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WESTERN HEMISPHERE

Navigating Tighter Global Financial Conditions

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Preface

The October 2022 *Regional Economic Outlook: Western Hemisphere* was prepared by Santiago Acosta-Ormaechea with contributions from Maximiliano Appendino, Isabela Duarte, Chao He, Takuji Komatsuzaki, and Samuel Pienknagura, under the supervision of Anna Ivanova and the guidance of Gustavo Adler, with the overall direction of Ilan Goldfajn and James Morsink. Genevieve Lindow provided outstanding support and coordinated the excellent research assistance work of Evelyn Carbajal, Erdem Dorjkhand, Kenji Moreno, and Gabriel Moura Queiroz. Contributions for boxes and country focus were provided by country teams and coordinated by Metodij Hadzi-Vaskov, Andrew Edward Hodge, Lucy Qian Liu, Adam Siddiq, Bert van Selm, and Joyce Wong. Annexes 4 and 5 were prepared by Yorbol Yakhshilikov and Yuanchen Yang, respectively. The report includes content from three background papers—available online at http://www.IMF.org/Americas—that benefited from the guidance of Jorge Roldós in the initial stagesprepared by Santiago Acosta-Ormaechea, Maximiliano Appendino, Isabela Duarte, Chao He, Takuji Komatsuzaki, Samuel Pienknagura, and Yuanchen Yang. Astrid Baigorria, Rafael Machado Parente, Flavien Moreau, Hyunmin Park, Ana Sofia Pires Mendes Abranches Pessoa, Rafael Portillo, Aneta Radzikowski, and Pedro Rodriguez provided production support. The report also benefited from the coordination of editing and production by Cheryl Toksoz, from the Communications Department. Translations to other languages (Spanish and Portuguese) were led by Virginia Masoller, Vanesa Demko, Eric Fernandes Macedo, and Carlos Viel. This report reflects developments and staff projections through September 26, 2022.

Outlook for the Western Hemisphere: Navigating Tighter Global Financial Conditions

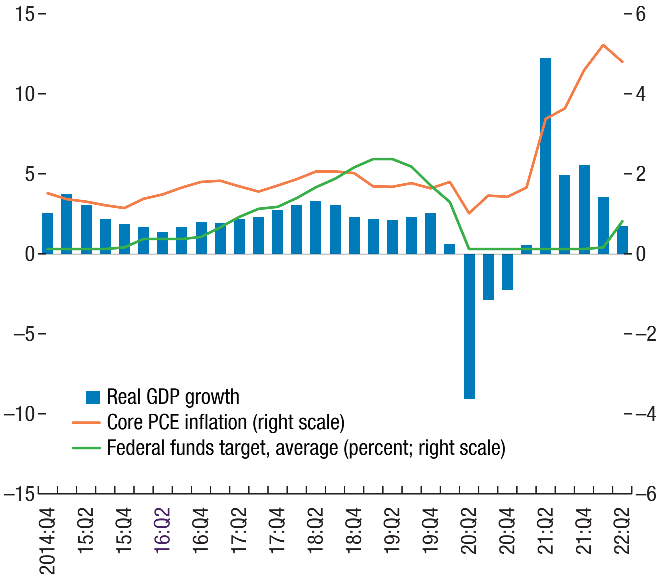
Recent developments in the Western Hemisphere—that is, the United States/Canada and Latin America and the Caribbean (LAC)—have been dominated by the impact of two distinct global shocks: the COVID-19 pandemic and then the Russian invasion of Ukraine. A third shock—the tightening of financial conditions—is now shaping the outlook. After contracting sharply in 2020, most of the Western Hemisphere' economies recovered strongly in 2021 and early 2022, helped by the global recovery, the normalization of service sectors, and booming commodity prices. However, inflation pressures built up with pandemic-related disruptions, expansionary policies, rebounding demand, and the impact of the war in Ukraine on energy and food prices. The swift response of LAC's monetary authorities to rising inflation—well ahead of other economies—helped contain price pressures and keep long-term inflation expectations anchored, but inflation remains high. Amid global monetary and financial tightening, and the ensuing slowdown in global growth and softening of commodity prices, activity is expected to decelerate throughout the Western Hemisphere in late 2022 and 2023, while inflation pressures are expected to recede gradually. Downside risks dominate the outlook and stem from tighter financial conditions, a more pronounced global slowdown, and entrenched inflation. For LAC, a sharp fall in commodity prices and social unrest are important risks. With inflation yet to abate and most economies still operating at or near potential, monetary policy should avoid easing prematurely and must stay the course. Clear communication of policy intentions will be key to reducing uncertainty and keeping inflation expectations anchored. Fiscal support deployed to mitigate the impact of inflation on the most vulnerable should be accompanied by compensating measures, where fiscal space does not exist, but also support monetary authorities' efforts to tame inflation. Given rising financing costs, strengthening fiscal frameworks and advancing with inclusive fiscal consolidation—that protects key social objectives—will be essential to credibly putting public debt on a firm downward path while ensuring social stability. Boosting LAC's medium-term growth requires raising productivity and good-quality public and private investment. Supply-side policies should focus on strengthening human capital, simplifying and modernizing labor regulations, and lifting barriers to firm entry and exit.

US Outlook and Policies

The US economy recovered strongly from the most acute phase of the pandemic, expanding by 5.7 percent in 2021 (Figure 1) and bringing activity close to the prepandemic trend in that year. Strong private consumption and investment drove the recovery, supported by highly accommodative monetary and fiscal policies. Employment rebounded rapidly, bringing the unemployment rate down to end-2019 levels by early 2022, but the participation rate remains below prepandemic values, mainly due to early retirements.

Initially, inflation was limited to items affected by supply-chain disruptions, but it has become more broad-based since late 2021. Core personal consumption expenditure inflation rose to 5.3 percent year over year in February 2022 and stayed elevated although declined somewhat to 4.6 percent year over year in July (Figure 1). The acceleration of prices was accompanied by a rapid depletion of economic slack, persistent supply-chain disruptions, and labor shortages. The war in Ukraine exacerbated price increases for energy and food. A pickup in wage growth, initially limited to lower-income workers, has become broad-based since late 2021, with the employment cost index of private sector wages and salaries growing by 5.7 percent year over year in the second quarter of 2022, but real wages have continued falling for most US workers.

Figure 1. United States: Real GDP Growth, Core PCE Inflation, and Federal Funds Target Rate
(Year-over-year percent change; unless noted otherwise)



Sources: IMF, World Economic Outlook database; US Federal Reserve; and IMF staff calculations.
Note: PCE = personal consumption expenditure.

The Federal Reserve halted net asset purchases in March 2022, began reducing the size of its balance sheet in June, and has increased policy rates by 300 basis points since February with the goal of bringing inflation back to the 2 percent objective and ensuring that long-term inflation expectations remain well anchored. The Federal Reserve also signaled its expectation to increase the federal funds rate quickly to about 4½ percent, implying that positive ex ante real rates would be reached by late 2022, according to the median projection of Federal Open Market Committee participants. Although this rapid monetary policy tightening has helped anchor long-term inflation expectations, elevated short-term inflation expectations are a cautionary tale. Fiscal policy is becoming substantially less accommodative as the exceptional fiscal support implemented in 2020–21 expires, and the general government fiscal deficit falls by about 7 percentage points of GDP in 2022. The tightening of monetary policy and the signaling of further rate increases have led to a significant tightening of financial conditions, including an increase in Treasury yields, and sell-offs on equity and bond markets. The US dollar has appreciated by about 13 percent on a nominal effective basis since its trough in mid-2021.

Growth is expected to slow to 1.6 percent in 2022 as tighter financial conditions weigh on demand. Private consumption growth slowed to an annualized 1½ percent in the second quarter of 2022 from 2½ percent in the fourth quarter of 2021 and is expected to drop to almost zero by early 2023 as falling real incomes and depleted savings begin to constrain spending. Real GDP growth is projected to slow to 1 percent in 2023. Weaker demand is expected to weigh on imports, with the current account deficit narrowing from 4¾ percent of GDP in the first quarter of 2022 to about 3 percent by the end of 2023. The slowing economy is projected to raise the unemployment rate to more than 5 percent by 2024, leading to softer wage and price pressures, which are expected to lower core personal consumption expenditure inflation to about 2½ percent by end-2023. However, if inflation proves more persistent than currently expected, the Federal Reserve would need to tighten monetary policy more, and growth prospects would worsen.

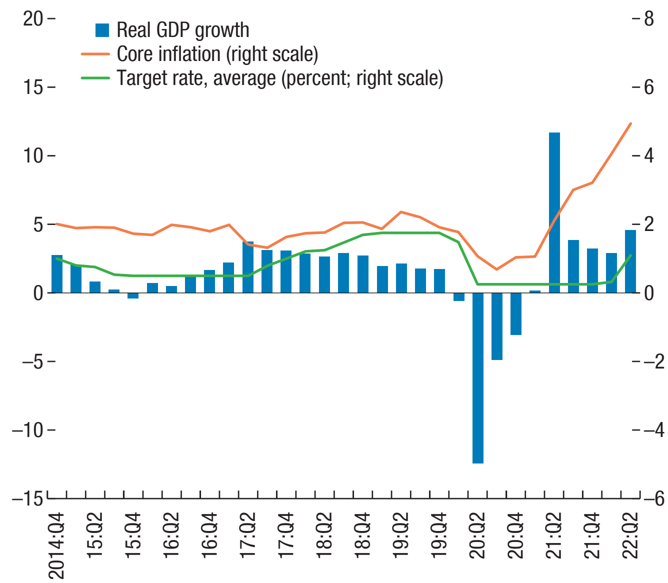
Supply-side reforms are needed to boost productivity, expand the labor force, and reduce poverty. Implementing supply-side measures proposed by the US administration could help boost labor force participation, innovation, and productivity. These include expanding public support for childcare, increasing migration, investing in infrastructure, providing a more expansive earned income tax credit, increasing educational opportunities (particularly for low-income students), and improving funding for apprenticeships. Also, introducing paid family leave; making a well-targeted, refundable child tax credit a permanent feature of the safety net; and expanding health care coverage and food assistance for lower-income families would make inroads into reducing poverty. Achieving the US administration's climate goals requires a multipronged strategy that combines broad-based carbon pricing, sectoral "feebates" (tax/subsides for above/below average emissions), regulatory actions, and the elimination of subsidies for fossil fuels and carbon-intensive agriculture. The recently passed Inflation Reduction Act includes some of these elements, but achieving the US climate goals requires additional action.

Canada Outlook and Policies

Canada's economy continues to recover from the pandemic, but the rebound has been accompanied by accelerating inflation. After a 5.2 percent contraction in 2020, real GDP expanded by 4.5 percent in 2021 and reached its prepandemic level by the end of the year because of unprecedented policy stimulus and a successful rollout of COVID-19 vaccines (Figure 2). The economy continued to grow rapidly in the first half of 2022, driven by strong household consumption owing to an increasingly tight labor market and robust business and residential investment. The unemployment rate fell to a record low of 4.9 percent in July before increasing to 5.4 percent in August. Labor force participation has returned to its prepandemic level, and elevated job vacancies are driving up wage growth. With strong domestic recovery, surging commodity prices, and global supply challenges, consumer price index inflation has become more broad-based and reached a 40-year high of 8.1 percent in June before moderating to 7.0 percent in August. While medium- and long-term inflation expectations of households and businesses remained stable, shorter-term inflation expectations have risen significantly.

Growth momentum is expected to wane in the near term, amid a slowing global economy, tightening financial conditions, and elevated inflation, with GDP growth moderating to 3.3 percent in 2022 and 1.5 percent in 2023. Elevated inflation and rising interest rates are expected to slow private consumption and housing activity, while the weaker global outlook is weighing on exports and business investment. Headline inflation is projected to moderate to 6.9 percent by the end of 2022 and 3.2 percent by the end of 2023 as the energy and food-price shock dissipates, and excess demand responds to monetary tightening both domestically and abroad.

Figure 2. Canada: Real GDP Growth, Core Inflation, and Target Rate
(Year-over-year percent change; unless noted otherwise)



Sources: Bank of Canada; Haver Analytics; IMF, World Economic Outlook database; and IMF staff calculations.

The near-term policy priority is to address demand-supply imbalances and bring inflation back to target. With its 75 basis points hike in September, the Bank of Canada has brought the policy rate to 3.25 percent and has reiterated its commitment to price stability by signaling additional rate hikes. Given that inflation pressures remain broad-based and elevated, the Bank of Canada should continue its decisive withdrawal of monetary accommodation. Clear communication will be key to guiding the market and keeping medium-term inflation expectations well anchored. Fiscal policy should support disinflation by steadily reducing the cyclically adjusted primary deficit. To enhance fiscal credibility and transparency, the federal government could strengthen its medium-term fiscal framework by adopting a specific debt anchor, supported by an operational rule to determine how the fiscal position reverts to the debt anchor after shocks. Fiscal policy could be enhanced through the adoption of rules-based automatic stimulus. It remains necessary to continue implementing structural reforms—such as removing trade barriers, promoting infrastructure investment, and diversifying the economy beyond traditional sectors—to raise productivity. On climate transition, while Canada has already laid out ambitious plans for carbon pricing to reduce its currently high level of greenhouse gas emissions, an important challenge will be how to prepare for a world of declining demand for oil and gas, given the importance of that sector to the economy.

Latin American and the Caribbean Outlook and Policies

Recent Developments

Despite a rapidly changing external environment, the region's recovery from the pandemic continued on a firm footing in the first half of 2022, though at different speeds across subregions and accompanied by rising inflation pressures.

Activity Held Up in Early 2022

The recovery from the pandemic continued firmly in late 2021 and early 2022 as mobility generally returned to prepandemic levels, helped by high vaccination rates and mild, new COVID-19 variants. This allowed most contact-intensive sectors to reopen vigorously and service sectors to catch up with manufacturing amid a strong pickup in private consumption and exports, and a robust employment recovery.

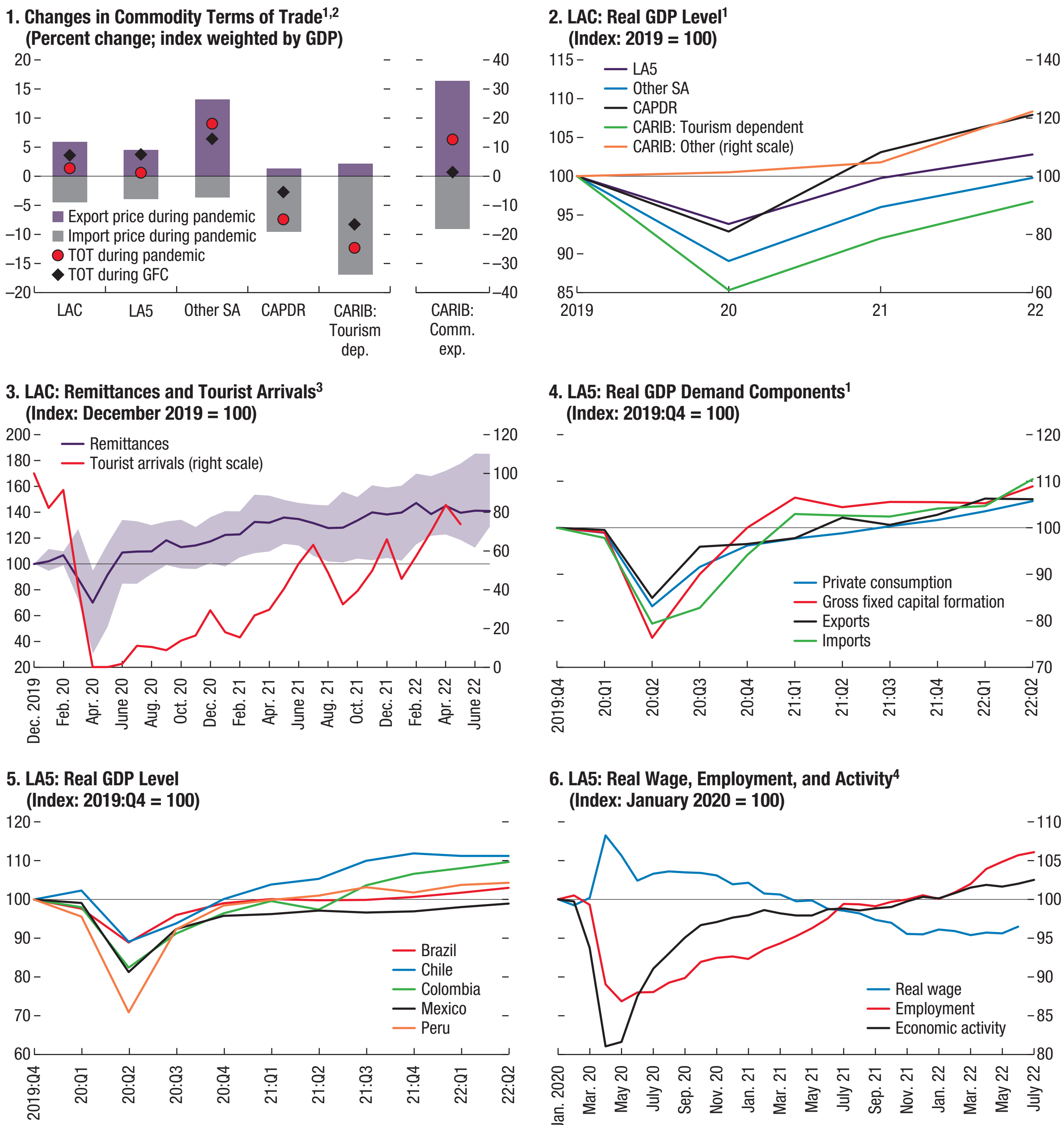
The rebound of commodity prices from early pandemic lows—propelled further by the impact of Russia's invasion of Ukraine on commodity markets—supported activity in LAC, though with heterogeneous impact across subregions. The role of terms of trade in supporting the region's recovery was similar, although less prominent, to the one played during the aftermath of the global financial crisis when food and energy prices reached historical highs (Figure 3, panel 1). In addition, the strong recovery of the United States and other key trading partners during 2021 and the still-accommodative global financial conditions through early 2022 also supported activity. This allowed GDP to surpass prepandemic levels in most subregions.

However, the recovery has been multispeed (Figure 3, panel 2). Most Latin America 5 (LA5; Brazil, Chile, Colombia, Mexico, Peru) and other South American economies continued firmly in early 2022 with the rebound initiated in 2021 supported by high commodity prices (see Box 3 for country details). Likewise, Caribbean commodity exporters—driven largely by Guyana's rapid oil sector expansion—recovered briskly on the back of high commodity export prices. In Central America, Panama, and the Dominican Republic, buoyant exports, the solid rebound of tourism—helped by the rapid US recovery—as well as policy support in some cases (Hadzi-Vaskov and Wong 2022) helped solidify the recovery in 2021 and early 2022 (Figure 3, panel 3; Box 1). Strong remittances, also driven by the rebound in activity in the United States and helped by the increased digitalization of transactions (Annex 4), further propelled the recovery, although activity has slowed more recently. Meanwhile, tourism-dependent Caribbean economies still lag other subregions as tourism is yet to return to prepandemic levels, despite the accelerating rebound (Figure 3, panel 3; Box 2).

Among LA5 economies, activity during the first half of 2022 was supported by firm growth in private domestic demand—favored by accommodative policies feeding into early 2022 in some cases (Chile, Colombia)—and by a robust export performance due to solid global demand and high export prices (Figure 3, panel 4). Both the service sector and manufacturing recovered strongly in this context, propelling output beyond prepandemic levels, except for Mexico (Figure 3, panel 5).

Along with the recovery in activity, employment in LA5 economies has firmly surpassed prepandemic levels, though with heterogeneity across gender and skill levels. After declining in late 2021, real wages appear to have reached bottom and have

Figure 3. Recent Economic Developments



Sources: Caribbean Tourism Organization; Gruss and Kebhaj (2019); Haver Analytics; IMF, Commodity Terms of Trade database; IMF, World Economic Outlook database; national authorities; and IMF staff calculations.

Note: CAPDR = Central America, Panama, and the Dominican Republic; CARIB: Comm. exp. = Caribbean: Commodity exporters; CARIB: Tourism dep. = Caribbean: Tourism dependent; GFC = global financial crisis; LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); LAC = Latin America and the Caribbean; SA = South America; TOT = terms of trade.

