USD 8bn refinery complex. Obrador re-centred the nation's focus on the development of PEMEX, claiming that the energy reform of his predecessor Enrique Pena Nieto had failed to yield positive results. In February, the government announced a rescue package for PEMEX that includes a USD 3.9bn capital injection in addition to tax cuts. When in late-March the government shut down all non-essential businesses, crude oil production was spared. Yet, the slump of oil prices

USD 26.3BN
PEMEX' loss in H1 2020

04 Latin America

caused by the reduced global demand forced PEMEX to suspend as much as 45 service contracts worth USD 160mn in June 2020, looking to cut expenses. To ensure PEMEX' continuing operations during the pandemic, the government allocated USD 4.5bn in financial aid in the first half of 2020, Fitch Solutions estimated. Yet, PEMEX' performance continued to deteriorate progressively. The company's net loss for the first nine months of 2020 reached USD 26.3bn, more than three times the loss recorded in the same period of 2019.

On top of this unsatisfactory performance, PEMEX ended H1 2020 with a net debt of USD 105.5bn, more than any other oil company in the world. Two of the three global rating agencies – Moody's and Fitch Ratings – have already cut the debt of PEMEX to junk status, a move that will substantially increase the financing costs for Obrador's pet project.

Still, the government seems determined to continue supporting PEMEX and the financial support in 2021 may even increase. What's more, in September 2020 Obrador said he may roll back the 2013-2014 energy sector liberalisation in 2021 if he is unable to rescue PEMEX with existing laws. Hence, if oil demand and prices do not recover in 2021, the obsession of the Mexican government with saving PEMEX may plunge the country into a fiscal nightmare.

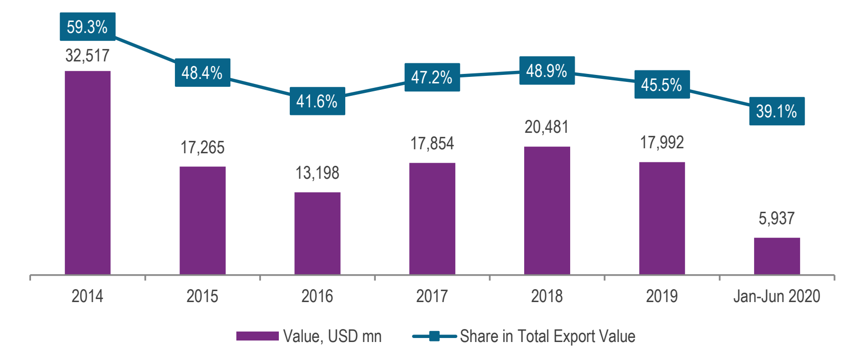
A Different Story

The Colombian government had a very different approach towards mineral extraction activities in the face of the rising concerns related to the spread of COVID-19. First, mining and oil & gas exploration and production were exempt from the full shutdown imposed on many businesses in the country when a national lockdown was announced in mid-March. In addition, in April 2020 the government allowed the postponement of surface rights payment for 15 working days after the end of the mandatory quarantine measures. Furthermore, in June 2020 it provided financial support measures to back the continuing activities of small-scale and traditional miners, as well as tax incentives focused on the promotion of investments in mineral and hydrocarbon exploration.

Despite all measures taken, the COVID-19 pandemic had a major negative impact on Colombia's mineral extraction industry, mainly because of its extreme focus on coal and oil - revenues from these two commodities are subject to wide swings resulting from fluctuations in the global energy market. Notably, the coal and the oil & gas segments generated 5.6% of the country's GDP in 2019. That share fell to 4.1% in the first half of 2020. As a result of the slump of international commodity prices, Colombia's exports of coal and oil fell by 38.8% y/y in the first eight months of 2020, which led to a 24.3% y/y contraction of total exports.

