BRICS

RUSSIA | 2020

BRICS Economic Bulletin

By the CRA Research Group

CONTENTS

FOREWORD

Almost 20 years have passed since the BRIC acronym was first used in economic discussions, and 10 years have passed since BRICS has become a formal grouping in its current form. Throughout these years, the BRICS countries have been developing their partnership in several areas, and the cooperation on macroeconomic and financial issues has become one of its key elements.

At the Sixth BRICS Summit in Fortaleza in 2014 the BRICS countries established the New Development Bank, aimed at financing infrastructure and sustainable development projects in BRICS and other emerging and developing economies. At the same Summit, the BRICS countries signed the Contingent Reserve Arrangement (CRA), a currency swap mechanism intended to cushion the effects of short-term pressures on countries' balance of payments.

In order to support the decisions of the BRICS CRA administrative bodies, two years later, in 2016, the countries established the System of Exchange of Macroeconomic Information (SEMI) and the CRA Research Group – a network of economists from all five central banks, who exchange macroeconomic statistics, discuss the latest macroeconomic developments in each country and share their views on topical issues of the international financial agenda on a quarterly basis. Since 2018, the results of those expert discussions are formalized in the Economic Notes, published quarterly and available to the members of the CRA Research Group and the CRA administrative bodies.

The research and analytical potential of the CRA Research Group has not been fully realized yet. This year, we present the next step in the BRICS countries' analytical work – the first issue of the BRICS Economic Bulletin. We hope that the preparation of such a document would become an annual activity of the CRA Research Group and that, over time, the document will evolve into a regular framework for comprehensive analysis of economic vulnerabilities. While the overall focus of the Bulletin is on balance of payments, the precise theme of the Bulletin may change from year to year, depending on the macroeconomic developments in the BRICS and globally.

The 2020 is a year of COVID-19 – a black swan, which brought about significant changes for the economies all over the world. "This time really is different", said Carmen Reinhart and Kenneth Rogoff when *discussing* the COVID-19 crisis, alluding to their well-known book on the history of several economic meltdowns. Indeed, unlike to previous events, the current crisis did not originate in the economy itself, but was the result of an unprecedented health-related emergency, requiring urgent measures to protect the people from a deadly contagion.

We therefore decided to focus the first issue of the Bulletin on this topic. At the start of 2020, our economies were generally well equipped to grow above 2019 levels. But the massive decline in economic activity due to mobility restrictions, which were introduced all over the world to stem the spread of the virus and to reduce the strain on the national healthcare systems, induced a combination of shocks in our economies, dragging them down and making the goals for the GDP growth, set at the beginning of the year, unachievable. Central banks' and national governments' prompt and decisive actions, providing support to businesses and households, helped to dampen the adverse effects of the pandemic, but only to some extent.

At the same time, the downturn has not created any substantial balance of payments pressures in the BRICS countries. In some cases, the crisis has even helped to improve the current account balances – due to lower imports, most notably in services, as travel and tourism came to an almost complete halt once countries introduced the restrictions.

Only two months are left until the end of 2020, but we keep on facing new turns in the story of this pandemic. The signs of optimism and indications of a possible quick recovery, which were identified by the beginning of the third quarter, are no longer consistent with the rising number of new cases and restrictions being re-introduced around the world. The effectiveness of the existing treatments and vaccines being developed is still under question, implying that the pandemic is not going to go away any time soon. The longer the pandemic lasts, the worse are the scarring effects on all our economies, and the longer will be the road back to normalcy and previous growth trajectories.

While the impact of the outbreak can only be fully evaluated in the years to come, the analysis below reflects on the developments in our economies in the first two quarters of 2020. We also present proposals on how to enhance our cooperation further.

This first issue of the Bulletin would not have seen the light of the day without contributions and inputs by Eduardo Urbanski from the BCB, Mohua Roy, Smita Sharma and Ajesh Palayi from the RBI, Shilei Fan from the PBC and Linda Motsumi and Piet Swart from the SARB, as well as many other colleagues, who revised the document at various stages and provided useful comments and edits.