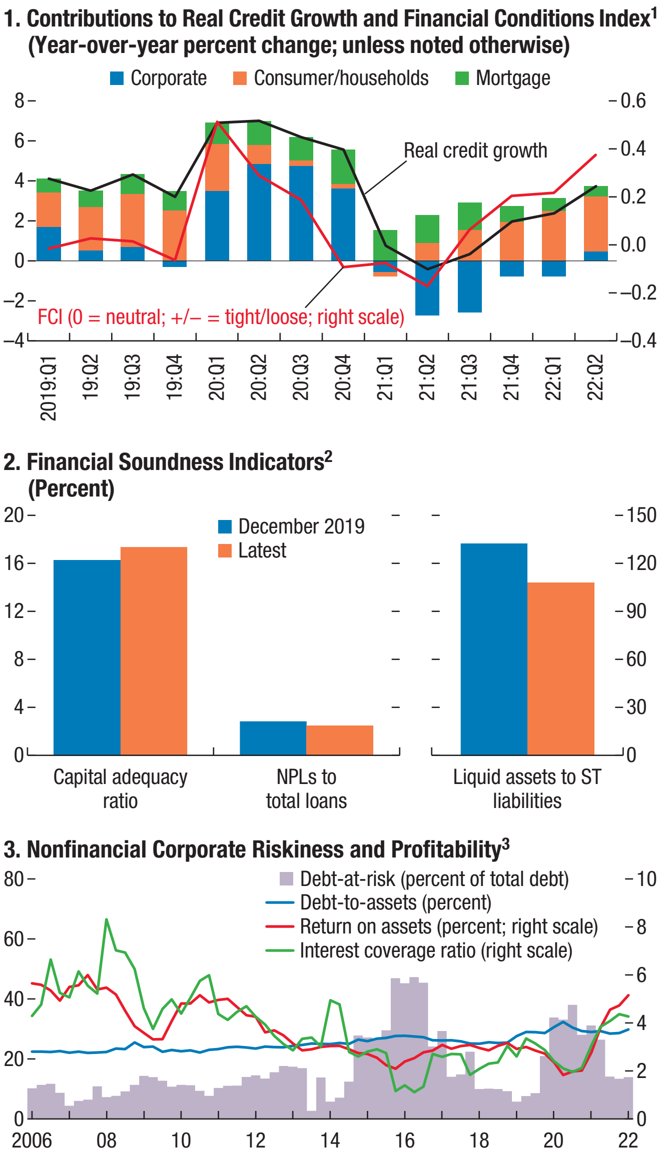
[1]Aggregates are purchasing-power-parity GDP-weighted averages.

[2]"During pandemic" refers to period April 2020 until July 2022. "During GFC" refers to period January 2009 to March 2011.

[3]Remittances deflated by US consumer price index (includes Colombia, the Dominican Republic, El Salvador, Guatemala, Honduras, Jamaica, Mexico, and Nicaragua). Tourist arrivals include Caribbean countries only. Shaded area refers to the minimum-maximum range of remittances of all countries included.

[4]Seasonally adjusted. Real wage and employment are labor force-weighted averages. Economic activity is purchasing-power-parity GDP-weighted average.

Figure 4. LA5: Domestic Banking and Corporate Financial Indicators



Sources: Bloomberg Finance L.P.; Haver Analytics; national authorities; and IMF staff calculations.
Note: FCI = financial conditions index; LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); NPLs = nonperforming loans; ST = short term.
[1]Purchasing-power-parity GDP-weighted average. For the methodology to construct the financial conditions index, see Online Annex of the October 2018 *Global Financial Stability Report*.
[2]Purchasing-power-parity GDP-weighted average. Chile is excluded from liquid assets to short-term liabilities because of data limitations. Latest data are as follows: Brazil (capital adequacy ratio: July 2022, NPLs: 2021:Q3, liquidity: 2021:Q4); Chile, Mexico (December 2021); Colombia (May 2022); and Peru (June 2022).
[3]Interest coverage ratio is earnings before interest and tax divided by interest expense. Debt-at-risk is defined as debt of companies with interest coverage ratio of less than 1. Both earnings before interest and tax and interest expense are computed as four-quarter moving averages. Median across firms is reported for all measures, except for debt-at-risk (which refers to the percent of total debt of the sample of firms).

recently shown incipient signs of recovering (Figure 3, panel 6).

Sound Banks and Nonfinancial Corporations Supported the Recovery

Economic activity in 2021 and early 2022 was supported by the resurgence of credit to the private sector, particularly households, despite the tightening of financial conditions (Figure 4, panel 1). This was helped by healthy financial systems in most countries in the region, which had solid buffers before the pandemic and remained well capitalized and liquid throughout the downturn (Figure 4, panel 2)— with few signs of asset quality deterioration despite the withdrawal of support and regulatory forbearance measures.

However, corporate credit slowed in 2021 and remained subdued in early 2022, partly reflecting the unwinding of the extraordinary pandemic-related liquidity support received in 2020. After deteriorating early in the pandemic, corporate balance sheets strengthened in 2021 and the first half of 2022, helped by the robust economic recovery, high commodity prices, and contained wage growth in some cases. Corporate profitability has recovered to levels last seen during previous peaks in commodity prices, contributing to the weak demand for credit and the improving return on assets, interest coverage ratio, and debt-at-risk indicators (Figure 4, panel 3).

Inflation Has Risen to Its Highest Level in a Quarter Century

Inflation in LAC has been on an upward trend since early 2021, reaching levels not seen since 1996 and posing the greatest challenge to the region's inflation-targeting regimes since their inception.

However, there are notable differences in inflation levels across subregions, partly reflecting their different stages of recovery from the pandemic, along with differences in the weight of food, energy, and imported goods in the consumption basket; the degree of exchange rate pass-through; and the scope of measures taken to contain food and energy price increases. Inflation has been particularly high in LA5 economies—where inflation exceeded the central banks' tolerance bands by 6.2 percentage points, on average, in the August inflation print, including by 3.8 and 6.9 percentage points in Brazil and Colombia, respectively—followed by other Caribbean economies, particularly commodity exporters (Figure 5, panel 1).

Although inflation has been rising globally, price pressures have been somewhat higher in LA5 economies than in other emerging markets because of a larger impact of global food and energy price increases in LA5, reflecting differences in the composition of consumption baskets. The exception has been emerging Europe, where the war-related energy shock has led to heightened price pressures (Figure 5, panel 2). Imported inflation, reflecting pandemic-related supply disruptions and rapidly rising commodity prices, was a key contributor to domestic price increases in LA5 economies since 2021. Pass-through from exchange rate depreciations also contributed to domestic price pressures, particularly during the first quarter of 2020 and recently. Also, the initial uptick in goods and commodity prices was followed by accelerating services' prices amid the normalization of mobility and the reopening of contact-intensive sectors (Figure 5, panel 3), a pattern also observed in the United States.

The war in Ukraine amplified inflation pressures through higher food and energy prices, with a particularly adverse impact on the poor because of the larger weight of food and energy in their consumption basket. Amid these compounding external shocks and strong domestic demand in several countries in the region, inflation pressures have become broad-based (Figure 5, panel 5), feeding into core inflation and wages, and showing signs of increasing persistence (see Annex 2).

LAC's monetary authorities have raised policy rates swiftly—ahead of most other emerging market and advanced economies (Figure 5, panel 6)—with ex ante real policy rates reaching 6 percent in August 2022, up from close to zero in mid-2021, likely bringing monetary policy into contractionary territory in most cases, though there is always uncertainty about estimates of neutral rates. Headline inflation in LA5 has shown some recent signs of stabilizing, supported by the softening of some commodity prices and waning producer price inflation, but it is too early to say if the "tide" has turned as core inflation has continued rising in some countries (Figure 5, panel 4). Likewise, while medium-term inflation expectations appear broadly anchored within central banks' tolerance bands, shorter-term expectations have been rising.

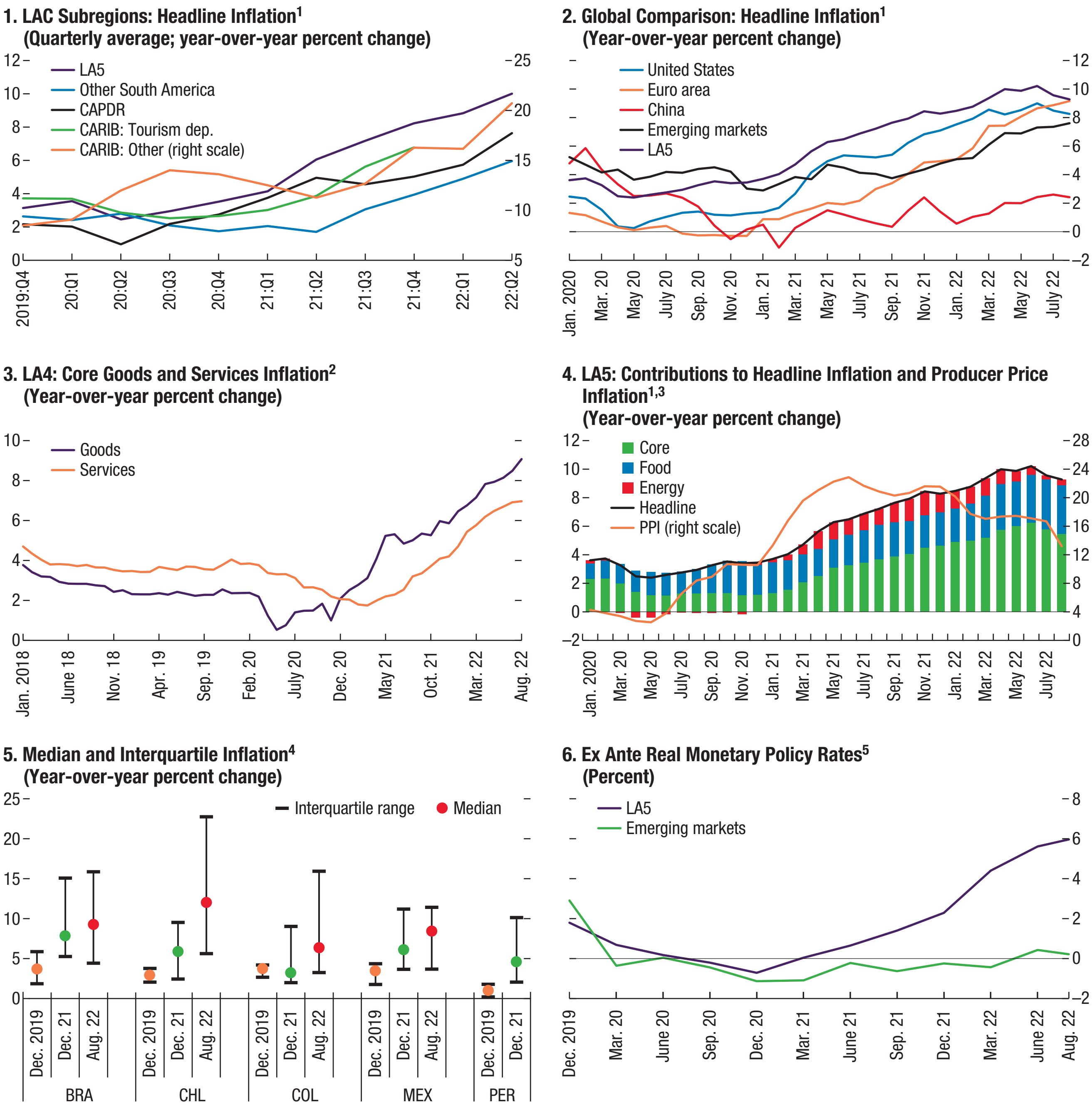
Fiscal Policy Supported the Vulnerable amid the Food and Energy Price Shock

Most countries in LAC introduced fiscal measures (mostly tax cuts and exemptions or subsidies to households and specific industries) to mitigate the impact of high food and energy prices on vulnerable households, especially after the outbreak of the war in Ukraine. Although new measures were largely announced as temporary, their estimated fiscal cost—of about 0.8 percent of GDP for 2022, in addition to 0.4 percent of existing subsidies—is sizable, partly reflecting that they have been mostly untargeted (Figure 6, panel 1).

Despite these additional fiscal outlays, fiscal policy in LAC is projected to remain broadly neutral in 2022, after the withdrawal of pandemic-related stimulus in 2021 (Figure 6, panel 2). There are important differences across countries, however, with Chile tightening fiscal policy significantly in 2022 after a highly expansionary stance in 2021. Conversely, a positive fiscal impulse is expected in Brazil during 2022 amid higher transfers and tax cuts to contain the effects of inflation on households and businesses.

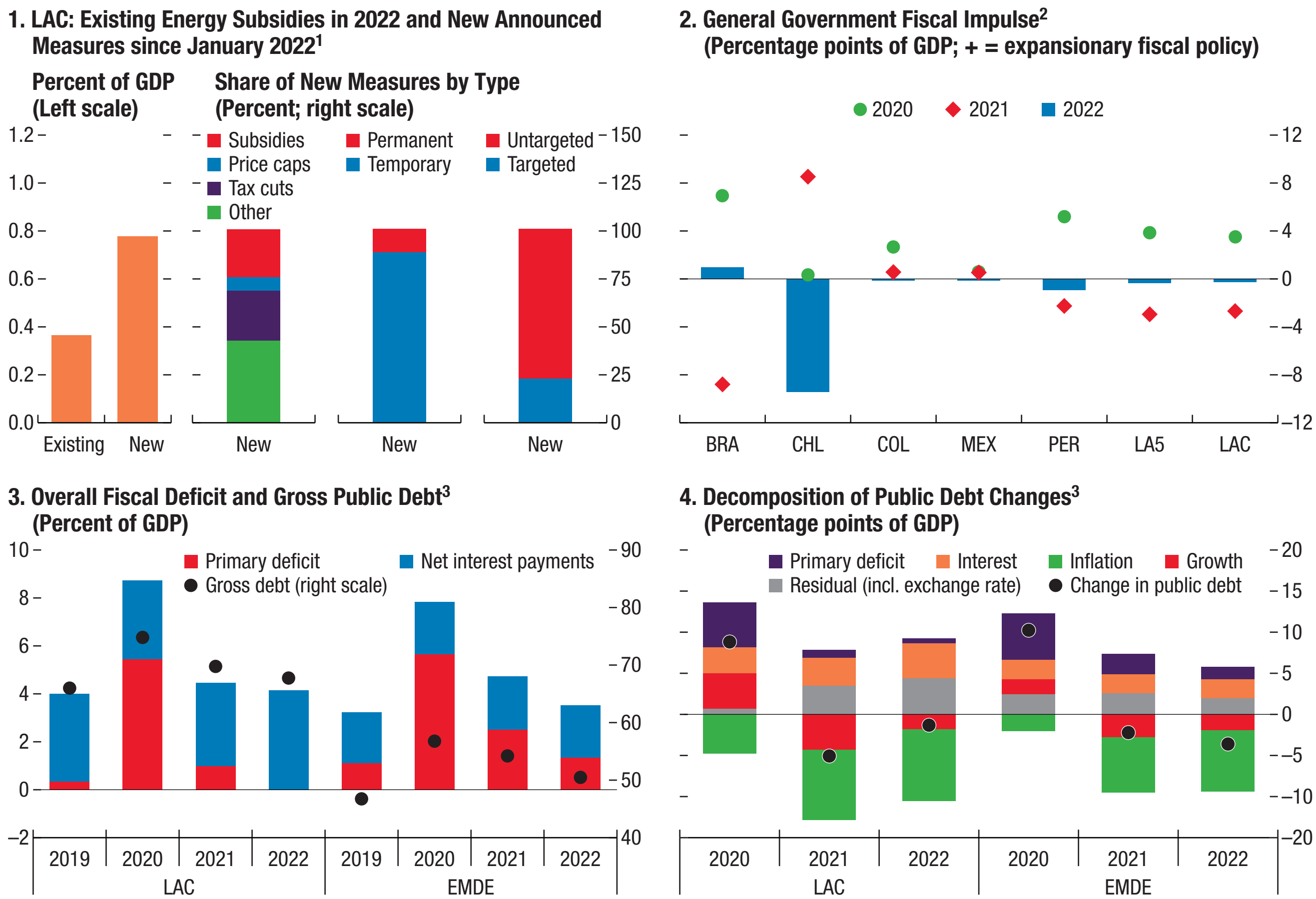
While the overall fiscal deficit in LAC is expected to remain broadly unchanged from 2021 (Figure 6, panel 3) and marginally higher than in 2019, net interest payments account now for a larger share of the deficit, as financial conditions tightened and public debt maturity shortened since the outbreak of the pandemic. By contrast, fiscal balances are expected to strengthen considerably during 2022 in other emerging

Figure 5. Inflation and Monetary Policy Developments



Sources: Consensus Economics; Global Finance Data; Haver Analytics; IMF, International Financial Statistics database; national authorities; and IMF staff calculations.
Note: Data labels use International Organization for Standardization (ISO) country codes. CAPDR = Central America, Panama, and the Dominican Republic; CARIB = Caribbean; CARIB: Tourism dep. = Caribbean: Tourism dependent; Emerging markets = Hungary, India, Indonesia, Malaysia, Philippines, Poland, Romania, Thailand; LA4 = Latin America 4 (Brazil, Chile, Colombia, Mexico); LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); LAC = Latin America and the Caribbean; Other SA = Other South America (excludes Argentina and Venezuela); PPI = producer price inflation.
[1]Aggregates are purchasing-power-parity GDP-weighted averages.
[2]Core goods exclude food, transportation, and housing. Core services exclude transportation and housing.
[3]Core inflation is defined as headline inflation less food and energy.
[4]The analysis does not include Peru as data on consumer price index subcomponents ends in 2021 due to a change in the classification.
[5]Ex ante real policy rate is the difference between nominal policy rate and one-year-ahead inflation expectations. Aggregates are purchasing-power-parity GDP-weighted averages.

Figure 6. Fiscal Policy Developments



Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: Data labels use International Organization for Standardization (ISO) country codes. EMDE = emerging market and developing economies (excluding China and LAC); LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); LAC = Latin America and the Caribbean.
[1]Existing measures (2022) are based on IMF staff calculations, cover energy subsidies. New measures (2022) include those to compensate for higher energy and food prices announced since January 2022, based on country desk surveys up to June 2022. Measures are considered targeted if announced as benefiting some specific segments of the population and temporary if announced with an end date. Tax cuts include exemptions.
[2]Defined as the change in structural primary deficit. Aggregates are fiscal year US dollar nominal GDP-weighted averages. For Chile, values refer to the change in structural non-mining primary deficit. For Colombia, values refer to the consolidated public sector's change in structural non-oil primary deficit.
[3]Aggregates are fiscal year US dollar nominal GDP-weighted averages. LAC excludes Venezuela. Decomposition of public debt changes as in Acosta-Ormaechea and Martinez (2021).

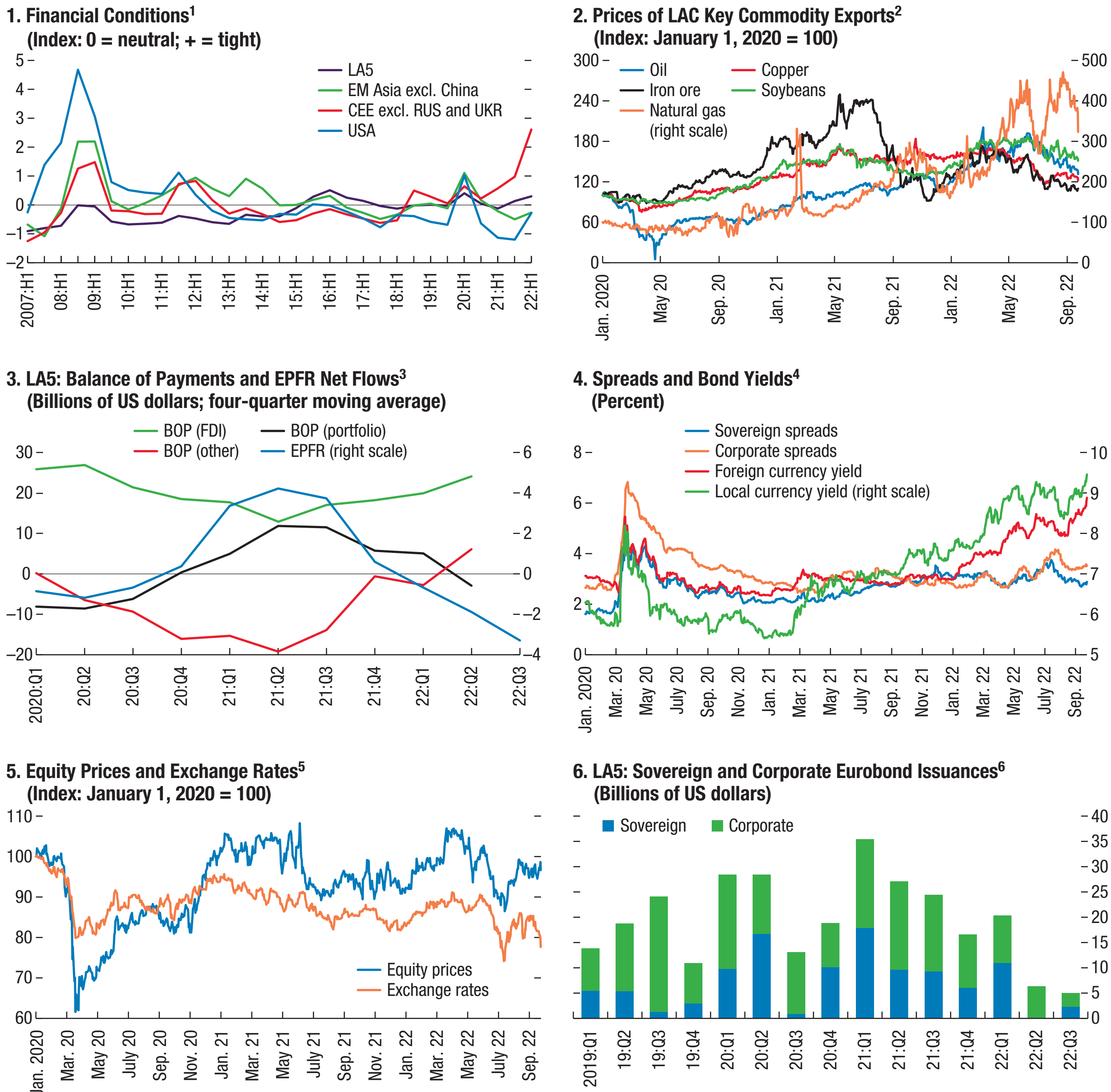
markets amid continued fiscal consolidation efforts and broadly unchanged interest payments.

