From Infection to Inflation:
GLOBAL CRISES HIT HARD POOR AND VULNERABLE HOUSEHOLDS IN LATIN AMERICA AND THE CARIBBEAN
From Infection to Inflation: GLOBAL CRISES HIT HARD POOR AND VULNERABLE HOUSEHOLDS IN LATIN AMERICA AND THE CARIBBEAN

LAC Team for Statistical Development:
Regional Poverty and Inequality Update
Poverty & Equity Global Practice
ACKNOWLEDGMENTS

This report was produced by the Poverty and Equity Global Practice in the Latin America and Caribbean Region of the World Bank. The core team was led by Sergio Olivieri and consisted of Ivan Gachet, Diana Sanchez Castro, Jaime Fernandez, Kelly Montoya, Karen Barreto Herrera, Cicero Braga, and Hernan Winkler. Oliver Balch edited and enriched the document, Pamela Gunio and Ana Carolina Leguizamo provided outstanding administrative assistance. The team worked under the supervision and guidance of Ximena Del Carpio (previous Practice Manager, ELCPV) and Carlos Rodriguez-Castelan (current Practice Manager, ELCPV).

The team would like to thank the peer reviewers, Nandini Krishnan (Lead Economist, GPV03), Christoph Lakner (Program Manager, DECIS), and Marcela Melendez (Senior Advisor, LCRCE) for their comments and David Sislen (Practice Manager, SLCUR), Maria Gonzalez (Program Manager, SLCSO) and Hugo Nopo (Senior Economist, ELCPV) for their remarks. The document also benefited from country-specific inputs received from: Maria Davalos, Alejandro De la Fuente, Jacobus Joost De Hoop, Roy Katayama, Gabriel Lara Ibarra, Monica Robayo, Lourdes Rodriguez Charnussy, Gustavo Canavire, Javier Romero, Luciana De la Flor Giuffra, Vincenzo Di Maro, Carolina Mejia-Mantilla, Eliana Rubiano, Trinidad Saavedra Facusse, Mariel Siravegna, Agustin Arakaki, Ricardo Campante, Kiyomi Cadena, Christian Gomez Canon, Juan Manuel Monroy, Ana Rivadeneira, Fabio Sala Cereda, Diego Tuzman, Erika Schutt, Angela Lopez, Sofia Hidalgo, Silvia Granados, Luigi Butron, Constanza Vergara, Leah Arabella, and Luis Flores.

The findings, interpretations, and conclusions expressed in this work do not necessarily reflect the World Bank’s views, its Board of Executive Directors, or the governments they represent. The World Bank does not guarantee the accuracy of the data included in this work. Nothing herein shall constitute or be considered a limitation upon or waiver of the privileges and immunities of the World Bank, all of which are specifically reserved.

The numbers presented in this brief are based on two regional data harmonization efforts known as the Socio-Economic Database for Latin America and the Caribbean (SEDLAC) and the Labor Database for Latin America and the Caribbean (LABLAC), joint efforts of the World Bank and the Center of Distributive, Labor and Social Studies (CEDLAS) at the National University of La Plata in Argentina. They increase the cross-country comparability of selected findings from official household and labor surveys. For that reason, the numbers discussed here may be different from official statistics reported by governments and national offices of statistics. Such differences should not be interpreted in any way as a claim of methodological superiority because both sets of numbers serve the same important objectives: regional comparability and the best possible representation of the facts of individual countries. The welfare aggregate used in this study is income based.
EXECUTIVE SUMMARY

Latin America and the Caribbean (LAC) have faced extraordinary challenges over the last three years that reverted the social gains of the previous two decades. The Covid-19 pandemic, sluggish economic growth, fiscal constraints and increased debt stress, inflationary pressures, and the collateral effects of the Russian invasion of Ukraine have taken a toll on the region. These shocks have hit poor and vulnerable populations the most, increasing poverty and inequality; and moving millions out of the middle class. Yet, the region has been relatively resilient in recovering from these crises, albeit in uneven fashion. By the end of 2022, the labor markets had improved, poverty had receded, and the middle class had recovered, despite economic growth fluctuations and political instability across the region. Still, the LAC region has not completely regained its pre-pandemic socio-economic conditions in many countries and a closer look at the distributional impacts over these years could help identify opportunities.

The COVID-19 pandemic resulted in severe health impacts and a reversal in many of its socio-economic gains. The region’s gross domestic product (GDP) contracted by 6.4 percent in 2020, causing hardships for all but the richest households and increasing inequality. The socio-economic impact of the pandemic came on the back of several years of sluggish economic growth, which had weakened the capacity of the region's governments to react. Low-skilled workers, women, and those working in the informal economy were most affected by the economic shock of COVID-19; almost one in ten (8.3%) working adults lost their jobs. During the pandemic, around 19 million people fell back into poverty, mostly in urban areas. The living conditions of poor populations also deteriorated, with Peru posting a particularly sharp widening of its poverty gap. The rise in poverty came despite impressive government efforts to cushion COVID-19's negative impacts on people’s livelihoods. The one notable exception in this regard is Brazil, where a successful cash transfer program compensated for almost all the income losses experienced by poor households. A rare upside of the pandemic was the increase in internet use, which was seen most strongly in respect of digital banking. This shift in behavior helped foster financial inclusion, although internet access remains far from universal or evenly spread.