COLOMBIA'S COAL AND OIL EXPORTS DOWN BY 38.8% Y/Y IN JAN-AUG 2020

Colombia's Extractive Industry Exports



Source: DANE

A Golden Opportunity

However, there have been some positive news for Colombia's mining in 2020. Rising demand for gold and copper has been a welcoming news for Colombia, Latin America's fourth biggest gold producer and the sixth-largest copper miner. The economic recession sparked by the COVID-19 outbreak resulted in a surge in gold prices in H1 2020 as the mineral benefits from its image as a safe haven for investors in periods of uncertainty. At the same time, the ongoing transition towards increasing the share of cleaner energy sources has helped international copper prices remain stable in an overall pandemic environment.

The rise in international gold prices could not have come at a better time for Colombia. The country has four large-scale gold and copper mining projects due to start commercial operations between 2020 and 2024, which could help double its gold output in that period. The first projects, scheduled to come online in early 2021, are Buritica and Gramalote in the Antioquia and Norte de Santander departments, respectively. These two projects are expected to add at least 19.8 tonnes of gold per year to the country's output, representing a 54% increase from 2019. Overall, gold mining is set to receive more than USD 3.4bn in investments over the 2020-2024 period for the development of the Gramalote, Buritica and Soto Norte gold projects. Soto Norte, located in the Santander department, is still awaiting its environmental licence but could start commercial operations in 2024, adding 11.4 tonnes of gold to the country's output. Besides gold, copper is also expected to see a surge in its production levels in Colombia. The Quebradona mine, a gold-copper project in the Antioquia department, is scheduled to start commercial operations in 2023 and is expected to double the country's copper output as of 2019.

In addition to supporting large-scale gold projects, the government has also been active in curbing illegal mining operations, often associated with violence and practices generating risks to the environment and the human health. In doing so, the government has started legalising traditional and subsistence miners across the country. As part of these efforts, in July 2020 the Mining Agency (ANM) launched GENESIS, a digital platform for the registry of subsistence or traditional miners in Colombia. Subsistence mining is defined as mining that involves only manual tools, with no machines or explosives. In October 2020, the Ministry of Mines and Energy published a decree to facilitate the legalisation of small miners, allowing holders of mining titles to voluntarily renounce or return part of the concession area affected by illegal mining operations and hand it over to the mining authority so that it can deliver the said area to miners who do not have title but were already present in the area. The national legalisation policy aims to regulate the status of around 27,000 miners before the end of 2022. According to official figures, more than 10,000 miners had already started the process by the end of 2019.

COLOMBIA TO LEGALISE STATUS OF 27,000 SMALL MINERS BY END-2022

Shifting the Focus

The extreme dependence of Colombia's mining industry on a few minerals, despite the country's significant geological potential, is a deeply rooted problem, and has various explanations. Years of armed conflict with guerrilla groups have left about half of the national territory economically underdeveloped and geologically non-explored. Other challenges include a widespread illegal mining and a complex and often contradictory regulatory framework for mining exploration. The lack of significant new oil discoveries and the global trend toward the substitution of coal-fired electricity generation plants with greener energy sources have prompted the government to look for alternatives and try to diversify the industry. Oddly enough, the COVID-19 crisis might turn into the long awaited breaking point that drives the positive change in Colombia's mining exploration.

Adequate or not, the outcome of the measures taken by the governments to support the mining industry is yet to be evaluated. Yet, most measures, from direct financial support for troubled oil companies to diversification of exploited minerals, are very similar to the steps taken in difficult periods in the past – they are largely focused on further expanding the output in order to compensate for falling prices, or conversely, to take advantage of high prices. Hence, they are not likely to cause any significant structural changes and reduce the large dependence of the region on mineral commodities exports. In order to prepare for the post-pandemic realities, governments must re-evaluate the engines of economic growth. In the case of mining, this might be the right time to adopt a clear regulatory environment to foster investments without sacrificing the environment and to restructure the industry so as to generate revenues without sacrificing the needs of local communities. This might also be the right time for governments in the region to rethink the mining industry value chain in order to transform the countries from input suppliers, exposed to the volatilities of commodities prices, into manufacturing hubs. ISI

PANDEMIC MAY TRIGGER THE LONG-AWAITED TRANSFORMATION OF COLOMBIA'S MINING SECTOR

A LOOK BACKSTAGE

Picking a title for the 2021 edition of EMIS Foresight was harder than ever before. We were unanimous as to the main topic of the magazine, but for a long time could not strike the right note, as we were torn between compassion for the COVID-19 victims, concern about the global economy, and fear for our health and that of our loved ones. We oscillated from hope to despondency, but kept focusing on opportunities that proved there was a way forward. We hope that our title pickings will add colours to the mental picture you have painted of the hard year that is behind us, and of the better ones that lay ahead.