LAC's public debt ratios displayed large swings since the outbreak of the pandemic, reaching historical highs in 2020 after rising close to 9 percentage points of GDP (slightly less than peer countries), and followed by a marked reversal in 2021–22 due to large inflation surprises and a solid growth rebound (Figure 6, panel 4). While public debt is expected to be only about 1.7 percent of GDP above prepandemic levels by the end of 2022, it remains considerably above the levels observed in other emerging markets.

Global Winds Are Shifting

The external environment was supportive of LAC's recovery in 2021 and early 2022, but it is turning rapidly. Amid tightening global financial conditions (Figure 7, panel 1), global demand is weakening, commodity prices are softening—except for natural gas because of supply disruptions in Europe (Figure 7, panel 2)—and

Figure 7. Global Economic and Financial Conditions



Sources: Bloomberg Finance L.P.; Bond Radar; Emerging Portfolio Fund Research; Haver Analytics; IMF, Balance of Payments Statistics database; and IMF staff calculations.
Note: BOP = balance of payments; CEE = central and eastern Europe; EM = emerging markets; EPFR = Emerging Portfolio Fund Research; FDI = foreign direct investments; LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); LAC = Latin America and the Caribbean; RUS = Russia; UKR = Ukraine; USA = United States.
[1]For methodology and variables included in the financial conditions index, refer to the Online Annex of the October 2018 *Global Financial Stability Report*. LA5 is purchasing-power-parity GDP-weighted average.
[2]Oil refers to the average of Brent, West Texas Intermediate, and Dubai Fateh petroleum spot prices. Natural gas refers to the Henry Hub spot price. The spike in natural gas prices during February 16–17, 2021, is smoothed out considering one-period-ahead and lagged averages.
[3]Balance of payments flows exclude special drawing rights allocations.
[4]Median of LA5 countries. Sovereign spreads refer to EMBIG spreads (US-dollar-denominated sovereign bonds). Corporate spreads refer to the CEMBI spreads (US-dollar-denominated corporate bonds).
[5]Median of LA5 countries. Exchange rates refer to the bilateral exchange rates against the US dollar; an increase denotes an appreciation.
[6]Data for the third quarter of 2022 are until September 26, 2022.

Table 1. Western Hemisphere: Real GDP Growth
(Year-over-year percent change)

			Projections		Difference from April 2022 WEO	
	2020	2021	2022	2023	2022	2023
United States	–3.4	5.7	1.6	1.0	–2.1	–1.3
Canada	–5.2	4.5	3.3	1.5	–0.6	–1.3
Latin America and the Caribbean	**–7.0**	**6.9**	**3.5**	**1.7**	**1.0**	**–0.8**
LAC excluding Venezuela	–6.6	7.0	3.4	1.7	0.8	–0.8
South America	–6.6	7.3	3.6	1.6	1.3	–0.5
CAPDR	–7.1	11.0	4.7	3.6	–0.1	–0.4
Caribbean						
Tourism Dependent	–14.7	7.8	5.2	3.6	0.5	–0.3
Other	1.3	3.4	16.7	9.3	2.8	–2.7
Of which: Commodity Exporters	4.0	6.1	24.6	12.8	4.4	–3.6
Memorandum						
LA5	–6.2	6.3	3.0	1.2	1.1	–0.9
Brazil	–3.9	4.6	2.8	1.0	2.0	–0.4
Mexico	–8.1	4.8	2.1	1.2	0.1	–1.3

Sources: IMF, World Economic Outlook (WEO) database; and IMF staff calculations.
Note: Regional aggregates are purchasing-power-parity GDP-weighted averages. For country group information, see page 46. CAPDR = Central America, Panama, and the Dominican Republic; LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); LAC = Latin America and the Caribbean.

capital flows to emerging market economies are slowing (October 2022 *World Economic Outlook*).

The impact of shifting external conditions is already apparent in LAC's financial markets. While other flows have shown some resilience so far, portfolio flows into the region have weakened, particularly bond-related flows (Figure 7, panel 3), and foreign-currency sovereign and corporate spreads have widened (Figure 7, panel 4). In this context, domestic currency yields have risen, equity prices have declined, and domestic currencies have weakened (Figure 4, panel 5), although the latter have fluctuated in tandem with commodity prices.

With rising financing costs and retrenching capital flows, LA5 sovereigns and corporations have reduced their external debt issuances significantly in recent months (Figure 7, panel 6). As global conditions turn, the growth momentum seen earlier in the region is expected to subside.

Regional Outlook

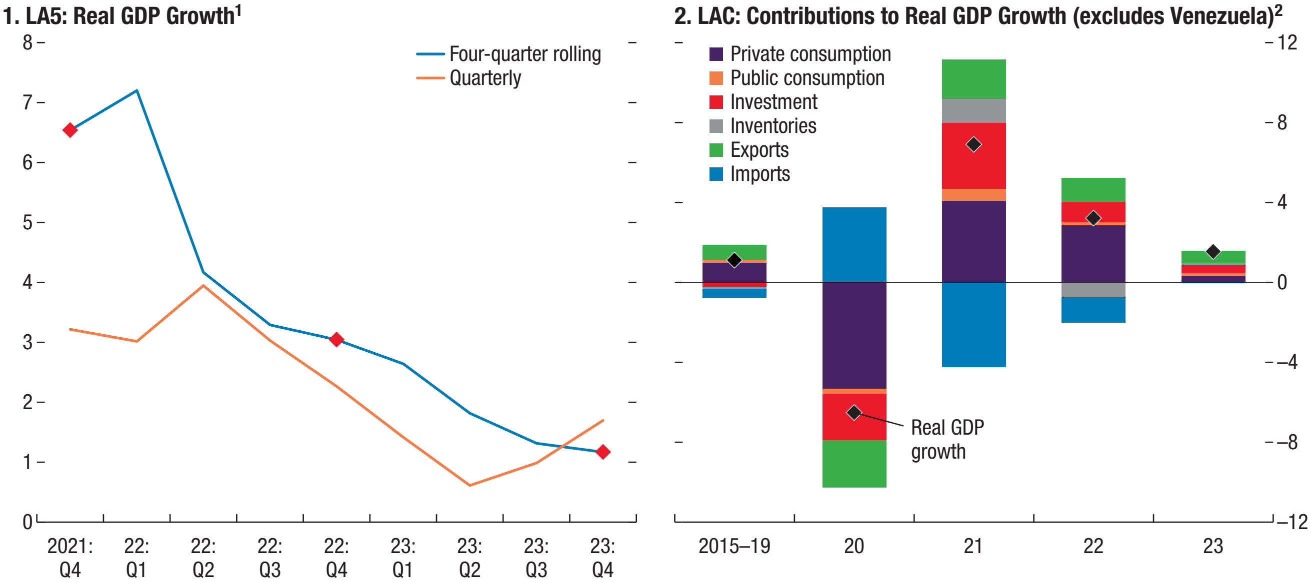
Weakening Short-Term Growth

After expanding by 6.9 percent in 2021, LAC is expected to grow by 3.5 percent in 2022—still above potential growth—entailing a 1 percentage point upward revision to 2022 growth relative to the April 2022 *World Economic Outlook* forecast owing to the solid outturn in the first half of the year (Table 1).

However, a deceleration is expected in late 2022 and 2023 (Figure 8, panel 1) as output is near potential in most countries, and external conditions turn less favorable. Private consumption and investment, key contributors to growth during 2021–22 amid pandemic pent-up demand, are expected to take a more muted role (Figure 8, panel 2), while public consumption and exports return to prepandemic growth rates.

These developments take place as tighter global financial conditions weigh on domestic activity, including through lower capital inflows, higher yields (Figure 9, panel 1), and a slowdown in private credit. While strong economic fundamentals can partially shield countries

Figure 8. Growth Outlook
(Year-over-year percent change)



Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: Aggregates are purchasing-power-parity GDP-weighted averages. LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); LAC = Latin America and the Caribbean.
[1]Four-quarter rolling refers to the continuous sum of four quarters, in a rolling manner, including that of the quarter in which the year-over-year growth is computed. Red markers indicate annual year-over-year growth.
[2]Also excludes Aruba, Barbados, Dominica, Grenada, Guyana, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, and Trinidad and Tobago because of data limitations. Inventories include statistical discrepancies.

from tighter global financial conditions, the region's picture is mixed. Some fundamentals have improved relative to previous episodes of tightening of global financial conditions (mainly international reserve buffers and central banks' credibility), while others that tend to amplify external financial spillovers (for example, foreign currency public debt, public gross financing needs, and current account deficits) have worsened in some countries, partly because of the pandemic's impact (Figure 9, panel 2).

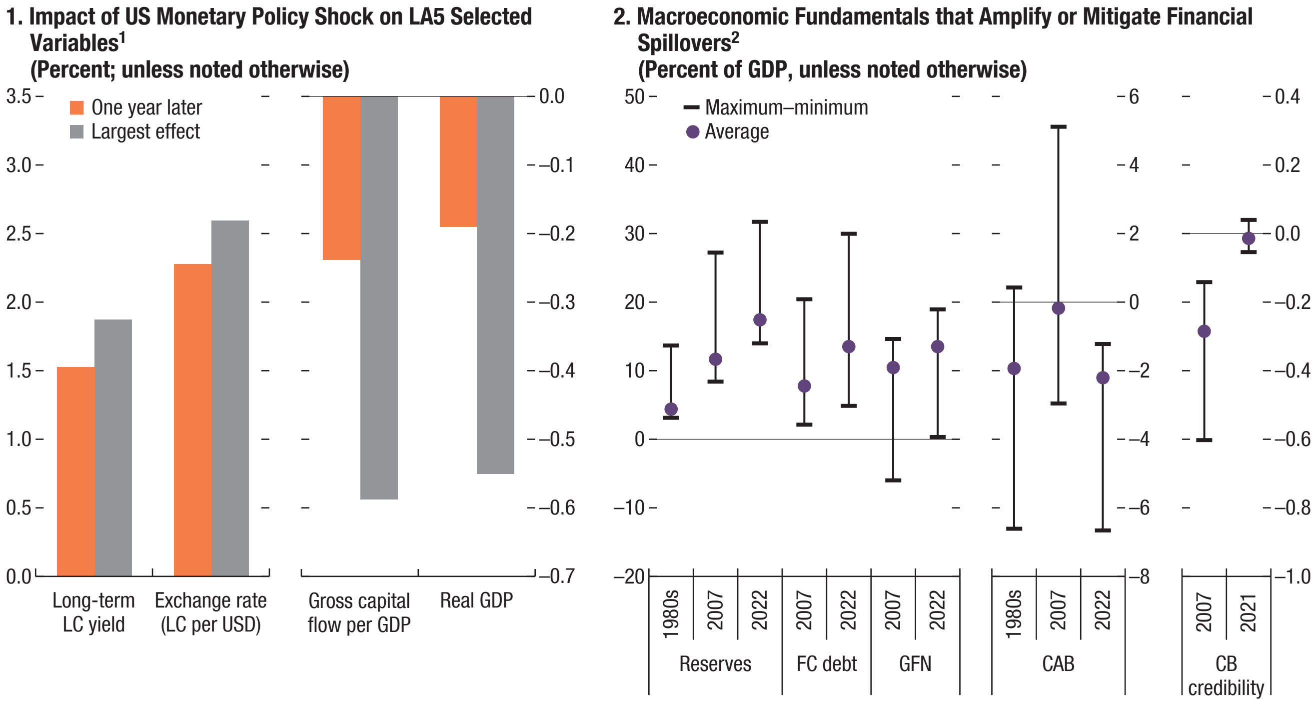
Weakening commodity prices, amid lower global growth, will also affect activity in the region, especially in net commodity exporters of South America and the Caribbean. Meanwhile, lower remittances are expected to affect Central America, Panama, and the Dominican Republic (Box 1), while tourism-dependent Caribbean countries are likely to see weaker tourism, along with adverse effects on competitiveness in some cases as the US dollar appreciates (Box 2).

Amid the weaker external environment and domestic contractionary policies that will weigh on domestic demand, the region's economy is projected to slow further in 2023 to 1.7 percent—a downward revision of the 2023 forecast by 0.8 percentage point relative to April 2022 *World Economic Outlook* projections (Table 1).

Persistent Inflation

Amid broad-based inflation pressures, and lagged effects of monetary tightening, inflation in LAC is projected to remain high for some time, reaching 14.6 percent by the end of 2022—a 4.6 percentage point upward revision compared with the April 2022 *World Economic Outlook* forecast—and 9.5 percent by the end of 2023, a 2.4 percentage point revision (Table 2). These sizable revisions reflect higher and more persistent inflation than anticipated, partly driven by high energy and food prices, and the faster-than-expected expansion of domestic demand in some cases.

Figure 9. Spillovers and Vulnerabilities from Tighter US Monetary Conditions on LA5 Economies



Sources: IMF, International Financial Statistics database; IMF, World Economic Outlook database; and IMF staff calculations.
Note: CAB = current account balance; CB = central bank; FC = public foreign currency; GFN = public gross financing needs; LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); LC = local currency; USD = US dollars.
[1]Impulse response one year later and largest impact within three years. Size of the shock is 1 percentage point increase in US two-year bond yield for long-term local currency yield and for the rest, one standard deviation tightening of US two-year bond yield on the day of the Federal Open Market Committee meetings. In case of long-term local-currency yields, the impact is computed within six months. Changes in gross capital flows are measured in percent of GDP. See details in Annex 1.
[2]Average is purchasing-power-parity GDP-weighted. Central bank credibility is measured by the inverse of sensitivity of long-term inflation forecasts to inflation surprises. Data for 1980s refer to the average of the period 1980–89.

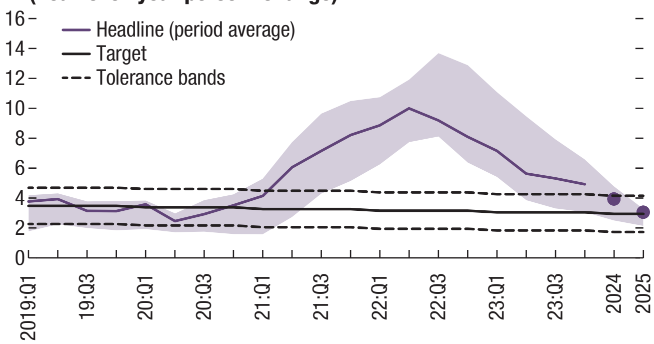
Table 2. Western Hemisphere: End-of-Period Inflation
(Year-over-year percent change)

			Projections		Difference from April 2022 WEO	
	2020	**2021**	**2022**	**2023**	**2022**	**2023**
United States	1.5	7.4	6.4	2.3	1.1	0.0
Canada	0.7	4.7	6.9	3.2	2.3	1.0
Latin America and the Caribbean	**6.3**	**11.6**	**14.6**	**9.5**	**4.6**	**2.4**
South America	8.0	14.1	18.0	12.1	5.9	3.2
CAPDR	2.8	5.1	7.8	4.4	2.2	0.5
Caribbean						
Tourism Dependent	2.5	5.4	8.3	4.3	8.3	4.3
Other	14.4	11.7	16.8	9.0	10.0	5.7
Of which: Commodity Exporters	8.6	11.0	10.8	6.8	2.2	1.3
Memorandum						
LA5	3.5	8.3	7.8	4.9	1.5	1.4
Brazil	4.5	10.1	6.0	4.7	–0.7	1.2
Mexico	3.2	7.4	8.5	4.8	2.6	1.4

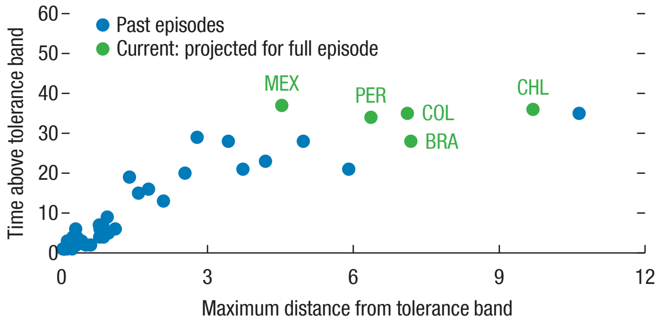
Sources: IMF, World Economic Outlook (WEO) database; and IMF staff calculations.
Note: Regional aggregates are geometric purchasing-power-parity GDP-weighted averages. Venezuela is excluded from all inflation aggregates. For country group information, see page 46. CAPDR = Central America, Panama, and the Dominican Republic; LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); LAC = Latin America and the Caribbean.

Figure 10. Inflation Outlook

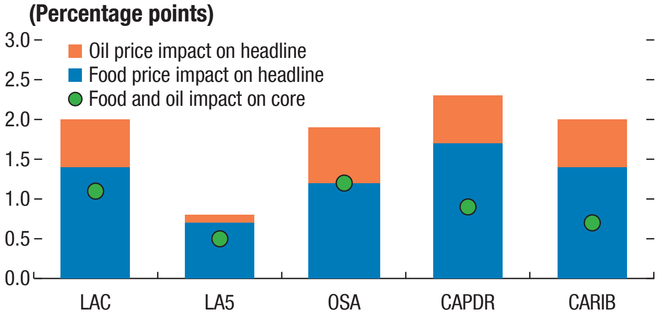
1. LA5: Headline and Target Inflation[1]
(Year-over-year percent change)



2. LA5: Inflation Episodes[2]
(*X*-axis: percentage points; *Y*-axis: months)



3. Estimated Impact of Global Food and Oil Price Shocks on LAC's Domestic Headline and Core Inflation[3]
(Percentage points)



Sources: Haver Analytics; IMF, World Economic Outlook database; national authorities; and IMF staff calculations.
Note: Data labels use International Organization for Standardization (ISO) country codes. CAPDR = Central America, Panama, and the Dominican Republic; CARIB = Caribbean; LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); LAC = Latin America and the Caribbean; OSA = other South America.
[1]Purchasing-power-parity GDP-weighted averages of LA5 countries. For Chile, tolerance band defined as target +/– 1 percentage point. Shaded area shows minimum-maximum range of headline inflation.
[2]Inflation episodes identified as periods (in months) with year-over-year inflation above the central banks' tolerance bands—1 percentage point above target for Chile. Blue dots: completed past inflation episodes since 2000. Green dots: expected for current episode based on October 2022 *World Economic Outlook* projections.
[3]Estimated impact (using local projection method) of a 10 percent increase in international food and oil prices on domestic headline and core inflation after one year. Sample period is 1990–2021.

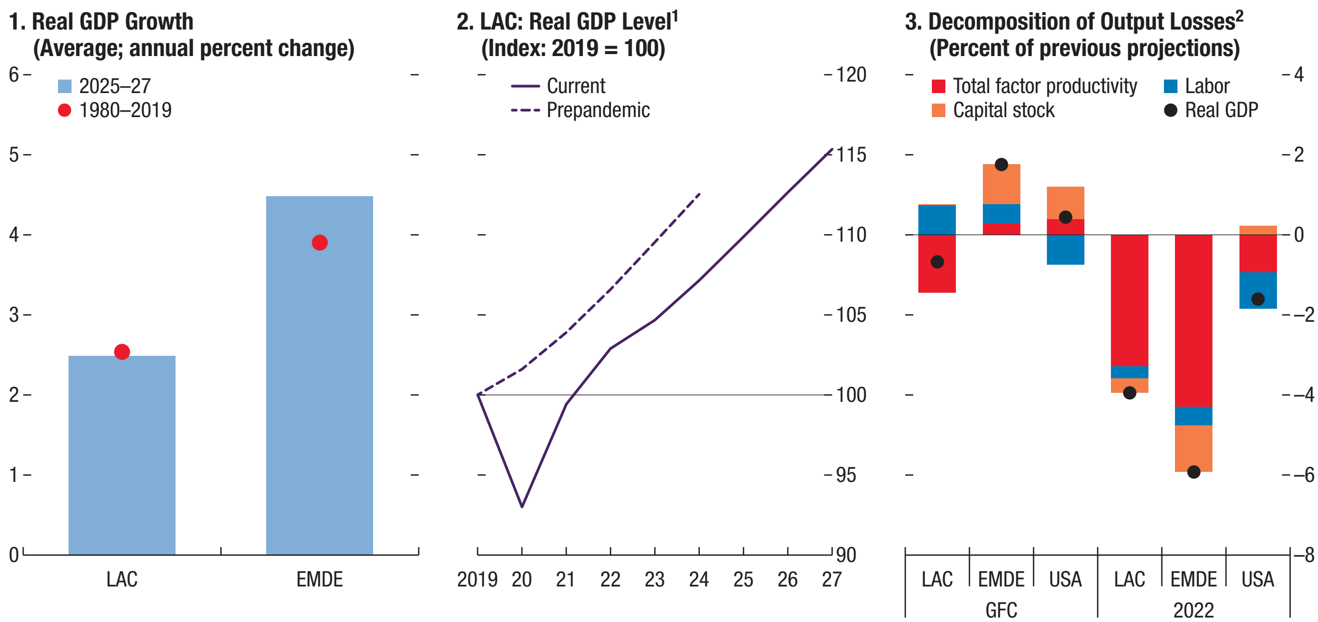
For LA5, inflation is expected to reach 7.8 percent by the end of 2022 and 4.9 percent by the end of 2023, remaining considerably above the central banks' tolerance bands throughout 2022–23 while converging to the bands by the end of 2023 and to the inflation target by late 2024 (Figure 10, panel 1). The expected duration of this inflation episode (that is, until inflation returns to the tolerance bands) is commensurate to the observed inflation overshooting, in line with past episodes, although the large deviations from the target this time warrant a cautious interpretation of the historical relationships (Figure 10, panel 2).