Zhanna Smirnova,
Chair of the CRA Research Group in 2020,
Senior Economist, Bank of Russia

I. RECENT DEVELOPMENTS: ALREADY WEAK GROWTH FACED UNPRECEDENTED CHALLENGE

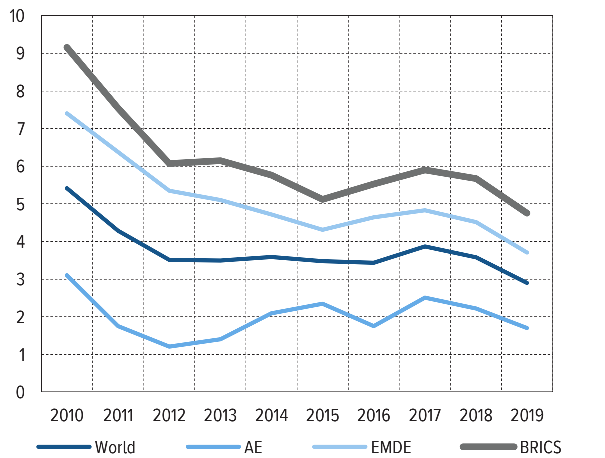
Pre-COVID Conditions

The last year of the 2010s was full of challenges, which weighed down the pace of global growth. According to the *the International Monetary Fund (IMF)*, after an expansion of 3.9% in 2017 and minor slowdown to 3.6% in 2018, the global economy plunged into a decelerated growth rate of 2.9% in 2019, which was the lowest growth reading since the Global Financial Crisis (GFC) of 2008-2009. Despite a notable shift towards accommodative monetary policy in the advanced economies at the beginning of 2019, and the subsequent improvement in financial markets, global uncertainty remained elevated throughout the year due to ongoing trade disputes and geopolitical tensions. Firms were cutting back their spending on capital goods, and supply chains experienced disruptions, which altogether significantly affected trade across the globe. According to *the World Trade Organization (WTO)*, the volume of merchandise trade was down by 0.1% in 2019, after a rise by 2.9% in 2018; the dollar value of merchandise trade fell by 3% in 2019, after a rise by 10% in 2018.

BRICS economies, despite altogether growing faster than the wider group of emerging market and developing economies (EMDEs), were also following the downward trend. Growth rates in all BRICS countries in 2019 was lower than in 2017, even though in 2018 the picture was more varied – in 2018, China's growth slowed down only by a minor 0.1 percentage points, Brazil kept the same growth rate as the year before, Russia added 0.7 percentage points to the previous year's number, while India[1] and South Africa were decelerating. Overall, the BRICS slowdown in 2017-2019 was a result of not only global, but also idiosyncratic factors, including accumulated structural weaknesses (such as decelerating productivity growth, large regulatory burden on businesses, inefficient public spending, and the huge role of state-owned enterprises in the economies).

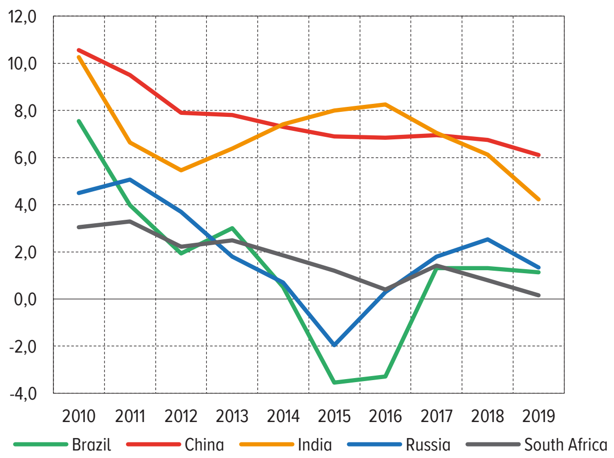
On **the demand side**, household consumption played a substantial role in supporting growth in all BRICS countries, with government consumption providing additional visible support in Russia, India, and South Africa. Gross capital formation expanded strongly in Brazil and South Africa and only moderately in Russia and China, while contracting in India.