ISI Emerging Markets Group

EMIS CEIC

Disclaimer:

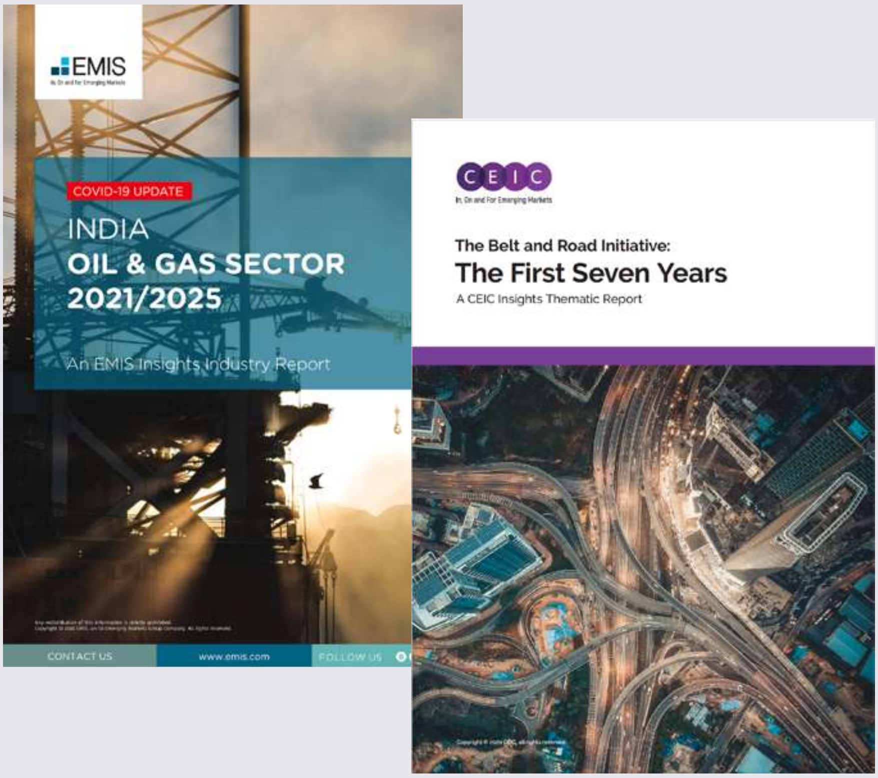
The material is based on sources which we believe are reliable, but no warranty, either expressed or implied, is provided in relation to the accuracy or completeness of the information. The views expressed are our best judgment as of the date of issue and are subject to change without notice. ISI Emerging Markets takes no responsibility for decisions made on the basis of these opinions.

Any redistribution of this information is strictly prohibited.

ISI Emerging Markets Group

EMIS CEIC

WE PUBLISH



- 300+ reports per year
- 25+ markets
- 40 industries
- 3 languages - English, Chinese, Portuguese

GET ACCESS

EUROPE HEADQUARTERS

14 New Street
London
EC2M 4HE
United Kingdom

Voice: +44 20 7153 1205
europe@isimarkets.com

AMERICAS HEADQUARTERS

12 East 49th St,
8th Floor, New York
NY 10017
United States

Voice: +1 212 610 2900
americas@isimarkets.com

ASIA HEADQUARTERS

15/F V-Point
18 Tang Lung Street
Causeway Bay
Hong Kong SAR of P.R.China

Voice: +852 2591 3379
asia@isimarkets.com