The expected downward path of commodity prices will contribute to bringing inflation down. For each 10 percent increase in international food and energy prices, headline inflation in LAC is estimated to increase by 2 percentage points within a year, with core inflation increasing half as much (Figure 10, panel 3). About three-quarters of this impact is explained by food prices, reflecting their greater relevance in the consumption basket of the average household in the region. This impact is larger in subregions where imported food and energy account for a larger fraction of consumption, such as Central America, Panama, and the Dominican Republic, as well as the Caribbean. These estimates indicate that the 14 and 41 percent rise in international food and energy prices observed in 2022, respectively, may have contributed by as much as 5 percentage points to headline inflation in LAC. On the other hand, the projected softening of global food and energy prices in 2023 —by about 6 and 13 percent, respectively—could contribute to lowering headline inflation by about 1.6 percentage points during 2023–24.

Pandemic Scarring

Over the medium-term, LAC's growth is projected to return to its long-term (1980–2019) average of 2.5 percent—considerably below peer economies, as observed historically and especially in the aftermath of the global financial crisis and the commodity super cycle in the mid-2010s (Figure 11, panel 1). LAC's output is projected

Figure 11. Medium-Term Growth Projections and Scarring



Sources: IMF, World Economic Outlook database; Penn World Tables 10.0; and IMF staff calculations.
Note: Purchasing-power-parity GDP-weighted averages. EMDE = emerging market and developing economies (excluding China and LAC); GFC = global financial crisis; LAC = Latin America and the Caribbean; USA = United States.
[1]Current refers to the October 2022 *World Economic Outlook* vintage; prepandemic refers to the January 2020 *World Economic Outlook* vintage.
[2]For GFC, comparison of October 2009 and October 2010 *World Economic Outlook* projections in 2010. For 2022, comparison of January 2020 and October 2022 *World Economic Outlook* projections.

to remain below its prepandemic trend by 4.8 percent by 2024, largely because of pandemic-related losses in productivity (a pattern also seen after the global financial crisis) and employment, to a lesser extent (Figure 11, panels 2 and 3).

Underlying LAC's productivity losses is the interaction of the unusual nature of the COVID-19 crisis (which affected some sectors disproportionately) and serious interrelated obstacles to factor reallocation, specifically informality, rigid labor market regulations, and frictions to firm entry or exit (Annex 3). The pandemic's heavy toll on human capital is also expected to constrain medium-term growth as the region endured long spells of school closures—on average, students in the region lost (fully or partially) two-thirds of in-person school days (World Bank, UNICEF, and UNESCO 2022), while poor internet connectivity hampered remote learning severely.

Risks to the Outlook

Risks to the region's outlook are tilted to the downside amid tightening financial conditions, slowing global growth, and weakening commodity prices.

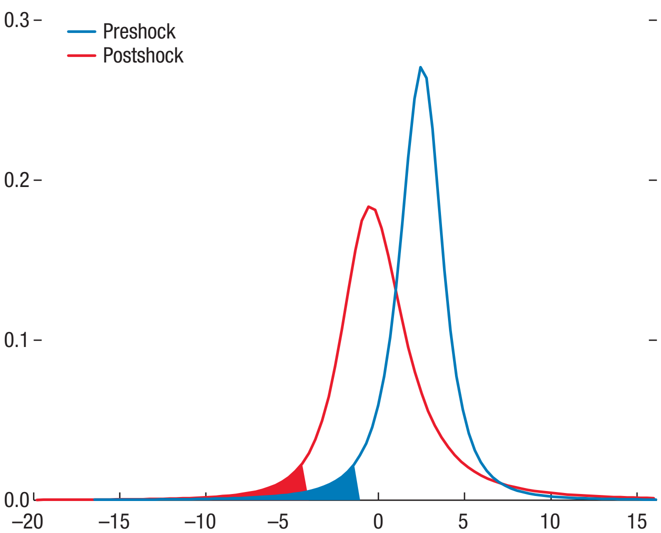
External Risks

Downside Risks

Additional tightening of global financial conditions. Tighter-than-anticipated US monetary policy and financial conditions more broadly could materially affect key asset prices in the region, including foreign and local currency yields, which have historically been very sensitive to US financial conditions (Annex 1). Such additional tightening would also increase the likelihood of severe adverse growth outcomes or "tail events" (Figure 12).

Tighter-than-expected financial conditions also carry the risk of worsening already-fragile public debt dynamics in LAC. For instance, under a

Figure 12. LA5: Growth-at-Risk
(X-axis: percentage points; Y-axis: probability density)

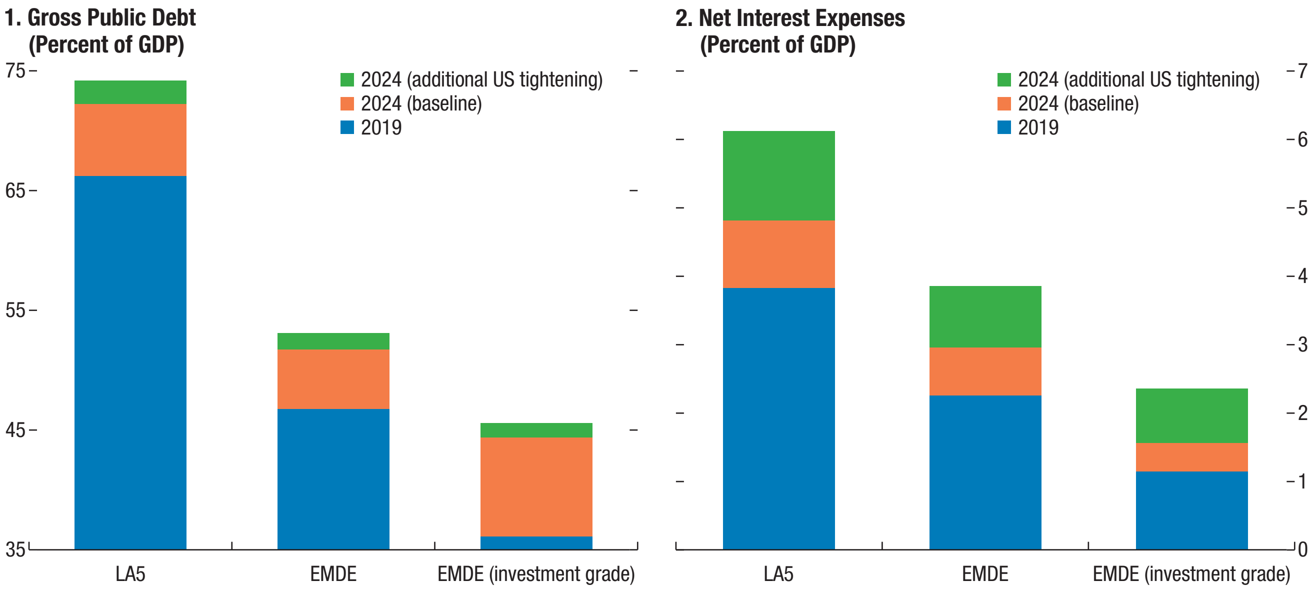


Source: IMF staff calculations.
Note: Distribution of aggregate LA5 growth, based on quantile regression. Shock is one standard deviation tightening in US financial conditions index. Shaded areas show tail outcomes with 5 percent probability. See additional details in Annex 1. LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).

plausible scenario of additional US monetary tightening compounded by increases in risk premiums, public debt—and especially the interest bill of LA5 economies—would rise materially by 2024, with both fiscal metrics reaching high levels in historical perspective and relative to peer countries, especially investment-grade emerging market economies (Figure 13). Sustaining high interest bills could prove difficult amid dire social spending demands and limited fiscal space. With high public debt levels, the sovereign-bank nexus could become a source of fragility for some economies in the region, where banks' exposure to the sovereign has been trending up since 2015 and is correlated with public debt levels (April 2022 *Global Financial Stability Report*).

Tighter global financial conditions could also have consequences for private sector debt dynamics. Although corporate balance sheets generally appear resilient to rising interest rates (Figure 14, panel 2), there could be pockets of vulnerability as nonfinancial corporate and household indebtedness—especially in the form

Figure 13. Public Debt Dynamics Under Additional US Monetary Policy Tightening

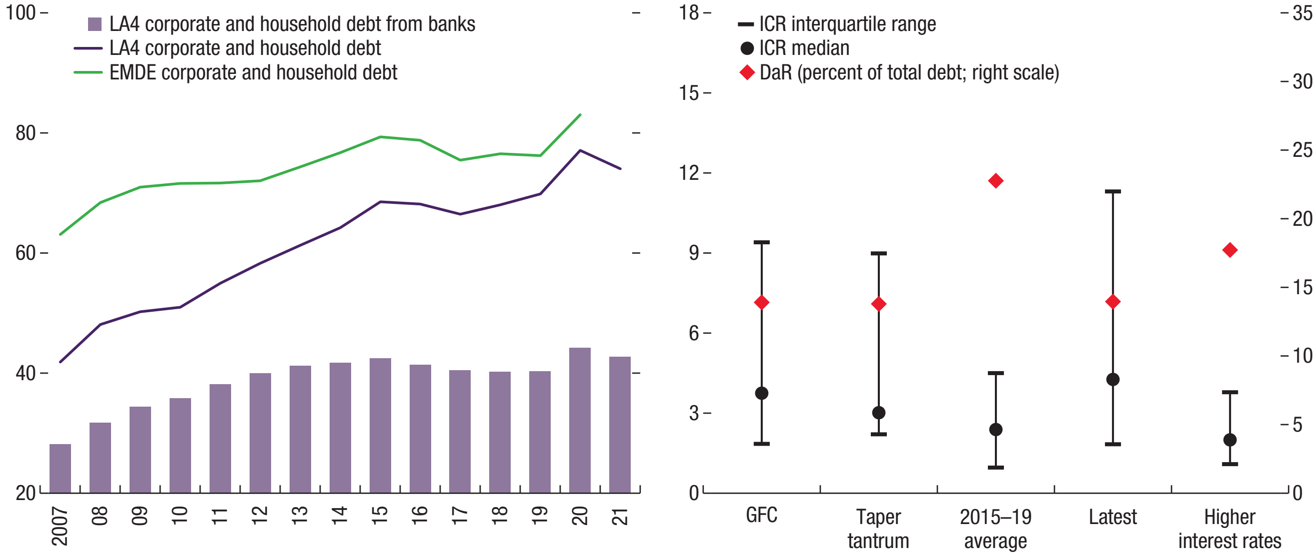


Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: The additional US tightening scenario assumes that the effective interest rate of each country's public debt increases by 110 and 190 basis points from the baseline in 2023 and 2024, respectively, as a result of rising risk-free rate and risk premium. The exercise abstracts from growth and exchange rate effects, which are likely to worsen debt dynamics. Investment-grade economies based on the median sovereign credit rating of Fitch Ratings, Moody's, and Standard and Poor's as of July 2022. EMDE = emerging market and developing economies (excluding China and Latin America and the Caribbean); LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).

Figure 14. Private Sector Debt Vulnerabilities and Spillovers from US Financial Conditions on LA5's Corporations

1. Private Sector Debt[1]
(Percent of GDP)

2. Interest Coverage Ratio and Debt-at-Risk[2]



Sources: Bloomberg Finance L.P.; Haver Analytics; IMF, Global Debt database; IMF, World Economic Outlook database; national authorities; and IMF staff calculations.
Note: DaR = debt at risk; EMDE = emerging market and developing economies (excluding China and Latin America and the Caribbean); GFC = global financial crisis; ICR = interest coverage ratio; LA4 = Latin America 4 (Brazil, Chile, Colombia, Mexico); LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).
[1]Aggregates are US dollar nominal GDP-weighted averages. LA4's and EMDE's corporate and household debt include debt to banks, nonbanks, and market debt issuances.
[2]Includes nonfinancial corporations of LA5 countries. ICR is defined as earnings before interest and tax divided by interest expense. Both earnings before interest and tax and interest expense are four-quarter moving averages. DaR indicates debt at risk (that is, percent of total debt of firms with ICR less than one). Higher interest rate scenario assumes that the effective interest rate of each corporate increases by 150 basis points from the latest level.

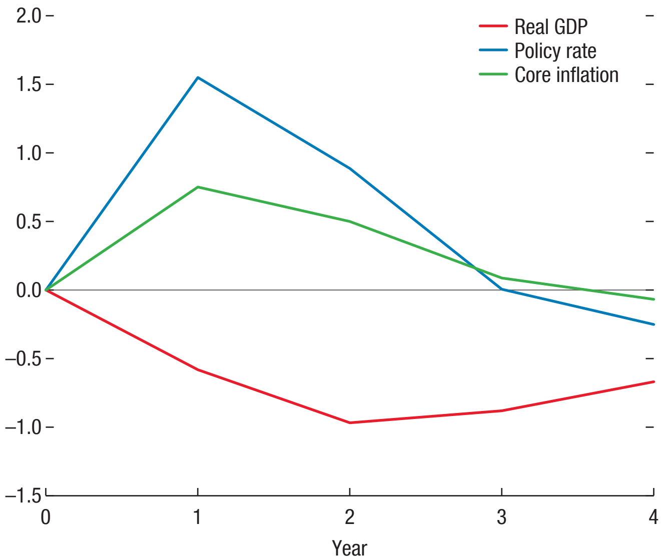
of nonbank borrowing (Annex 5)—rose markedly in the larger economies of the region before the pandemic (Figure 14, panel 1). Likewise, higher borrowing costs may increase the proportion of households facing debt-servicing difficulties, affecting banks' return, especially where consumer loans are relatively large. At the same time, the region's banking systems have generally made important strides in building resilience through lower currency mismatches, greater liquidity buffers, and stronger regulation, suggesting that financial stability risks are less concerning than in previous episodes of external financial conditions tightening.

Slower-than-anticipated global growth. Weaker growth in the United States (a "hard landing" scenario), Europe (a recession triggered by an escalation of the war in Ukraine or a more severe energy crisis), or China (COVID-19 lockdowns) could lead to a global recession with significant spillovers on LAC through supply-chain disruptions; weaker commodity prices; and lower remittances, external demand, and tourism. Although the accompanying fall in commodity prices could bring some welcome relief to inflation pressures, it would hamper an important growth engine for net commodity exporters—mostly South American and some Caribbean economies.

Natural disasters and extreme weather events are a major source of risk for some countries in the region. Climate change is expected to increase the frequency and intensity of extreme weather events, likely affecting agricultural output and nonresilient infrastructure and thus growth (IMF 2021b).

Global fragmentation. Russia's invasion of Ukraine has raised risks of global fragmentation. Although this may present benefits to some countries in the region (for example, amid new export markets and production opportunities with nearshoring),

Figure 15. LA5: Inflation Expectation Shock
(Percentage points, deviation from baseline)



Source: IMF staff calculations based on IMF's Western Hemisphere Module general equilibrium model.
Note: Inflation expectation shock of 75 and 50 basis points in year 1 and year 2, respectively. Results shown as simple average of LA5 countries. LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).

the overall impact in LAC would arguably be negative, including because of its likely impact on technological adoption, reduced cooperation to address global structural challenges (climate change, debt resolution), and disruptions to international transactions.

Upside Risks

Higher-than-anticipated commodities prices would benefit net commodity exporters in the region, but they would also exacerbate inflation pressures. Net commodity importers, mostly in Central America and the Caribbean, would be affected negatively by both worse terms of trade and higher inflation.

New export opportunities. The current crisis may open new export opportunities for South American economies (including to increase food and energy security globally) because their export basket is close to that of Russia and Ukraine. Also, the global shift to green technologies could benefit some countries in the region (particularly, Brazil, Chile, Mexico, and Peru) because of their natural endowment of metals needed for the energy transition, though taking advantage of these opportunities will require additional investment and financing.

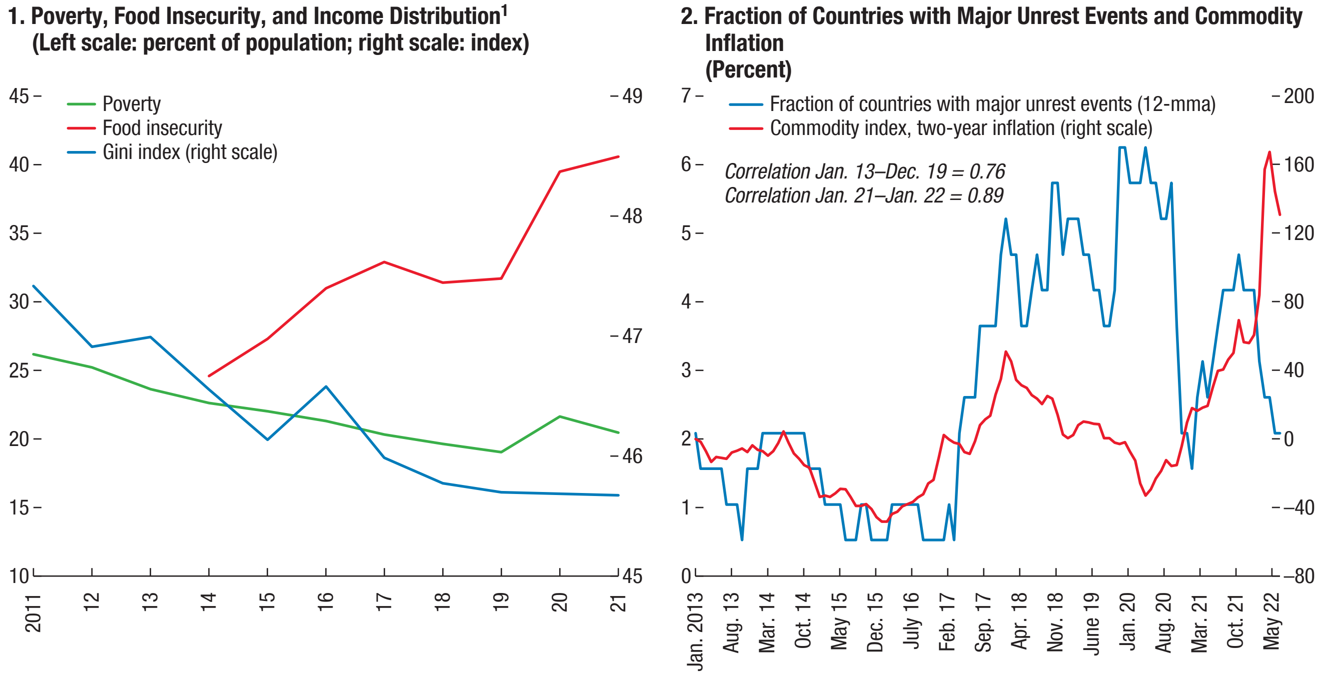
Regional and Domestic Risks

Domestic risks stem from more entrenched inflation and higher social tensions:

- Increasing wage pressures, weaker domestic currencies, and the unwinding of tax reductions and caps on administered prices could result in more persistent and entrenched inflation pressures, requiring additional monetary policy tightening, thereby dampening economic activity. Moreover, as suggested by the IMF's Western Hemisphere Module general equilibrium model (Andrle and others 2015), transient shocks to inflation expectations could exacerbate inflation-output trade-offs, requiring additional policy tightening with a sizable short-term impact on the economy to bring inflation back to target (Figure 15).
- Social tensions increased notably in LAC in recent years, first because of the growth deceleration that followed the end of the previous commodity boom, then because of the pandemic, and more recently because of the spike in food and energy prices. These shocks have weakened social cohesion in the region by exacerbating food insecurity amid elevated poverty and inequality (Figure 16, panel 1). Greater social tensions could lead to episodes of social unrest, particularly if food and energy costs remain high (Figure 16, panel 2), posing additional challenges to growth in LAC (Barrett and others 2020).

Upside risks include *faster-than-anticipated productivity growth* because of the leap in digitalization after the pandemic.

Figure 16. LAC: Poverty and Social Indicators



Sources: Barret and others 2020; IMF, World Economic Outlook database; United Nations, Food and Agriculture Organization database; World Bank, World Development Indicators database; and IMF staff calculations.
Note: 12-mma = 12-month moving average; LAC = Latin America and the Caribbean.
[1]Poverty is based on $5.50 threshold. Food insecurity refers to both moderate and severe prevalence. Gini index data for 2021 is estimated using 2020 Gini index growth. LAC sample determined by data availability.

Policy Recommendations

Short-Term Priorities

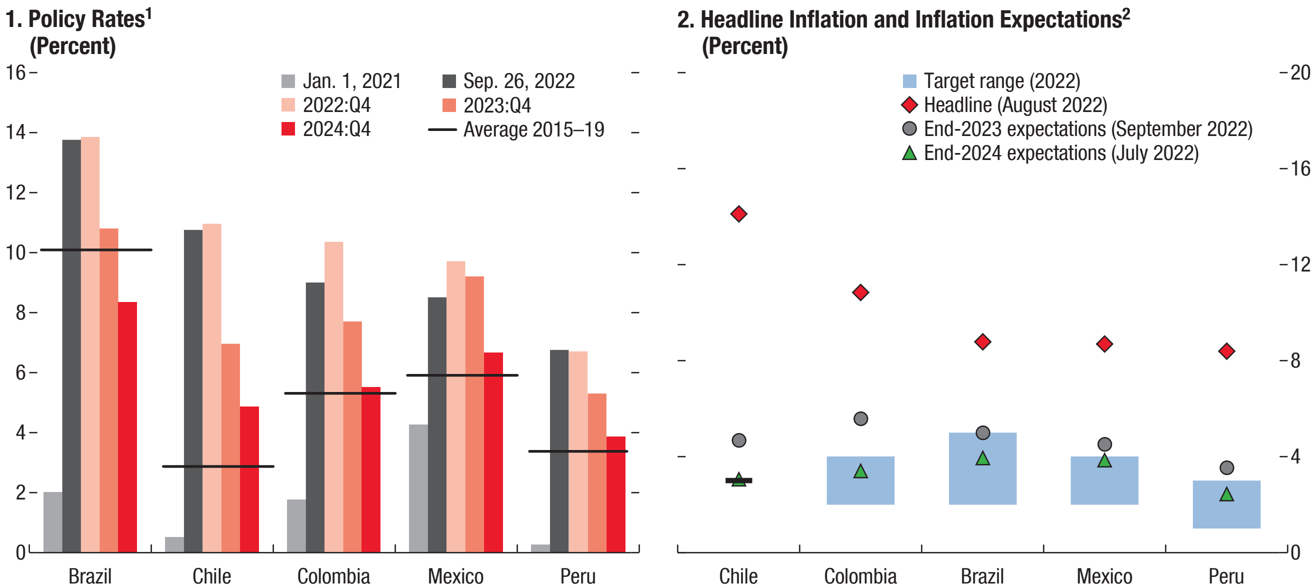
Monetary Policy Should Not Ease Prematurely, Must Stay the Course

LAC's major central banks' swift policy rate response to rising inflation (Figure 17, panel 1) has been instrumental in maintaining long-term inflation expectations broadly anchored (despite sizable inflation surprises) and preserving the credibility of monetary frameworks built over the last two decades.