The unprecedented disruption to education and health during the COVID-19 pandemic will leave lasting scars on human capital accumulation and the welfare of an entire LAC generation. During the pandemic, children across the region encountered severe disruptions to their learning, with more than 75 percent of their total instruction time lost due to school closures. Parents and governments both tried to provide alternative schooling opportunities, but learning losses remained severe, especially for children in poor households. In addition, a rise in food shortages impacted many children’s physical and cognitive development, with levels of child stunting expected to rise as a result. The combined effect of these twin educational and health shocks is likely to be a reduction in future labor incomes for today’s school-age cohort. In 2045, they are projected to be earning 6.4 percent less than they would have earned were it not for the pandemic only due to learning losses. This income reduction will result in an estimated increase in poverty rates of around 1.7 percentage points, equivalent to five million more people falling into poverty than would otherwise be the case.
A year after the onset of COVID-19, the region is bouncing back, yet not sufficiently fast to put the worst effects of the pandemic behind it. A combination of uneven access to vaccines, sporadic containment measures, and an enfeebled labor market has stopped welfare standards from returning to their pre-pandemic levels. By 2021, a proportion of the nine million jobs lost during the pandemic had been regained, but employment levels remain 3.1 percentage points below the immediate pre-pandemic period. Furthermore, many of these regained jobs are of a lower quality than before. Most notably, levels of self-employment and informality have grown, while formal labor has seen a shift away from secure employment in large firms to insecure work in small firms. In the long term, this may well result in negative effects on the region's productivity, as well as on labor demand. More immediately, households are experiencing an ongoing deterioration of their welfare standards. Fiscal constraints have reduced 'governments' capacity for public transfers (which helped mitigate some of the pandemic's worst effects, especially in Brazil), while private remittances have also fallen. As a result, many poor households are struggling to meet their basic needs. Even though poverty was reduced in 2021, around ten million additional people remained impoverished. Moreover, the pandemic eroded their financial assets, leaving them less able to cope with shocks in the future. This situation contrasts with the experience of the richest quintile, who have bounced back quickly, enlarging the region's already sizeable economic divide.

The knock-on effects of global events have stymied LAC's recovery in the early stages of the post-pandemic period. Russia's invasion of Ukraine in early 2022 and its impact on international fuel and food prices have caused average inflation in the region to reach 8.9 percent (excluding Argentina). This sharp rise in prices is hampering households' purchasing power and causing employment quality (but not quantity) to remain below previously projected levels. Poor households are especially vulnerable in light of their experience of food insecurity and reduced savings during the pandemic. While some benefit has come to net food-producer households from higher commodity prices, this has been offset (in part or in total) by higher input costs, notably fertilizers. At the same time, LAC countries have limited fiscal room for additional social programs. Poverty levels are subsequently forecast to hit 31.0 percent in 2022 (excluding Brazil), a rise of 1.3 percentage points on 2019 levels (equivalent to around eight million individuals). Inequality is also expected to grow, with a projected half-point rise in the Gini coefficient compared to the period prior to the Ukraine conflict.

The weak economic outlook for 2023 will slightly improve employment and labor incomes, but poverty will remain above pre-pandemic levels. On average, employment in LAC is likely to be 0.9 percent above total employment in 2019, representing a creation of about 1.5 million jobs across the region. This job creation will be accompanied by lower quality, leaving many workers exposed to higher levels of vulnerability and income shocks. Moreover, average labor income would increase slightly (0.3 percent), which is not enough to reach pre-pandemic levels (i.e., 3 percent below its pre-pandemic levels). Excluding Brazil, poverty rates at US$6.85 a day (2017 PPP) are expected to reduce 0.2 percentage points, lifting 300,000 individuals out of poverty in 2023. Considering Brazil, poverty rates are also expected to decline from 28.6 percent in 2022 to 28.3 percent in 2023. Yet, poverty levels will remain above pre-pandemic levels (1.1 percentage points excluding Brazil and 0.1 percentage points including Brazil). A slight recovery in the middle class is also expected in 2023, but total numbers still below pre-pandemic levels. Excluding Brazil, the middle class will mildly increase from 34.3 percent in 2022 to 34.5 in 2023, 1.5 percentage points below pre-pandemic levels. Yet, including Brazil, the middle class is expected to decrease by 0.1 percentage points from 37.1 percent in 2022 to 37.0 percent in 2023, with about one million people falling out of this population segment.
Despite the challenges ahead, the LAC region has the potential to overcome them in its traditional areas of comparative advantage and the opportunities arising from resilient green growth. As shown in the report *The Promise of Integration: Opportunities in a Changing Global Economy*, the region needs to complement long-term structural reforms to reduce systemic risk, raise the level and quality of education, invest in infrastructure, and ensure well-functioning financial markets with a comprehensive approach to integrate the region into the global economy, particularly the US and European markets. In addition, it needs to take advantage of its comparative advantage in the green economy. The transition to the green economy could be an opportunity to improve well-being in the region by creating new quality jobs, enhancing labor incomes, and contributing to poverty reduction. However, this transition will demand a significant change to labor markets in LAC countries. This change will create new jobs but at the same time it could potentially destroy jobs and displace workers in many sectors. This process will require investment in human capital for the training and reskilling of workers. It will also demand well-designed social programs to protect the most vulnerable during the transition (e.g., active labor market programs), as well as incentives for informal workers to shift to new productive firms involved in green technologies.