BRICS WEIGHTED GROWTH IN THE PAST 10 YEARS FOLLOWED GLOBAL TRENDS *Chart 1*
IN PERCENT, YEAR-ON-YEAR



Source: IMF, CRA Research Group

INDIVIDUAL BRICS ECONOMIES HAD THEIR UPS AND DOWNS OVER THE PAST 10 YEARS *Chart 2*
IN PERCENT, YEAR-ON-YEAR



Source: IMF

[1] *For India here and below, if not specified otherwise, data for 2019 refers to the fiscal year 2019-2020 (April 2019-March 2020).*

On **the supply side**, the services sector (especially, trade and ICT-related services) was driving growth in all BRICS countries, with the industry lagging behind (specifically, industrial production). Mining industries were down in Brazil and South Africa, while growing moderately in Russia.[2] Agriculture was showing mixed dynamics – it was on the rise in Brazil and India, but contracted in South Africa.

Inflationary pressures in BRICS countries remained generally well-contained in 2019, with lower metal and energy prices playing a moderate role. At the same time, in India and China, inflation accelerated substantially by the end of 2019 due to a rise in food prices, with the reading in India breaching the target range. Inflation in Brazil increased slightly by the end of the year, remaining within the target range. In South Africa, after an accelerating in the first half of the year, inflation went back closer to the lower end of the target band. In Russia, inflation was decelerating for most of the year, falling slightly below the target by the end of the year.

BRICS external positions remained generally solid in 2019, backed by healthy levels of foreign exchange reserves and relatively low dependence on external financing.

Real effective exchange rates.[3] In 2019 REER depreciated in Brazil and South Africa by 1.8% and 3.2% relative to the countries' respective average figures for 2018, whereas in Russia and India, REER appreciated by 3.6 and 2.1%, respectively. In China, REER remained almost unchanged, depreciating by a minor 0.4% compared to its 2018 average.

Current account balances. Current account deficit in India and South Africa narrowed in 2019 compared to 2018, as lower oil prices and deceleration of domestic demand in both countries led to lower imports, improving the trade balances. In India, additional support to current account was provided by remittances. For South Africa, the continued global demand for gold assisted the trade balance, while lower gross dividend payments decreased the income deficit. In contrast, in Brazil, the current account deficit has widened, influenced by a larger decline in exports vis-à-vis imports. This decline in exports reflected a reduction in external demand.

Lower oil prices were the main reason behind the substantial narrowing of the current account surplus in Russia, and at the same time, one of the reasons for the widening of current account surplus in China. Current account surplus in China also reflected lower deficit in services.

The financing of current account deficits in Brazil, India and South Africa was overall in line with trends in previous years. In South Africa, most of the current account deficit in 2019 was financed by portfolio flows, while in Brazil net FDI more than fully covered the current account financing needs. In India, the current account deficit was financed by a combination of FDI, portfolio and other investments, with FDI financing the major amount.

Financial and Capital Account (excluding reserve assets). In Russia, India, China and South Africa, inflows were recorded in both net FDI and portfolio investments. In Russia, the inflows arrived after outflows in 2018 on both FDI and portfolio investments. In India, the portfolio flows reversed to inflows after outflows in 2018. In Brazil, while the inflow in FDI continued in 2019, net portfolio investments experienced outflows.

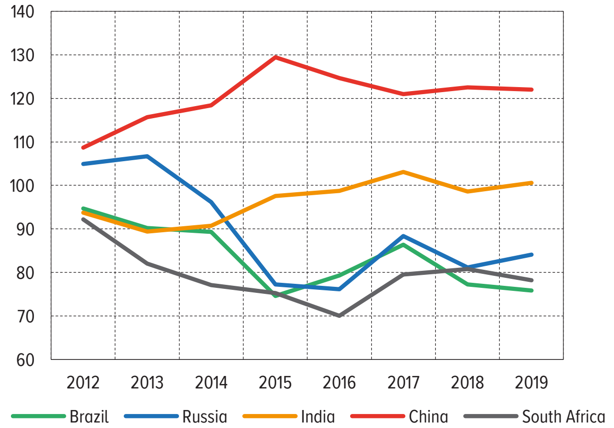
Reserve assets. Reserve accumulation trends have diverged, with Brazil using a small portion of its FX reserves to address excess volatility and liquidity shortages in the last quarter of 2019, while India and Russia were building up volumes throughout 2019. Russia's reserves increase reflected the FX purchases under the fiscal rule[4], while India has been able to add to the reserves on the back of FDI flows and higher external commercial borrowings. Reserves in South Africa also expanded, but the increase was largely stemmed from the proceeds from international bonds issued by the South African government. Finally, mild increase in China's reserve assets mainly reflected valuation effects.