However, inflation pressures are yet to abate and could become entrenched. Nominal wages have been trending upward and at an accelerating pace, partly reflecting strong labor markets. A fast wage recovery could add to broader price pressures. Likewise, the recent depreciation of the region's currencies may pass through to domestic prices. Partly reflecting these developments, one-year-ahead inflation expectations in LA5 economies have recently edged upward (Figure 17, panel 2; Annex 2).

With inflation running well above target and output near or above potential in most countries, monetary authorities should avoid easing prematurely, must stay the course, and be ready to act promptly if new inflation shocks occur or there is incipient evidence of a de-anchoring of medium-term inflation expectations. Although maintaining a tight monetary stance may become more challenging as economic activity slows, authorities should continue to be guided by the long-term benefits of low inflation rather than the short-lived trade-off between inflation and output. While calibrating monetary policy in this context of high uncertainty might be challenging, the costs of having later to restore price stability if inflation becomes entrenched is very high. Effective communication of policy intentions—including what developments will guide future policy actions—will remain key to reducing policy

Figure 17. Monetary Policy Rates and Inflation Expectations in LA5 Economies



Sources: Bloomberg Finance L.P.; Consensus Economics; Haver Analytics; national authorities; and IMF staff calculations.
Note: LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).
[1]Future policy rates based on market expectations.
[2]Brazil inflation target is set to decline from 3.5 percent in 2022 to 3 percent in 2025. Chile does not have tolerance bands; midpoint target is shown.

uncertainty and maintaining inflation expectations anchored.

With global financial conditions tightening, LA5 economies may face bouts of currency pressures, with potential implications for financial stability and inflation. Exchange rates should be allowed to operate as shock absorbers, but foreign exchange intervention could be deployed usefully to address disorderly market conditions and prevent abrupt exchange rate movements, particularly where currency mismatches or pass-through to already-high inflation are a concern.

Fiscal Policy Should Support the Vulnerable while Helping Tame Inflation and Rebuilding Fiscal Space

Governments in the region have provided support to vulnerable households to mitigate the effects of higher energy and food costs to preserve social cohesion. Although a large fraction of the support was announced as temporary, the risk of increasing fiscal costs could mount if current high prices persist. Domestic prices should be allowed to converge to international prices—as international food and energy prices recede or by gradually withdrawing fiscal support if high international prices prove persistent—while strengthening the targeting of support for vulnerable groups. This would contain fiscal costs while incentivizing production and restraining demand for scarce goods.

Fiscal support to mitigate the inflation shock should be accompanied by compensating measures, where fiscal space does not exist, but also support monetary authorities' efforts to tame inflation. Strengthening of fiscal accounts would also increase resilience to the changing global financial conditions.

Private Sector Balance Sheets Should Be Monitored Closely as Financial Conditions Tighten

Bank regulators should continue monitoring closely the evolution of nonperforming loans as financial conditions tighten while ensuring adequate loss provisions and write-offs. Selected macroprudential tools, including countercyclical capital buffers, may need to be deployed to support and make the financial system more resilient to shocks as financial conditions tighten.

Policymakers should also strengthen prudential supervision and regulation of nonbank financial corporations, which have grown in importance in the region (Annex 5). Balance sheets of nonfinancial firms and households should also be monitored closely as pockets of debt overhang could emerge after the pandemic and the tightening of financial conditions.

Medium-Term Policies

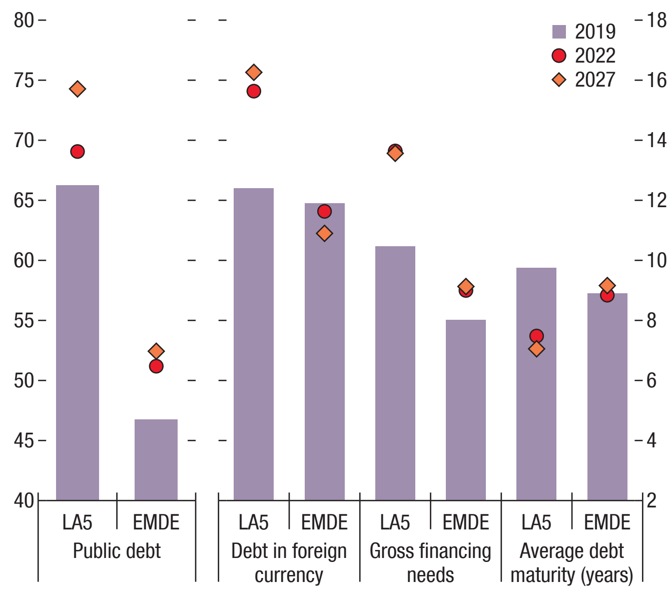
Inclusive Fiscal Consolidation Is Needed to Ensure Social Stability and Fiscal Sustainability

LAC's public debt is projected to remain broadly stable over the medium term, though above already-elevated prepandemic levels and with significant heterogeneity across subregions. Public debt of LA5 economies is expected to follow an upward trajectory over the medium term, while debt in other economies of the region is projected to decrease, especially in countries that embarked on debt-restructuring operations (Box 2) and in commodity-exporting Caribbean economies experiencing strong growth. Public debt foreign-currency exposures and gross financing needs are expected to remain high by historical standards and relative to peers, partly reflecting the shortening of debt maturities since the outbreak of the pandemic (Figure 18).

These vulnerabilities are compounded by the risk of rapidly rising ex ante real interest rates, which will exert more upward pressure on debt dynamics and require larger fiscal surpluses to stabilize debt. Moreover, progress in reducing fiscal deficits during 2021–22 largely reflects inflation surprises—which have helped contain real spending and wage growth (Figure 19, panel 1)—instead of structural measures to durably reduce spending. Thus pressures to unwind some of these savings could mount, especially on wages. Reining in real spending growth will require well-designed expenditure caps because inflation surprises are unlikely to contribute again.

Durably reducing public debt will likely require sustained improvements in primary balances. For example, reversing by 2027 at least half of the increase in public debt observed in LA5 economies since 2019 would require, under baseline assumptions, sustaining a primary balance of about 1.8 percent of GDP during 2023–27—1.3 percentage points of GDP higher than currently projected, sizably higher than the region's historical average, and higher than the level required in other emerging markets (Figure 19, panel 2).

Figure 18. Public Debt Indicators
(Percent of GDP; unless noted otherwise)

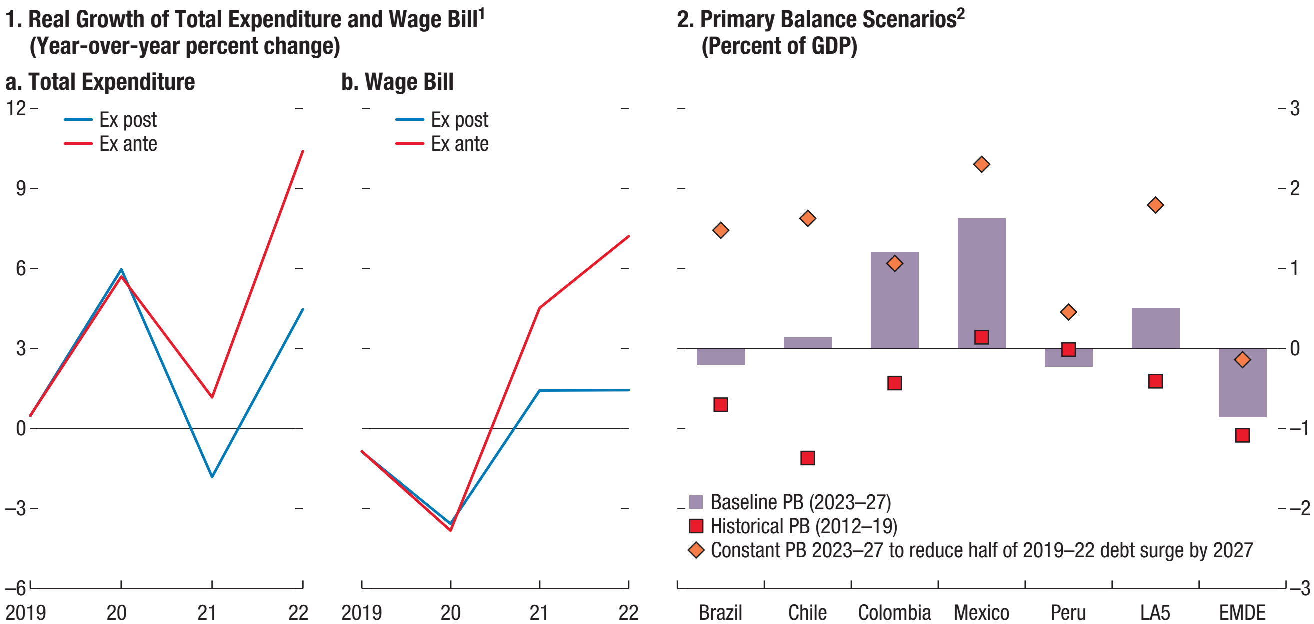


Sources: IMF, Vulnerability Exercise database; IMF, World Economic Outlook database; and IMF staff calculations.
Note: Aggregates are fiscal year US dollar nominal GDP-weighted averages. EMDE = emerging market and developing economies (excluding China and Latin America and the Caribbean); LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).

However, with dire social needs in the region, fiscal consolidation can only be effective and sustainable if it is inclusive and conducive of greater social cohesion. This means protecting the poor while maintaining longer-term fiscal sustainability and raising potential growth. Both inclusive revenue mobilization and expenditure rationalization measures will be needed to strengthen public finances.

To mobilize revenue, personal income taxation could be strengthened by improving design features such as minimum and maximum income thresholds as well as statutory rates and exemptions, and providing well-targeted compensations to low-wage earners—particularly

Figure 19. LA5: Government Spending Trends and Fiscal Adjustment Scenario



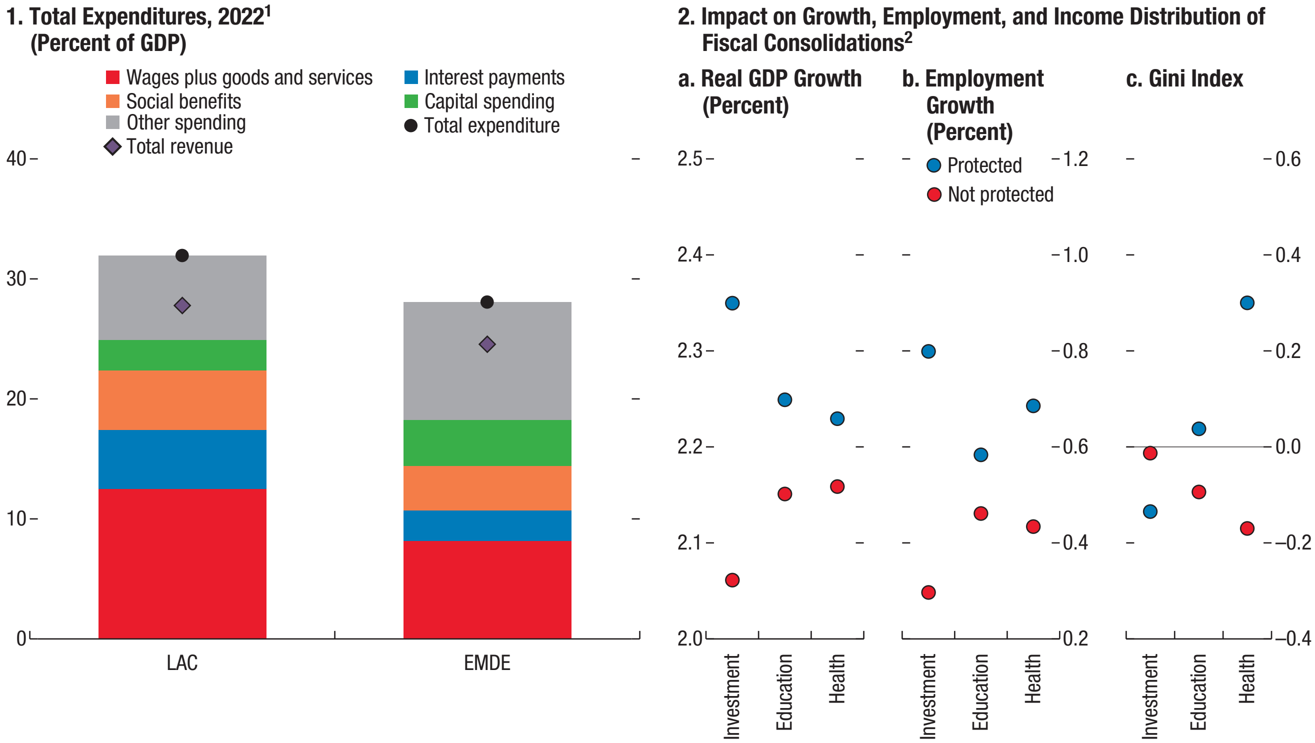
Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: EMDE = emerging market and developing economies (excluding China and Latin America and the Caribbean); LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru); PB = primary balance.
[1]Real expenditure and wage bill are purchasing-power-parity GDP-weighted averages deflated by average headline consumer price index inflation. Ex post is based on realized inflation and October 2022 *World Economic Outlook* projections for 2022 onwards. Ex ante is based on countries' inflation targets.
[2]The figure reports primary balances under baseline projections (bars), historical averages (red squares), and (constant) levels required to reverse by 2027 half of the increase in debt observed between 2019 and 2022 (orange diamonds). Aggregates are fiscal year US dollar nominal GDP-weighted averages.

female workers—to incentivize their participation in the formal labor market, as needed. Efficiency of other taxes such as the value-added tax and corporate income tax could also be improved (IMF 2021a). The ongoing global corporate income tax reform provides an opportunity to revisit corporate taxation thoroughly to mobilize revenues, including through taxation of rents derived from the extraction of natural resources that safeguard investment and growth (Klemm and Mansour 2022).

On the spending side, rationalization should focus on wages and goods and services, along with social benefits and pension reforms in some cases. These spending outlays are higher in LAC relative to other emerging market economies (Figure 20, panel 1). By contrast, the region devotes limited resources to capital spending, contributing to low investment rates (public and private) and economic growth relative to peers. Moreover, as seen historically, increasing spending pressures, including from rising financing costs, tend to reduce capital spending further. Improving spending efficiency, public procurement systems, and the targeting of social transfers, along with reductions in energy subsidies, are also key to contain spending growth. Making spending rationalization inclusive, however, is paramount to ensure social stability and fiscal sustainability. This means protecting spending to support the poor—through well-targeted social spending, efficient investment, and health and education spending. Countries that protected such outlays during recent fiscal consolidation episodes tended to fare better in growth and income distribution (Figure 20, panel 2).

Enhancing existing medium-term fiscal frameworks with the aim of strengthening fiscal discipline while protecting key spending outlays will also be key to durably reducing public debt levels and mitigating fiscal vulnerabilities. By garnering broad political consensus, such frameworks could

Figure 20. Public Spending Composition and Economic Impact of Fiscal Consolidations



Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: EMDE = emerging market and developing economies (excluding China and Latin America and the Caribbean); LAC = Latin America and the Caribbean (excluding Venezuela).
[1]Aggregates are fiscal year US dollar nominal GDP-weighted averages.
[2]Protected (not protected) refers to cases in which public investment, education, and health spending during the consolidation years have an annual change above (below) the mean of all consolidation episodes. When such spending changes are above the mean, the underlying consolidation episodes is classified as "protecting" the respective spending outlay. Gini index (disposable income) scale is inverted; higher values reflect improvement in income distribution. Identification of fiscal consolidation episodes follow David and Leigh (2018) for LAC, and Devries and others (2011) and Alesina and others (2018) for advanced economies. Sixty-six fiscal consolidation episodes in 11 LAC countries and 16 advanced economies covering the period 1978–2016 are analyzed.

also reduce public financing costs and help secure additional fiscal space (Cardenas and others 2021). Strengthening public debt management practices could also help reduce fiscal vulnerabilities, which are larger in LAC relative to peers.

Boosting Productivity Is Paramount to Increasing Potential Growth and Resilience

Tackling the region's longstanding productivity underperformance relative to other emerging markets and advanced economies will be crucial to boosting potential growth and making the region's economies more resilient (Annex 3).

A comprehensive reform agenda, that includes streamlining and modernizing business and labor regulations, could reduce informality, increase productivity, and enhance flexibility and resilience to shocks. The link between informality, productivity, and resilience suggests that the benefits of such agenda could be sizeable. Resource allocation and associated productivity gains could be facilitated by improving insolvency frameworks and easing firms' entry and exit. Simplifying and improving labor and corporate taxation, including by lowering compliance costs for workers and firms would also help reduce informality (IMF 2019, IMF 2021a). Bolstering human capital accumulation (particularly through high-quality investment in digitalization, basic education and vocational and technical training) and financial inclusion (through appropriate financial regulations) will also be key to reducing skills mismatches in the region, supporting productivity growth and limiting the scars from the pandemic (Ferreyra and others 2021; OECD 2019; World Bank 2021). Closing LAC's labor participation gap, by strengthening childcare and leave policies, would expand the supply of skilled workers and boost GDP growth (Novta and Wong 2017).

A broad set of government policies would also be needed to tackle climate change, involving measures such as removing fuel subsidies, increasing carbon taxes and adopting climate-supportive regulations, and scaling up green investments (IMF 2021b). Vulnerable countries, particularly in the Caribbean and Central America, also need to invest in resilience building and climate adaptation. The burden on public finances from these investments could be eased with deeper engagement of the private sector and the international community in providing funding and technical assistance.

Support from the international community will be key to helping LAC countries tackle both their short- and longer-term policy challenges, especially as global financial conditions tighten. Since the beginning of the pandemic, the IMF has made available close to $200 billion to 24 countries in the region, including canceled credit lines, of which $135 billion corresponded to Flexible Credit Lines for countries with strong fundamentals and policy frameworks. The 2021 general special drawing rights allocation, of which approximately $52 billion was directed to LAC, has also helped augment resources and relax financing constraints. The recently established Resilience and Sustainability Trust will help low-income and vulnerable middle-income countries build resilience to external shocks and ensure sustainable growth, contributing to their longer-term balance of payments stability. It will complement the IMF's existing lending toolkit by providing affordable financing to address longer-term challenges, including climate change and pandemic preparedness. The IMF also continued providing extensive policy advice and capacity development to countries in the LAC region throughout the pandemic. The IMF stands ready to continue engaging with the region through surveillance, programs, and capacity development. Capacity development spending for the region is expected to double in the next few years, with new areas such as climate- and gender-related activities supplementing more traditional topics.

Box 1. Central America, Panama, and the Dominican Republic: Country Focus

Strong external demand and a recovery in tourism bolstered activity in Central America, Panama, and the Dominican Republic in early 2022, while remittances inflows remained strong—especially in Guatemala, Honduras, and Nicaragua—supporting domestic demand. However, the weakening external environment, combined with the adverse impact of the inflation shock on real incomes and the resulting tightening of domestic policies are weighing on economic activity, which is expected to slow in the second half of 2022. Subsequently, prospects for growth in 2023 have weakened, and sizable downside risks remain, including from a weaker external demand, further increases in food and energy prices, new COVID-19 outbreaks, tighter global financial conditions, and reemergence of natural disasters.

Inflation in the region has reached levels unseen in over a decade, largely driven by global food and energy prices, although price pressures have also fed into core inflation reflecting robust domestic demand. Most countries with independent monetary policy in the region have raised policy rates in the context of rising inflation and inflation expectations. All countries in the region introduced fiscal measures to mitigate the impact of the price increases, largely focused on subsidies and price freezes. While most measures were announced as temporary, several have been extended multiple times, putting additional pressure on fiscal accounts.

Policies will need to remain nimble and responsive to incoming data, with the aim of preserving macroeconomic stability, taming inflation pressures, and avoiding a de-anchoring of inflation expectations, while protecting fiscal credibility. Sustaining fiscal consolidation should remain a priority, and resources should be prioritized to shield the most vulnerable from further price shocks through well-targeted programs. Associated costs should be offset by cuts in other nonessential expenditures to ensure that the budgetary impact is neutral. For all countries but especially for those with elevated social and infrastructure gaps, sound medium-term fiscal frameworks, together with improved fiscal transparency and governance, will be integral to achieving inclusive growth and alleviating poverty.

- In *Costa Rica*, a vigilant data-dependent approach for monetary policy remains appropriate. Fiscal consolidation under the fiscal rule should advance, while making space for resources to protect the most vulnerable, incentivize formal employment, pursue women's economic empowerment, and support the transition to a low-carbon economy.
- In the *Dominican Republic*, monetary and macro-financial policy normalization should be continued while maintaining temporary fiscal policy support to contain the impact of commodity prices. Global developments pose risks and may require nimble policies to shield the vulnerable and keep inflation expectations anchored.
- In *El Salvador*, the fiscal situation remains critical, making fiscal consolidation the top priority. Risks stemming from the adoption of Bitcoin as legal tender need to be addressed.
- In *Guatemala*, policies should remain agile to shield the vulnerable from high food and energy prices and focus on addressing longstanding social and infrastructure gaps (crucial to lifting inclusive growth and alleviating poverty), all supported by a solid medium-term fiscal framework.
- In *Honduras*, preserving macroeconomic stability while continuing to support the population remains essential.
- In *Nicaragua*, priorities include ensuring medium-term fiscal sustainability in an inclusive manner, solidifying financial stability, strengthening anti–money laundering/combating the financing of terrorism

This box was prepared by Metodij Hadzi-Vaskov and Joyce Wong, with inputs from Central America, Panama, and the Dominican Republic country teams.

Box 1. Central America, Panama, and the Dominican Republic: Country Focus *(continued)*

frameworks further to ensure exit from the Financial Action Task Force on Money Laundering gray list, and implementing structural reforms to support higher contribution of labor to growth.

- In *Panama*, the gradual fiscal consolidation should continue as envisioned under the Social and Fiscal Responsibility Law to ensure that public debt remains on a declining path. Building on recent progress, efforts should focus on swiftly exiting the Financial Action Task Force on Money Laundering gray list, which remains the authorities' top priority.

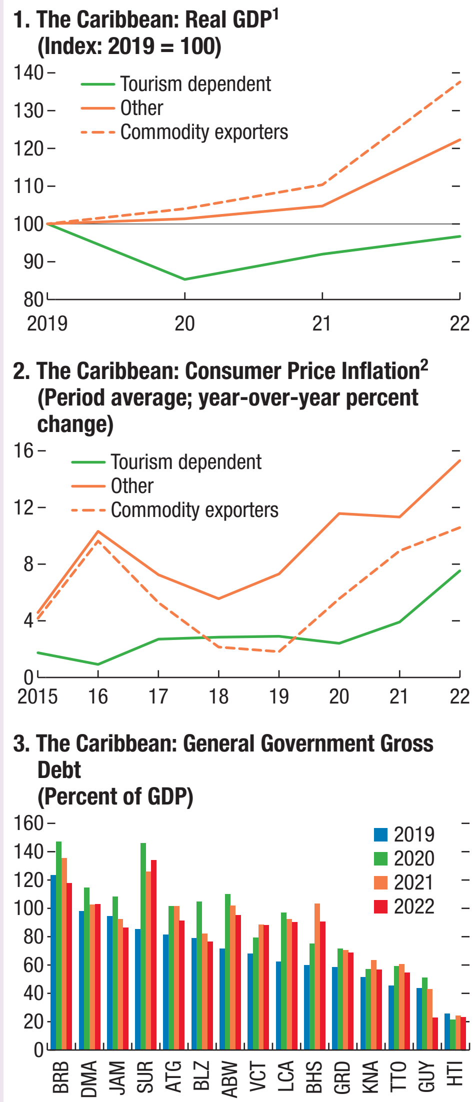
Box 2. The Caribbean: Uneven Recovery with Downside Risks

The recovery remains gradual and uneven (Box Figure 2.1, panel 1). With tourism remaining below prepandemic levels for most countries, tourism-dependent economies are expected to grow by about 5.2 percent in 2022 and 3.6 percent in 2023, after a deep recession in 2020, and a modest recovery in 2021. Countries that rely heavily on remittances (such as Belize, Haiti, and Jamaica) could see reduced inflows as the US economy slows. Commodity exporters (Guyana, Suriname, Trinidad and Tobago) are benefiting from high global commodity prices, while Guyana's growth is expected to remain in double digits in 2022 and 2023, as oil production continues increasing sharply. High global food and fuel prices and supply-chain disruptions have put upward pressure on domestic prices (Box Figure 2.1, panel 2) and threatened food and energy security because most countries in the region rely on imported fuel and food. In countries with floating exchange rates (such as Jamaica), policy interest rates have been raised, but the monetary policy transmission is weak.

Risks from tighter global financial conditions are limited, given the region's low financial integration. Risks to the outlook are tilted to the downside and include (1) slower growth in tourism source markets, (2) additional US dollar appreciation that could dent the competitiveness of countries that peg to the US dollar, (3) an escalation of the war in Ukraine, (4) additional supply-chain disruptions, (5) new COVID-19 outbreaks, and (6) natural disasters.

In response to high inflation, governments should provide temporary and well-targeted transfers to the vulnerable, by expanding social assistance programs while allowing a gradual pass-through of international prices and phasing out generalized subsidies. With elevated government debt in most countries (Box Figure 2.1, panel 3) and rising financing costs, policies should focus on restoring or safeguarding debt sustainability. As tourism returns to prepandemic levels, fiscal consolidation will be needed to restore fiscal space in tourism-dependent economies. In addition, ensuring debt sustainability may require novel financing solutions. For countries at risk of large natural disasters, contract clauses that allow for delayed repayments when disaster strikes (such as those recently introduced by Barbados and Grenada) are a promising way to increase financial resilience. Belize

Box Figure 2.1. The Caribbean



Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: Data labels use International Organization for Standardization (ISO) country codes. For country group information, please see page 46. "Other" includes commodity exporters.
[1]Aggregates are purchasing-power-parity GDP-weighted averages.
[2]Aggregates are US dollar nominal GDP-weighted averages.

This box was prepared by Bert van Selm, with research assistance by Adam Siddiq.

Box 2. The Caribbean: Uneven Recovery with Downside Risks *(continued)*

recently agreed to specific marine protections in exchange for a reduction in its international debt to private bondholders—a "debt-for-nature" swap.

Caribbean countries must also contend with the threat of more frequent and intense natural disasters and the rise in sea levels. Guided by disaster resilience strategies (such as those developed in Dominica and Grenada) and national disaster plans, countries should factor climate risks and adaptation policies into their budgets and infrastructure investments. The IMF's new Resilience and Sustainability Trust can help address climate challenges. All Caribbean IMF member countries are eligible for this longer-term, affordable financing, along with a conventional IMF arrangement, which provides a financing option to countries without prior access to concessional IMF financing. It may also help catalyze financing from international financial institutions and the private sector.

Box 3. Latin America 5 and Other South American Economies: Country Focus

In *Argentina*, domestic vulnerabilities and policy uncertainties, coupled with a worsening external environment, are aggravating the outlook. The policy tightening assumed under the IMF-supported program will be critical to strengthen stability and rein in inflation, which is now projected to reach 95 percent by the end of 2022. Real GDP growth is projected to moderate to 4 percent this year, but downside risks dominate this outlook.

In *Brazil*, growth is projected at 2.8 percent in 2022, reflecting the economy's strong performance in the first half of the year, but tighter financial conditions and global headwinds are expected to weigh on growth. Amid high and broad-based inflation, the central bank has raised the monetary policy rate to 13.75 percent, a 1,175 basis point increase since March 2021. After withdrawing the exceptional pandemic support in 2021, the government has relaxed the fiscal stance this year, including by approving tax relief measures to lower energy prices and expanding the social safety net. Public debt remains high amid relatively modest potential growth. Policy priorities—to promote inclusive growth and fiscal consolidation—include comprehensive tax and public administration reforms, reducing distortive mandatory public spending, promoting international trade, and reducing product and labor market rigidities.

In *Bolivia*, growth is projected to moderate to 3.8 percent in 2022, as export prices remain high but financial conditions tighten. The fixed exchange rate regime, together with strong agricultural production and various subsidies and price controls, has helped to keep domestic prices stable, but inflation is projected to edge upward by the end of 2022. Fiscal pressures and a declining stock of international reserves have increased Bolivia's vulnerability to external shocks.

In *Chile*, growth is expected to moderate to 2.0 percent in 2022 and –1.0 percent in 2023 amid the necessary recalibration of monetary and fiscal policies. The balance of risks is tilted to the downside, reflecting a challenging external environment. Risks also stem from possible social discontent emanating from high food and energy prices, unmet social demands, or the uncertain outcome of the constitutional reform process. Aided by decisive monetary tightening, inflation is expected to gradually converge to target by the end of 2024. The authorities' fiscal consolidation is advancing significantly faster than anticipated and will continue to be guided by the structural balance rule over the medium term amid ambitious reform plans for taxes, pensions, and health care.

In *Colombia*, private consumption continued to drive solid growth in the first half of 2022 amid robust employment and credit growth, while exports and business investment continue their recovery. A positive output gap, which already opened in the second quarter, is projected for the second half of 2022, raising overheating concerns amid already high inflation. The external deficit is also likely to widen. Given the monetary policy tightening in 2022 and fiscal consolidation in 2023, GDP growth is projected to moderate to 2.2 percent in 2023. Headline inflation is expected to converge to the central bank's target range in 2024.

In *Ecuador*, the economic recovery continued in early 2022, driven mainly by private consumption, but it is expected to moderate amid disruptions of agricultural exports to Russia, the global impact of the war in Ukraine, and domestic social unrest. Higher oil prices are expected to strengthen fiscal and external balances. The government is pursuing reforms in public procurement, public entities, social assistance, fiscal data quality and transparency, and tax administration, but a fragmented political landscape may challenge their implementation.

In *Mexico*, after a solid first half of 2022, the economy is expected to slow in late 2022 and early 2023, in tandem with the United States. Inflation has risen sharply in Mexico though somewhat less than in the United

This box was prepared by the Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru) and other South American country teams.

Box 3. Latin America 5 and Other South American Economies: Country Focus *(continued)*

States and Latin American peers. Banco de México has hiked the policy rate by 450 basis points to 8.5 percent since last summer. Fiscal policy is expected to remain prudent, in line with the traditional focus on long-term sustainability. The budgetary costs of the generalized fuel subsidy and higher interest costs because of upward inflation surprises are key near-term challenges.

Paraguay is still recovering from the pandemic. Facing a severe drought and the spike in global inflation, GDP growth is projected at only 0.2 percent for 2022, but it is expected to reach 4.3 percent next year. Responding to a strong rise in inflation (11.1 percent by July 2022), the central bank has steadily raised the policy rate since August 2021. Inflation is projected to converge back to the 4 percent target by early 2024.

In *Peru*, growth is moderating as the rebound from the 2020 slump wanes, external conditions tighten, and the policy stimulus is withdrawn. The balance of risks is tilted to the downside as significant external risks are compounded by heightened political uncertainty. Inflation peaked in June 2022 amid softening global energy and food prices, a 625 basis point increase in the central bank's policy rate in the last 13 months, and fiscal measures such as increases in energy subsidies and temporary tax exemptions. Inflation is expected to return to the target range in late 2023. Peru's fiscal and external buffers remain large, comparing favorably with most countries in the region.

In *Uruguay*, the recovery continued in early 2022, driven primarily by commodity exports and private consumption. Growth is projected to reach 5.3 percent in 2022 and moderate to 3.6 percent in 2023, as external conditions worsen, and the output gap closes. Additional monetary tightening will likely be needed to bring inflation within the target range over the monetary policy horizon. Fiscal accounts are projected to continue strengthening this year, but additional efforts will be needed to put debt on a firm downward path.

In *Venezuela*, after a seven-year contraction that shrunk the country's GDP by almost 75 percent, a tepid recovery is under way in the context of increasing oil production and an easing of restrictions on private sector production and imports. Venezuela has exited hyperinflation amid a sharp monetary policy tightening and a ramping up of foreign exchange interventions. The country continues to be immersed in a deep economic, political, and humanitarian crisis, which has resulted in about 6 million people (20 percent of the population) fleeing the country since 2014—one of the largest external displacement crises in the world.

Annex 1. Spillovers of US Monetary Tightening to Latin America

This chapter studies spillovers from US monetary policy tightening into Latin America, in the context of weakening commodity prices, combining empirical and model-based analyses.

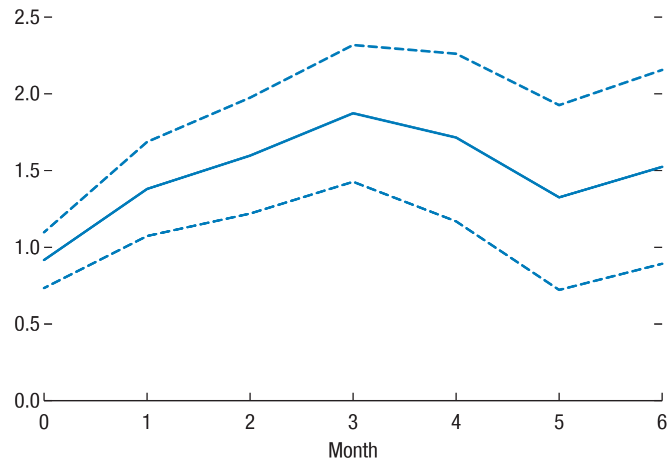
Historically, the tightening of global financial conditions generated strong spillovers to financial markets in the Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru), with a broad-based impact on sovereign debt markets: more than one-to-one shifts in US dollar and local currency bond yields in relation to the increase in US interest rates, sizable capital outflows, and depreciation pressures on domestic currencies (Annex Figure 1.1). Financial spillovers also had a substantial impact on domestic output, much of which was transmitted through the tightening of domestic financial conditions. Moreover, the likelihood of adverse tail events—for gross capital flows, exchange rates, and output—increased significantly with tighter US financial conditions.

Strong fundamentals—higher central bank credibility, reserve cushions, current account balances, lower public gross financing needs, and a lower foreign currency debt—tend to mitigate spillovers from US monetary policy (Annex Figure 1.2). The region has seen some of these fundamentals improve over time (compared with previous episodes of global financial tightening), but others have deteriorated, painting a mixed picture and suggesting that the region may still be vulnerable to marked shifts in US monetary policy.

High commodity prices, partly driven by supply-side shocks, have been an important counterbalancing force to the spillovers from US monetary policy in early 2022 for the net exporters of those commodities. However, US monetary policy tightening has historically been

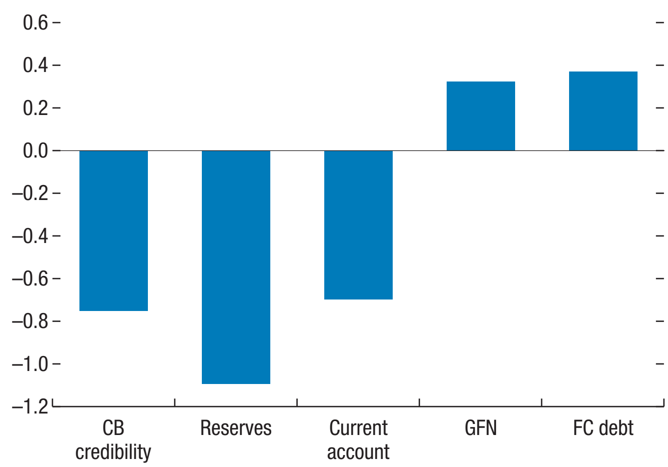
This annex presents a summary of October 2022 *Regional Economic Outlook: Western Hemispher*, "Spillovers of US Monetary Tightening to Latin America" (Background Paper 1), prepared by Maximiliano Appendino, Chao He, Takuji Komatsuzaki (lead), and Samuel Pienknagura.

Annex Figure 1.1. LA5: Impact of US Two-Year Bond Yield Increase on Long-Term Local Currency Yield
(Percentage points)



Source: IMF staff calculations.
Note: Short-term local-currency bond yields correspond to bonds with three months or shortest available maturity and long-term local-currency bond yields correspond to bonds with 10-year maturity. Point estimates (solid lines) are impulse responses to 1 percentage point change in the US two-year bond yields. Sample is monthly from January 2010 to December 2019. Ninety percent confidence intervals (dashed lines) are reported. LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).

Annex Figure 1.2. Differential Impact of US Two-Year Bond Yield Increase on Local Currency Yield
(Percentage points)



Source: IMF staff calculations.
Note: Columns show the differential impact of a rise of the US two-year bond yield on the local currency yield between emerging market economies with high and low values of the fundamentals mentioned in the *x* axis. Emerging market economies are Brazil, Bulgaria, Chile, Colombia, Hungary, India, Indonesia, Malaysia, Mexico, Peru, Philippines, Poland, Romania, Russia, Thailand, and Türkiye. See further details in IMF (2022a). CB = central bank; FC = public foreign currency; GFN = public gross financing needs.

associated with a weakening of commodity prices and a deterioration in the terms of trade of Latin America and the Caribbean countries, suggesting that the mitigating role of commodity prices may be reduced.

Annex 2. The Inflation Surge: Policy Trade-offs amid Uncertainty

This chapter studies the nature of Latin America's current inflation episode and the risks of inflation becoming entrenched, and discusses policy responses to mitigate these risks. The analysis is carried out in the context of the highest inflation spike observed in recent years that is testing the hard-won credibility of central banks in the region.

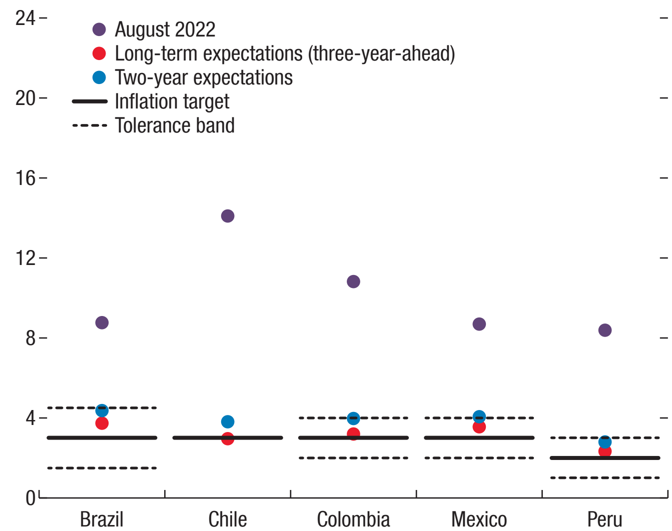
Global factors—reflecting the globally synchronized demand recovery and the increase in global commodity prices—were the main drivers of the current inflation surge, but the role of domestic factors has been increasing as inflation has become broad-based, leading to the acceleration of core goods and core services prices. The inflation process is also displaying increasing persistence, as indicated by Phillips curve estimates that point to inflation dynamics becoming increasingly backward-looking, similar to previous inflation episodes in the region (in 2008–09 and 2015–16). The expected duration of the current episode is broadly aligned with history, but deviations of inflation from central banks' tolerance bands are among the largest in recent decades, flagging upside risks to the persistence of the inflation process. Furthermore, even though nominal wages still seem to lag inflation, they are currently accelerating and may add inflation pressures amid tightening labor markets.

The swift policy actions of Latin American central banks have been key to keeping long-term inflation expectations broadly anchored despite multiple short-term inflation surprises since 2021 (Annex Figure 2.1), but rising short-term inflation expectations are a risk.

Policymakers should remain focused on preserving the long-term benefits of low inflation, rather than

Annex Figure 2.1. LA5: Actual and Consensus Forecasts Inflation

(End of period; year-over-year percent change)



Sources: Consensus Economics; Haver Analytics; national authorities; and IMF staff calculations.
Note: Two-year-ahead expectations are the average of July 2022 *Consensus Economics Forecasts* for end-2023 and end-2024. LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).

on the short-lived impact of monetary policy on output, by staying the course of tight monetary policy until the price pressures durably recede. The uncertain inflation process also requires central banks to continue effectively communicating their data-dependent policy decisions, and to appropriately signal future actions and contingency plans.

This annex presents a summary of October 2022 *Regional Economic Outlook: Western Hemisphere*, "The Inflation Surge: Policy Trade-offs amid Uncertainty" (Background Paper 2), prepared by Maximiliano Appendino (lead), Takuji Komatsuzaki, and Samuel Pienknagura.

Annex 3. Productivity in Latin America and the Caribbean: Recent Trends and the COVID-19 Shock

The growth history of Latin America and the Caribbean (LAC) is characterized by its productivity underperformance relative to peer emerging markets and developing economies and advanced economies.

This underperformance is widespread, cutting across sectors and different types of firms. Evidence from sectoral data shows that LAC exhibits productivity gaps relative to the United States in all sectors, and that these gaps are larger than in other emerging markets and developing economies (Annex Figure 3.1, panel 1). LAC's productivity gap is also evident in firm-level data, which show that firms in the region have lower productivity levels compared to similar firms in other emerging markets and developing economies.

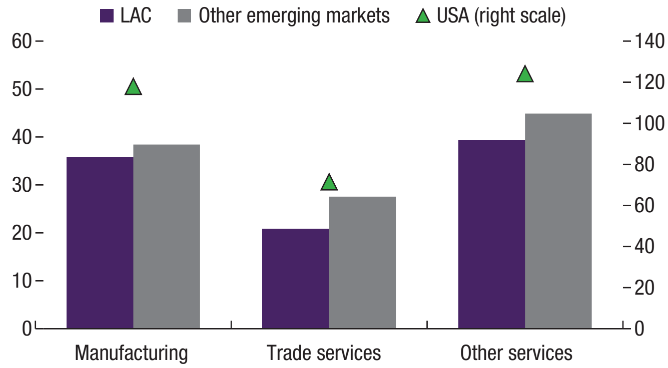
Several interrelated obstacles lie behind this pattern, including informality, burdensome regulations, complex and distortive taxation, and poor governance.

Moreover, economic downturns have historically hampered LAC's productivity more than in other regions. For example, in contrast to emerging markets and developing economies, firm-level productivity in LAC fell in the aftermath of the global financial crisis (Annex Figure 3.1, panel 2). More broadly, evidence on aggregate labor productivity also suggests that productivity in LAC falls after economic downturns, and even more than in other emerging markets and developing economies and advanced economies. In line with these findings, the pandemic is expected to result in large productivity losses in the region.

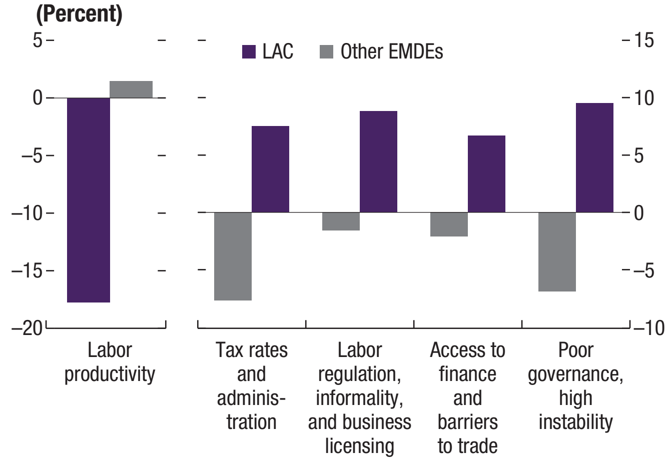
This annex, prepared by Santiago Acosta-Ormaechea (co-lead), Isabela Duarte, and Samuel Pienknagura (co-lead), is based on October 2022 *Regional Economic Outlook: Western Hemisphere*, "Productivity in Latin America and the Caribbean: Recent Trends and the COVID-19 Shock" (Background Paper 3).

Annex Figure 3.1. Visible Productivity Gaps across Sectors and after the Global Financial Crisis

1. Labor Productivity Levels across Sectors[1]
(Value added per employer in 2017; constant USD PPP, thousands)



2. Pre– and Post–Global Financial Crisis Difference in Average Labor Productivity and in Major Obstacles Faced by Firms[2]
(Percent)



Sources: Diepe (2021); IMF, World Economic Outlook database; World Bank Enterprise Surveys; and IMF staff calculations.
Note: For countries included in the other emerging markets, other EMDEs, and LAC samples, see IMF (2022c). EMDEs = emerging market and developing economies; LAC = Latin America and the Caribbean; PPP = purchasing power parity; USA = United States.
[1]PPP GDP-weighted average. Sectoral labor productivity is calculated for eight sectors: agriculture, construction, financial and business services, manufacturing, mining, trade services, utilities, and other services including transport services.
[2]Chart based on data from last survey before the global financial crisis (around 2007) and first survey after the global financial crisis (around 2015). Specific years vary by country due to availability of surveys. Bars indicate estimated difference in key variables pre– and post–global financial crisis for an average firm in LAC and in other EMDEs outside the region. For a detailed explanation of the four groups of obstacles and methodological details, see IMF (2022c).

LAC's productivity agenda should prioritize investments in human capital accumulation, focusing on improving its quality by addressing skills mismatches, and reverting the educational losses from the pandemic. Modernizing and streamlining business and labor regulation, including by strengthening insolvency frameworks to facilitate firms' entry and exit, could also yield significant productivity gains. These policies, coupled with tax reforms that enhance the design of labor and capital taxation to incentivize formalization while preserving fiscal sustainability, would lower compliance costs, reduce informality, promote productivity-enhancing investments, and increase the region's resilience to economic downturns. Moreover, the link between informality, productivity, and economic resilience suggests that such a reform agenda would also have sizable benefits in terms of increasing economic resilience.

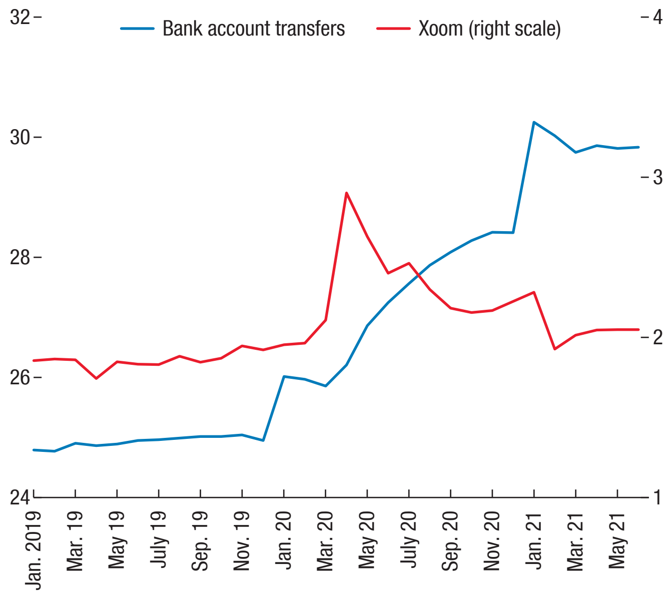
Annex 4. Remittances and Digitalization

Traditionally, remittances to Latin America and the Caribbean (LAC) have been mostly cash-based. Before the pandemic, only 23 percent of remittances were sent through digital means (including personal bank account transfers), with the rest being cash-based and conducted through brick-and-mortar remittances operators.

Remittances through bank account transfers increased with the pandemic-induced lockdowns, while instant digital remittances were also boosted, though only temporarily. Immigrants switched to digital modes as travel restrictions and lockdowns closed brick-and-mortar remittances operators in the United States in the initial phase of the pandemic (Annex Figure 4.1). In El Salvador, for instance, growth in remittances through bank account transfers averaged at 37 percent year-over-year in the second half of 2020, more than double the growth in other modes. Similarly, financial technology remittances that rely on technological innovations for money transfers, such as Xoom, accelerated rapidly during the pandemic. However, as lockdown restrictions eased, the use of financial technology remittances reverted to prepandemic levels, while the share of remittances through bank account transfers stabilized at above prepandemic levels.

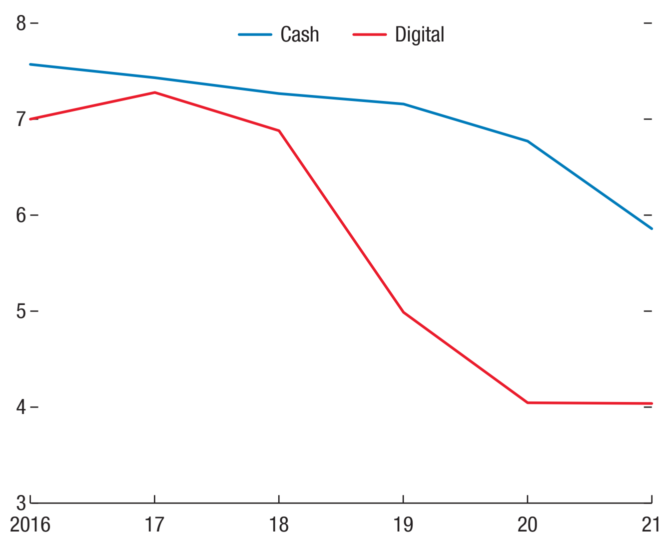
Despite this progress and the lower transaction costs of new remittances technologies, digital remittances in LAC remain among the lowest in the world. Available data indicate that the share of instant digital remittances in LAC increased from 8 percent in 2016 to about 17 percent in 2021, helped by the lower transaction costs of the new digital technologies (Annex Figure 4.2). Penetration of digital modes in LAC, however, remains below the 24 percent global average.[1] Moreover, the share of mobile money remittances in the region at 0.2 percent remains among the

Annex Figure 4.1. Digital Remittances in El Salvador
(Percent of total remittances)



Sources: National authorities; and IMF staff calculations.

Annex Figure 4.2. Digital and Cash Remittances Cost
(MoneyGram; average; percent of 200 US dollar transfer)



Sources: World Bank, Remittance Prices Worldwide database; and IMF staff calculations.
Note: Includes Brazil, Colombia, Costa Rica, the Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, and Peru.

This annex was prepared by Yorbol Yakhshilikov.
[1]Based on estimates for the region by Orozco and Martin (2022) and global estimates in the Western Union Company's 2016 and 2021 annual reports.

lowest in the world—below the world average of 1 percent and significantly below the average of 23 percent in the sub-Saharan Africa region. This is despite a wide access to mobile phones of LAC's population (78 percent), suggesting that the main obstacles to greater use of digital modes of remittances may not relate to the lack of access to information technologies.

Some structural factors (which are likely to constrain further digitalization) are behind the lower degree of digitalization in LAC. First, a low appetite for digital remittances is arguably linked to the limited use of digital money and financial inclusion more broadly in LAC, as cash dominates in the *receiving* economies with large informal sectors (Bersch and others 2021). Second, the limited demand for digital remittances also reflects low financial inclusion of the *sending* migrant population in the United States. Third, gaps in the regulatory environment also might explain the low penetration of digital remittances in LAC. For example, according to the Global System for Mobile Communications Mobile Money Regulatory Index, which captures some of the aspects relevant for digitalization of remittances, LAC scores the lowest in the world, especially in Know Your Customer regulation. This regulation ensures that remittances operators can identify and verify their customers to comply with anti–money laundering/combating the financing of terrorism regulation needed for LAC countries to maintain access to international payment systems such as, for example, correspondent banking. Tackling informality, improving financial inclusion, and aligning domestic regulatory frameworks with international standards—alongside a comprehensive application of rules for anti–money laundering/combating the financing of terrorism and compliance of digital IDs with Know Your Customer regulation—will be key to reaping the full benefits of new digital technologies in the region.

Annex 5. Risks Associated with the Nonbank Financial Sector in Latin America and the Caribbean

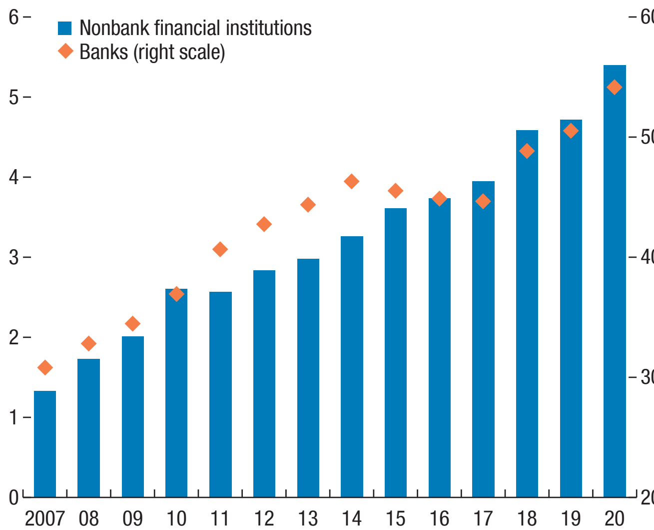
The nonbank financial sector has grown markedly in Latin America and the Caribbean (LAC) over the last 15 years, rising fourfold in size—driven mainly by nonbank activities Chile and Mexico—and outpacing other emerging market economies (Annex Figures 5.1 and 5.2). While still relatively small compared with the banking system, which supplies about 90 percent of the total credit to the private sector, nonbanks could pose financial stability risks.

The nonbank financial sector's landscape encompasses a wide range of institutions, including investment and pension funds, insurance companies, cooperatives, leasing companies, finance companies, and so on. Given the diversity of business models, balance sheets, and regulatory regimes, the risk profiles of these institutions are not necessarily uniform. Compared with banks, however, they are characterized by weaker liquidity and funding profiles (Fitch Ratings 2019), higher leverage (Aramonte and Avalos 2021; FSB 2021), more volatile returns (CGFS 2010; Fitch Ratings 2022), and lighter prudential and conduct supervision (Carstens 2021; World Bank 2018).

- *Funding and liquidity risk:* Compared with the banking sector, the nonbank financial sector in LAC tends to have more limited access to global capital markets and central bank liquidity support, making them more vulnerable to shifts in investors' risk appetite, especially for nonbank institutions that operate with large maturity mismatches (for example, investment funds that allow for daily withdrawals while investing in long-term, illiquid debt instruments). This was the case of some collective investment funds in Colombia at the onset of the pandemic, which faced

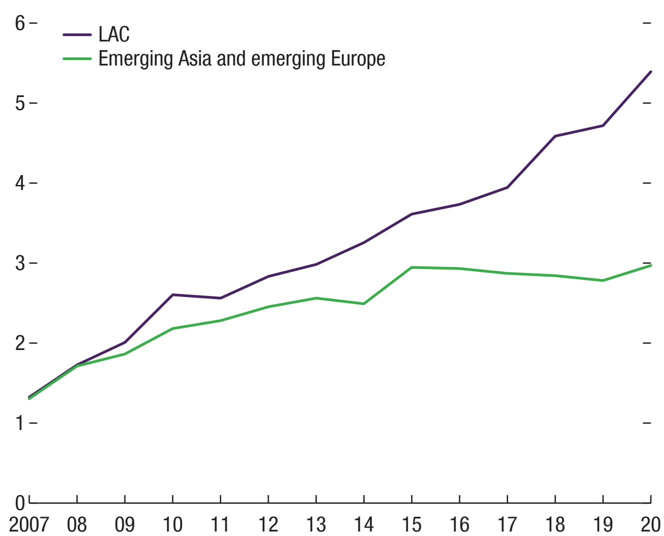
This annex was prepared by Yuanchen Yang.

Annex Figure 5.1. LAC: Credit to the Private Sector
(Percent of GDP)



Sources: IMF, International Financial Statistics database; World Bank, World Development Indicators database; and IMF staff calculations.
Note: "Nonbank financial institutions" refers to financial institutions other than monetary authorities and deposit money banks (including finance and leasing companies, money lenders, insurance corporations, pension funds, and foreign exchange companies). LAC = Latin America and the Caribbean.

Annex Figure 5.2. Domestic Credit to Private Sector from Nonbank Financial Institutions
(Percent of GDP)



Sources: IMF, International Financial Statistics database; World Bank, World Development Indicators database; and IMF staff calculations.
Note: LAC = Latin America and the Caribbean.

significant investor withdrawals leading to a 32 percent decline in total assets.

- *Volatile returns:* Because of limited capital buffers, high volatility of asset returns is often a source of risks for some nonbank lenders. For example, in Mexico, some large nonbank lending companies have faced rising financing costs and low profitability in the context of high inflation and subdued economic activity.
- *Regulation and supervision:* Lax regulation and supervision of the nonbank financial sector could also be a source of financial stability risk.

If sustained, the rapid growth of largely unregulated and intrinsically more vulnerable nonbank financial institutions could pose risks to financial stability, especially in a context of high uncertainty and tightening financial conditions. Policymakers should consider strengthening prudential supervision and regulation of these corporations and monitor them closely.

Annex 6. Country Notes

For *Argentina*, the official national consumer price index starts in December 2016. For earlier periods, consumer price index data for Argentina reflect the Greater Buenos Aires area consumer price index (prior to December 2013), the national consumer price index (IPCNu, December 2013 to October 2015), the City of Buenos Aires consumer price index (November 2015 to April 2016), and the Greater Buenos Aires area consumer price index (May 2016 to December 2016). Given limited comparability of these series on account of differences in geographical coverage, weights, sampling, and methodology, the *World Economic Outlook* does not report average consumer price index inflation for 2014–16 and end-of-period inflation for 2015–16. Also, Argentina discontinued the publication of labor market data starting in the fourth quarter of 2015, and new series became available starting in the second quarter of 2016.

For *Chile*, projections were prepared prior to the 2022 Article IV mission that ended on October 27, 2022 and thereby do not reflect mission updates.

For *Costa Rica*, the central government definition has been expanded as of January 1, 2021, to include 51 public entities as per Law 9524. Data back to 2019 are adjusted for comparability.

The fiscal series for the *Dominican Republic* have the following coverage: public debt, debt service, and the cyclically adjusted/structural balances are for the consolidated public sector (which includes the central government, the rest of the nonfinancial public sector, and the central bank); the remaining fiscal series are for the central government.

For *Ecuador*, the authorities are undertaking revisions of the historical fiscal data with technical support from the IMF.

For *Honduras*, projections were prepared prior to the 2022 Article IV mission that ended on October 5, 2022 and thereby do not reflect mission updates.

In December 2020, the *Uruguay* authorities began reporting the national accounts data according to System of National Accounts 2008, with the base year 2016. The new series begins in 2016. Data prior to 2016 reflect the IMF staff's best effort to preserve previously reported data and avoid structural breaks.

Since October 2018, *Uruguay's* public pension system has been receiving transfers in the context of a new law that compensates persons affected by the creation of the mixed pension system. These funds are recorded as revenues, consistent with the IMF's methodology. Therefore, data and projections for 2018–21 are affected by these transfers, which amounted to 1.2 percent of GDP in 2018, 1.1 percent of GDP in 2019, 0.6 percent of GDP in 2020, and 0.3 percent of GDP in 2021, and are projected to be 0.1 percent of GDP in 2022 and zero percent thereafter. See IMF Country Report 19/64 for further details.[1] The disclaimer about the public pension system applies only to the revenues and net lending/borrowing series.

The coverage of the fiscal data for *Uruguay* was changed from consolidated public sector to nonfinancial public sector with the October 2019 *World Economic Outlook*. In Uruguay, nonfinancial public sector coverage includes central government, local government, social security funds, nonfinancial public corporations, and Banco de Seguros del Estado. Historical data were also revised accordingly. Under this narrower fiscal perimeter—which excludes the central bank—assets and liabilities held by the nonfinancial public sector for which the counterpart is the central bank are not netted out in debt figures. In this context, capitalization bonds issued in the past by the government to the central bank are now part of the nonfinancial public sector debt. Gross and net debt estimates for 2008–11 are preliminary.

Projecting the economic outlook in *Venezuela*, including assessing past and current economic

[1]See Uruguay: Staff Report for the 2018 Article IV Consultation, Country Report 19/64 (International Monetary Fund, Washington, DC, February 2019).

developments used as the basis for the projections, is rendered difficult by the lack of discussions with the authorities (the last Article IV consultation took place in 2004), incomplete metadata of limited reported statistics, and difficulties in reconciling reported indicators with economic developments. The fiscal accounts include the budgetary central government; social security; FOGADE (insurance deposit institution); and a reduced set of public enterprises, including Petróleos de Venezuela, S.A. Following some methodological upgrades to achieve a more robust nominal GDP, historical data and indicators expressed as percentage of GDP have been revised from 2012 onward. For most indicators, data for 2018–22 are IMF staff estimates. The effects of hyperinflation and the paucity of reported data mean that IMF staff's projected macroeconomic indicators need to be interpreted with caution. Wide uncertainty surrounds these projections. Venezuela's consumer prices are excluded from all *World Economic Outlook* group composites.

Appendix Table 1. Western Hemisphere: Main Economic Indicators[1]

	Real GDP Growth (Year-over-year percent change)					Inflation[2] (End of period; percent)					External Current Account Balance (Percent of GDP)				
				Projections					Projections					Projections	
	2019	2020	2021	2022	2023	2019	2020	2021	2022	2023	2019	2020	2021	2022	2023
North America	**2.0**	**–4.0**	**5.5**	**1.8**	**1.0**	**2.1**	**1.6**	**7.2**	**6.6**	**2.6**	**–2.0**	**–2.6**	**–3.2**	**–3.4**	**–2.8**
Canada	1.9	–5.2	4.5	3.3	1.5	2.1	0.7	4.7	6.9	3.2	–2.0	–1.8	0.0	0.5	–0.2
Mexico	–0.2	–8.1	4.8	2.1	1.2	2.8	3.2	7.4	8.5	4.8	–0.3	2.5	–0.4	–1.2	–1.2
United States	2.3	–3.4	5.7	1.6	1.0	2.1	1.5	7.4	6.4	2.3	–2.1	–3.0	–3.7	–3.9	–3.1
Puerto Rico[3]	1.5	–3.9	2.7	4.8	0.4	0.5	–0.1	4.2	4.8	2.3	. . .	. . .	. . .	. . .	. . .
South America	**0.0**	**–6.6**	**7.3**	**3.6**	**1.6**	**10.5**	**8.0**	**14.1**	**18.0**	**12.1**	**–2.8**	**–1.2**	**–2.0**	**–1.9**	**–1.5**
Argentina[4]	–2.0	–9.9	10.4	4.0	2.0	53.8	36.1	50.9	95.0	60.0	–0.8	0.8	1.4	–0.3	0.6
Bolivia	2.2	–8.7	6.1	3.8	3.2	1.5	0.7	0.9	4.2	3.6	–3.3	–0.7	2.0	–1.4	–2.1
Brazil	1.2	–3.9	4.6	2.8	1.0	4.3	4.5	10.1	6.0	4.7	–3.5	–1.7	–1.7	–1.5	–1.6
Chile[4]	0.9	–6.1	11.7	2.0	–1.0	2.9	2.9	7.1	12.2	6.2	–5.2	–1.7	–6.7	–6.7	–4.4
Colombia	3.2	–7.0	10.7	7.6	2.2	3.8	1.6	5.6	11.0	6.0	–4.6	–3.4	–5.7	–5.1	–4.4
Ecuador	0.0	–7.8	4.2	2.9	2.7	–0.1	–0.9	1.9	3.8	1.4	–0.1	2.7	2.9	2.4	2.1
Paraguay	–0.4	–0.8	4.2	0.2	4.3	2.8	2.2	6.8	8.2	4.2	–0.5	2.7	0.8	–3.8	–0.1
Peru	2.2	–11.0	13.6	2.7	2.6	1.9	2.0	6.4	6.8	3.0	–1.0	0.8	–2.5	–3.0	–2.1
Uruguay	0.4	–6.1	4.4	5.3	3.6	8.8	9.4	8.0	8.9	7.2	1.6	–0.8	–1.8	–1.2	–1.9
Venezuela[4]	–27.7	–30.0	0.5	6.0	6.5	9,585	2,960	686	220	150	6.6	–8.0	–2.1	4.0	6.0
CAPDR	**3.3**	**–7.1**	**11.0**	**4.7**	**3.6**	**2.5**	**2.8**	**5.1**	**7.8**	**4.4**	**–1.0**	**1.3**	**–1.9**	**–3.2**	**–2.5**
Costa Rica[5]	2.4	–4.1	7.8	3.8	2.9	1.5	0.9	3.3	9.5	4.8	–1.3	–1.0	–3.3	–4.8	–4.4
Dominican Republic	5.1	–6.7	12.3	5.3	4.5	3.7	5.6	8.5	8.0	4.9	–1.3	–1.7	–2.8	–3.3	–2.7
El Salvador	2.4	–8.2	10.3	2.6	1.7	0.0	–0.1	6.1	6.0	2.0	–0.4	0.8	–5.1	–8.9	–3.9
Guatemala	4.0	–1.8	8.0	3.4	3.2	3.4	4.8	3.1	8.0	4.6	2.4	4.9	2.5	1.1	0.8
Honduras[4]	2.7	–9.0	12.5	3.4	3.5	4.1	4.0	5.3	11.0	6.2	–2.6	2.8	–4.3	–4.6	–4.3
Nicaragua	–3.8	–1.8	10.3	4.0	3.0	6.1	2.9	7.2	10.0	5.5	6.0	3.9	–2.3	–3.2	–2.8
Panama[6]	3.0	–17.9	15.3	7.5	4.0	–0.1	–1.6	2.6	4.4	3.0	–5.0	2.0	–2.2	–3.7	–3.3
Caribbean: Tourism Dependent	**1.4**	**–14.7**	**7.8**	**5.2**	**3.6**	**3.7**	**2.5**	**5.4**	**8.3**	**4.3**	**–2.9**	**–10.9**	**–9.7**	**–10.7**	**–8.7**
Antigua and Barbuda	4.9	–20.2	5.3	6.0	5.6	0.7	2.8	1.2	10.5	2.7	–7.5	–18.4	–15.0	–19.0	–14.7
Aruba	0.6	–18.6	17.2	4.0	2.0	3.6	–3.1	3.6	7.7	3.0	2.6	–13.0	1.4	2.9	3.3
The Bahamas	1.9	–23.8	13.7	8.0	4.1	1.4	1.2	4.1	7.2	3.4	–2.6	–24.5	–23.1	–18.2	–14.1
Barbados	–1.3	–13.7	0.7	10.5	5.0	7.2	1.3	5.2	10.0	6.7	–3.1	–6.9	–11.5	–10.0	–8.7
Belize	4.5	–13.7	16.3	3.5	2.0	0.2	0.4	4.9	8.0	2.5	–7.8	–6.3	–6.7	–7.3	–7.1
Dominica	5.5	–16.6	4.8	6.0	4.9	0.1	–0.7	3.5	3.5	4.9	–34.4	–29.3	–32.5	–30.6	–28.1
Grenada	0.7	–13.8	5.6	3.6	3.6	0.1	–0.8	1.9	5.4	2.3	–14.6	–21.0	–24.2	–24.5	–19.8
Jamaica	1.0	–10.0	4.6	2.8	3.0	6.2	5.2	7.3	9.5	5.5	–2.2	–0.4	0.9	–6.0	–5.2
St. Kitts and Nevis	4.8	–14.0	–3.6	9.8	4.8	–0.8	–1.2	1.9	3.4	2.2	–2.2	–8.0	–5.0	–5.3	–4.0
St. Lucia	–0.7	–24.4	12.2	9.1	5.8	–0.7	–0.4	4.1	5.5	2.3	5.7	–15.7	–11.0	–6.0	–0.1
St. Vincent and the Grenadines	0.4	–5.3	0.5	5.0	6.0	0.5	–1.0	3.4	8.0	2.1	–3.1	–15.1	–22.6	–26.5	–27.6
Caribbean: Other	**0.0**	**1.3**	**3.4**	**16.7**	**9.3**	**7.8**	**14.4**	**11.7**	**16.8**	**9.0**	**–4.9**	**–4.1**	**1.4**	**16.0**	**13.5**
Haiti[7]	–1.7	–3.3	–1.8	–1.2	0.5	19.7	25.2	13.1	31.5	14.8	–1.1	1.1	0.5	0.8	–0.5
Commodity Exporters	1.0	4.0	6.1	24.6	12.8	1.4	8.6	11.0	10.8	6.8	–6.6	–6.7	2.0	22.5	19.8
Guyana	5.4	43.5	23.8	57.8	25.2	2.1	0.9	5.7	9.4	6.0	–53.3	–16.4	–25.5	43.5	30.4
Suriname	1.1	–15.9	–3.5	1.3	2.3	4.2	60.7	60.7	35.2	22.9	–11.3	9.1	5.8	–2.0	–0.9
Trinidad and Tobago[4]	–0.2	–7.4	–0.7	4.0	3.5	0.4	0.8	3.5	6.5	3.8	4.3	–6.3	10.4	14.3	15.9
Memorandum															
Latin America and the Caribbean	**0.2**	**–7.0**	**6.9**	**3.5**	**1.7**	**7.7**	**6.3**	**11.6**	**14.6**	**9.5**	**–2.0**	**–0.2**	**–1.6**	**–1.7**	**–1.4**
LAC excluding Venezuela	**0.8**	**–6.6**	**7.0**	**3.4**	**1.7**	7.7	6.3	11.6	14.6	9.5	–2.2	–0.1	–1.6	–1.8	–1.5
Eastern Caribbean Currency Union[8]	2.1	–17.8	5.2	7.2	5.4	–0.1	–0.1	2.7	6.3	2.6	–6.6	–16.0	–16.9	–16.7	–13.2

Sources: IMF, World Economic Outlook database; and IMF staff calculations and projections.

Note: CAPDR = Central America, Panama, and the Dominican Republic; LAC = Latin America and the Caribbean.

[1]Regional output growth aggregates are purchasing-power-parity GDP-weighted averages. Consumer price index inflation aggregates exclude Venezuela and are geometric purchasing-power-parity GDP-weighted averages. Current account aggregates are US dollar nominal GDP-weighted averages. Consistent with the IMF *World Economic Outlook*, the cutoff date for the data and projections in this table is September 26, 2022.

[2]These figures will generally differ from period average inflation reported in the IMF *World Economic Outlook*, although both are based on the same underlying series.

[3]Puerto Rico is classified as an advanced economy. It is a territory of the United States, but its statistical data are maintained on a separate and independent basis.

[4]See Annex 6 for details on the data.

[5]Staff projections for Costa Rica were further updated in the context of the Third Extended Fund Facility Review mission.

[6]Ratios to GDP are based on the 2007-base GDP series.

[7]Fiscal year data. For Haiti, estimates and projections reflect information available through early September 2022.

[8]Eastern Caribbean Currency Union comprises Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines, as well as Anguilla and Montserrat (which are not IMF members).

Appendix Table 2. Western Hemisphere: Main Fiscal Indicators[1]

	General Government Primary Expenditure (Percent of GDP)					General Government Primary Balance (Percent of GDP)					General Government Gross Debt (Percent of GDP)				
				Projections					Projections					Projections	
	2019	2020	2021	2022	2023	2019	2020	2021	2022	2023	2019	2020	2021	2022	2023
North America	**32.6**	**42.3**	**38.8**	**35.0**	**34.8**	**–2.7**	**–11.7**	**–7.7**	**–2.1**	**–3.1**	**104.1**	**129.6**	**123.2**	**116.9**	**117.4**
Canada	37.7	50.1	43.4	40.3	39.2	0.1	–10.9	–5.5	–2.6	–1.4	87.2	117.8	112.9	102.2	98.7
Mexico[2]	21.8	24.2	23.0	23.6	23.8	1.4	–0.5	0.0	0.8	0.3	53.3	60.1	57.6	56.8	58.7
United States[3]	32.9	42.7	39.4	35.2	35.1	–3.2	–12.4	–8.4	–2.2	–3.5	108.8	134.5	128.1	122.1	122.9
Puerto Rico[4]	19.0	19.3	18.9	19.1	18.8	4.0	1.5	1.7	2.4	2.0	48.9	50.2	47.9	16.0	14.8
South America	**29.6**	**34.1**	**29.8**	**28.9**	**28.3**	**–1.2**	**–7.5**	**–1.4**	**–0.4**	**–0.8**	**75.7**	**86.1**	**79.4**	**75.9**	**75.1**
Argentina[5]	33.7	39.6	36.0	34.9	33.7	–0.4	–6.2	–2.5	–1.9	–1.4	88.8	102.8	80.9	76.0	69.5
Bolivia[6]	34.7	36.5	33.0	33.3	32.6	–5.8	–11.2	–8.0	–6.6	–5.3	59.3	78.0	80.5	82.6	85.1
Brazil[7]	30.5	36.7	28.7	29.0	28.7	–0.9	–9.1	0.7	0.8	–0.8	87.9	98.7	93.0	88.2	88.9
Chile[8]	25.5	28.3	32.6	24.9	24.8	–2.4	–6.6	–6.9	1.1	–0.7	28.3	32.6	36.3	36.2	36.9
Colombia[9]	29.8	30.5	31.2	31.4	30.3	–1.0	–4.4	–3.9	–3.1	0.4	52.4	65.7	64.6	61.1	60.0
Ecuador[8,10]	34.4	33.7	34.2	33.7	32.8	–0.7	–4.3	–0.2	2.3	3.4	51.4	60.9	62.2	58.9	56.2
Paraguay	21.7	24.4	23.7	22.4	21.6	–2.5	–5.7	–4.5	–3.5	–2.0	25.8	36.9	37.7	39.3	38.9
Peru[11]	19.9	24.7	22.2	21.9	22.3	–0.2	–6.9	–1.2	–1.0	–1.2	26.9	35.0	36.4	34.8	35.7
Uruguay[8,12]	28.8	30.2	28.9	27.7	27.3	–0.5	–2.1	–0.7	–0.7	0.1	61.0	68.3	65.1	61.2	62.6
Venezuela[8]	18.7	9.2	10.5	. . .	. . .	–10.0	–4.9	–4.5	. . .	. . .	201.4	319.1	240.5	. . .	. . .
CAPDR	**17.1**	**20.2**	**18.1**	**17.5**	**17.2**	**–0.6**	**–4.4**	**–0.9**	**–0.5**	**–0.2**	**46.3**	**59.5**	**55.9**	**54.3**	**53.8**
Costa Rica[13]	17.6	17.7	16.1	14.6	13.9	–2.6	–3.8	–0.3	1.1	1.4	56.4	67.2	68.2	67.6	66.5
Dominican Republic[14]	13.8	18.9	15.4	15.0	14.4	0.6	–4.7	0.2	–0.4	0.0	53.6	71.5	63.1	58.4	57.6
El Salvador[14]	23.5	28.7	27.5	26.9	27.0	0.6	–3.8	–1.1	–0.2	–0.5	71.3	89.4	82.4	80.3	81.3
Guatemala[15]	11.8	13.9	11.8	12.4	12.3	–0.6	–3.2	0.6	–0.1	–0.3	26.4	31.5	30.8	30.1	30.0
Honduras[8]	23.6	25.5	26.0	. . .	. . .	0.8	–3.8	–2.1	. . .	. . .	42.9	52.4	50.2	. . .	. . .
Nicaragua[14]	26.6	27.9	29.4	28.0	26.4	0.9	–1.0	–0.5	–1.7	–0.8	41.7	48.1	49.4	47.0	45.9
Panama[16]	20.0	26.0	22.4	21.3	20.6	–1.8	–8.0	–4.6	–1.9	–1.0	41.9	65.6	58.4	55.6	55.1
Caribbean: Tourism Dependent	**22.1**	**27.1**	**26.7**	**24.4**	**23.2**	**3.6**	**–1.6**	**–0.2**	**1.2**	**2.1**	**81.2**	**99.8**	**99.2**	**90.8**	**85.9**
Antigua and Barbuda	19.9	24.2	22.5	22.0	21.2	–1.2	–3.8	–1.6	–0.9	0.2	81.3	101.5	101.4	91.2	84.4
Aruba	19.4	33.9	25.0	20.0	19.1	4.1	–11.0	–5.3	0.3	1.5	71.6	110.1	101.8	95.0	93.1
The Bahamas[15]	17.6	22.8	28.7	22.7	21.5	0.8	–4.2	–9.3	–1.1	–0.7	59.7	75.0	103.3	90.7	86.6
Barbados[17]	24.5	30.9	29.8	28.6	25.6	6.2	–1.0	–0.9	1.0	3.5	123.2	147.0	135.4	117.9	110.0
Belize[15]	25.0	29.4	23.5	22.9	22.9	–0.3	–5.5	–0.5	–0.1	0.2	79.0	104.5	82.2	76.3	73.1
Dominica[18]	45.8	65.8	51.7	48.8	47.2	–6.2	–5.7	7.6	–1.7	1.2	97.9	114.5	102.7	102.8	98.3
Grenada[18]	19.8	24.9	29.7	32.8	26.4	6.8	3.2	2.1	–1.3	3.6	58.5	71.4	70.3	68.9	66.3
Jamaica[18]	23.5	25.6	23.7	22.4	22.4	7.1	3.5	6.5	5.1	4.7	94.3	108.1	92.3	86.2	79.7
St. Kitts and Nevis[18]	35.1	33.1	34.0	39.0	31.5	0.5	–1.5	8.3	–4.0	2.2	51.5	56.8	63.4	56.5	55.2
St. Lucia[18]	22.1	30.1	26.6	25.5	21.3	–0.5	–8.0	–2.9	–2.4	1.2	62.1	96.9	92.2	90.1	88.3
St. Vincent and the Grenadines[18]	27.9	31.5	35.0	35.7	33.9	–0.8	–3.5	–4.9	–6.5	–3.7	68.1	79.2	88.4	87.9	88.0
Caribbean: Other	**23.0**	**23.7**	**21.2**	**18.8**	**18.5**	**–2.6**	**–6.1**	**–4.3**	**–0.3**	**–0.1**	**42.5**	**51.6**	**47.6**	**41.5**	**39.3**
Haiti[15,19]	9.9	9.6	10.5	9.9	10.7	–1.8	–2.1	–2.2	–1.2	–2.0	25.8	21.3	24.2	23.1	22.1
Commodity Exporters	29.0	30.4	27.8	22.6	21.9	–3.0	–8.0	–5.6	0.2	0.8	49.9	66.0	62.0	49.6	47.0
Guyana[15]	27.6	30.0	25.3	15.6	15.4	–2.0	–7.3	–6.7	–0.4	–0.2	43.6	51.1	42.9	22.8	20.9
Suriname[20]	39.4	26.9	28.5	25.9	23.5	–19.0	–8.4	–1.3	1.7	3.5	85.2	146.1	125.7	134.0	117.1
Trinidad and Tobago[15]	27.5	30.9	28.6	26.0	25.5	–0.6	–8.2	–5.7	0.3	1.0	45.4	59.3	60.6	54.7	54.4
Memorandum															
Latin America and the Caribbean	**26.7**	**30.4**	**27.1**	**26.8**	**26.4**	**–0.5**	**–5.5**	**–1.0**	**–0.1**	**–0.5**	**67.9**	**77.4**	**71.8**	**69.3**	**69.2**
LAC Excluding Venezuela	**26.8**	**30.6**	**27.3**	**27.0**	**26.6**	–0.3	–5.5	–1.0	0.0	–0.4	66.0	74.8	69.8	67.8	67.8
Eastern Caribbean Currency Union[18,21]	25.9	32.4	31.1	31.5	27.8	0.3	–3.1	0.4	–2.7	0.7	66.1	85.4	85.2	80.3	77.1

Sources: IMF, World Economic Outlook database; and IMF staff calculations and projections.

Note: CAPDR = Central America, Panama, and the Dominican Republic; LAC = Latin America and the Caribbean.

[1]Definitions of government vary across countries, depending on country-specific institutional differences, including on what constitutes the appropriate coverage from a fiscal policy perspective, as defined by the IMF staff. All indicators are reported on a fiscal year basis. Regional aggregates are fiscal year US dollar nominal GDP-weighted averages. Consistent with the IMF *World Economic Outlook*, the cutoff date for the data and projections in this table is September 26, 2022.

[2]Includes central government, social security system funds, nonfinancial public corporations, and nonmonetary public financial corporations.

[3]For cross-country comparability, expenditure and fiscal balances of the United States exclude the items related to the accrual-basis accounting of government employees' defined-benefit pension plans, which are counted as expenditure under the 2008 System of National Accounts (2008 SNA) adopted by the United States but not for countries that have not yet adopted the 2008 SNA. Data for the United States in this table may thus differ from data published by the US Bureau of Economic Analysis.

[4]Puerto Rico is classified as an advanced economy. It is a territory of the United States, but its statistical data are maintained on a separate and independent basis.

[5]Primary expenditure and primary balance include the federal government, provinces, and social security funds. Gross debt is for the federal government only.

[6]Nonfinancial public sector, excluding the operations of nationalized mixed-ownership companies in the hydrocarbon and electricity sectors.

[7]Nonfinancial public sector, excluding Petrobras and Eletrobras, and consolidated with the Sovereign Wealth Fund. The definition includes treasury securities on the central bank's balance sheet, including those not used under repurchase agreements (repos). The national definition of general government gross debt includes the stock of Treasury securities used for monetary policy purposes by the central bank (those pledged as security in reverse repo operations). It excludes the rest of the government securities held by the central bank.

[8]See Annex 6 for details on the data.

[9]Nonfinancial public sector reported for primary balances (excluding statistical discrepancies); combined public sector including Ecopetrol and excluding Banco de la República's outstanding external debt reported for gross public debt.

[10]Public sector gross debt includes liabilities under advance oil sales, which are not treated as public debt in the authorities' definition. In late 2016, the authorities changed the definition of debt to a consolidated basis; both the historical and projection numbers are now presented on a consolidated basis.

[11]Gross debt is that of the nonfinancial public sector.

[12]The coverage of the fiscal data was changed from consolidated public sector to nonfinancial public sector with the October 2019 *World Economic Outlook*. Historical data were revised accordingly.

[13]Staff projections for Costa Rica were further updated in the context of the Third Extended Fund Facility Review mission. Central government only. As of January 2021, the central government definition has been expanded to include 51 public entities as per Law 9524. Data are adjusted back to 2019 for comparability.

[14]Central government for primary expenditure and primary balance; gross debt is presented on a consolidated basis.

[15]Central government only.

[16]Ratios to GDP are based on the 2007-base GDP series. Fiscal data cover the nonfinancial public sector excluding the Panama Canal Authority.

[17]Overall and primary balances cover budgetary central government. Gross debt covers central government debt, central government guaranteed debt, and arrears.

[18]Central government for primary expenditure and primary balance; public sector for gross debt. For Jamaica, the public debt includes central government, guaranteed, and PetroCaribe debt.

[19] For Haiti, estimates and projections reflect information available through early September 2022.

[20]Primary expenditures for Suriname exclude net lending.

[21]Eastern Caribbean Currency Union comprises Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines, as well as Anguilla and Montserrat (which are not IMF members).

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Country Groups and Country Abbreviations

Country Groups

Caribbean: Commodity Exporters	Caribbean: Other	Caribbean: Tourism Dependent	Central America, Panama, and the Dominican Republic (CAPDR)	Eastern Caribbean Currency Union (ECCU)	LA5	South America
Guyana	Guyana	Antigua and Barbuda	Costa Rica	Anguilla	Brazil	Argentina
Suriname	Haiti	Aruba	Dominican Republic	Antigua and Barbuda	Chile	Bolivia
Trinidad and Tobago	Suriname	The Bahamas	El Salvador	Dominica	Colombia	Brazil
	Trinidad and Tobago	Barbados	Guatemala	Grenada	Mexico	Chile
		Belize	Honduras	Montserrat	Peru	Colombia
		Dominica	Nicaragua	St. Kitts and Nevis		Ecuador
		Grenada	Panama	St. Lucia		Paraguay
		Jamaica		St. Vincent and the Grenadines		Peru
		St. Kitts and Nevis				Uruguay
		St. Lucia				Venezuela
		St. Vincent and the Grenadines				

List of Country Abbreviations

Antigua and Barbuda	ATG	Guyana	GUY
Argentina	ARG	Haiti	HTI
Aruba	ABW	Honduras	HND
The Bahamas	BHS	Jamaica	JAM
Barbados	BRB	Mexico	MEX
Belize	BLZ	Nicaragua	NIC
Bolivia	BOL	Panama	PAN
Brazil	BRA	Paraguay	PRY
Canada	CAN	Peru	PER
Chile	CHL	Puerto Rico	PRI
Colombia	COL	St. Kitts and Nevis	KNA
Costa Rica	CRI	St. Lucia	LCA
Dominica	DMA	St. Vincent and the Grenadines	VCT
Dominican Republic	DOM	Suriname	SUR
Ecuador	ECU	Trinidad and Tobago	TTO
El Salvador	SLV	United States	USA
Grenada	GRD	Uruguay	URY
Guatemala	GTM	Venezuela	VEN