[2] *Details are provided in the CRA Economic Note Q4, as well as in country reports, outlined in the References section.*

[3] *For consistency purposes, the BIS Broad indices database was used to evaluate REER dynamics.*

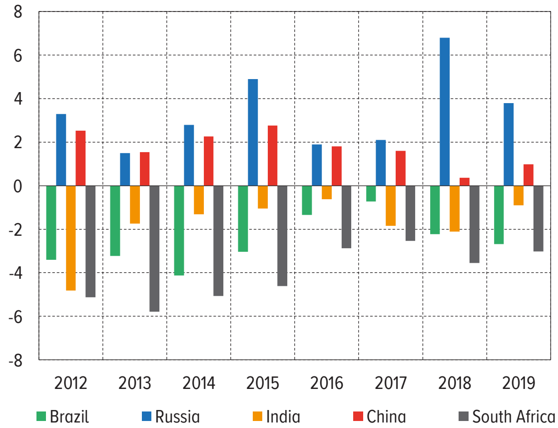
[4] *The fiscal rule was introduced in Russia at the beginning of 2017 to dampen the exchange rate volatility, induced by oil prices. According to the rule, the Ministry of Finance determines the volume of FX purchases/ sales, based on the current oil price, while the Bank of Russia conducts these operations on the market.*

REAL EFFECTIVE EXCHANGE RATE *Chart 3*
IN PERCENT, YEAR-ON-YEAR
REAL EFFECTIVE EXCHANGE RATE INDEX CHANGE, YEAR AVERAGE, 2010=100



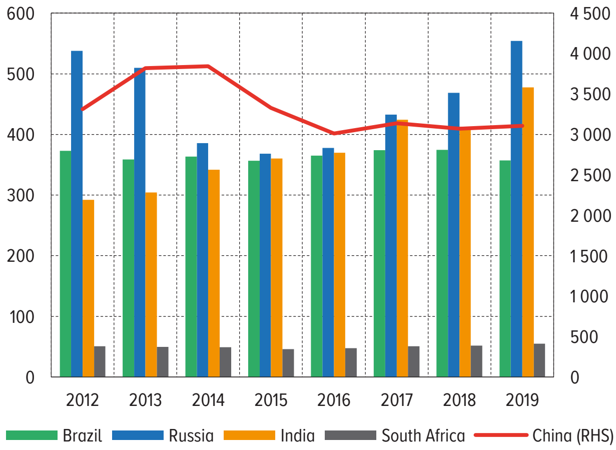
Source: Bank for International Settlements.

CURRENT ACCOUNT BALANCE *Chart 4*
IN PERCENT OF GDP



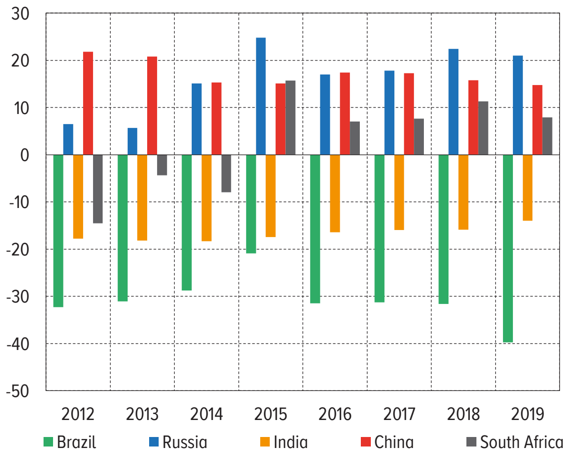
Source: CRA Research Group.

RESERVES ASSETS *Chart 5*
IN USD BILLION



Source: CRA Research Group.

NET INTERNATIONAL INVESTMENT POSITION *Chart 6*
IN PERCENT OF GDP



Source: CRA Research Group.

Net International Investment Position. NIIP declined substantially in Brazil, from (-33%) of GDP in 2018 to (-40%) of GDP in 2019, and in South Africa, from 13% to 9% of GDP, as liabilities expanded in both countries, while assets expanded less than liabilities in Brazil and declined in South Africa. In Russia and China, NIIP ratio to GDP in 2019 declined by 1% of GDP, to 21% and 14% of GDP respectively. In India, the ratio of NIIP to GDP in 2019 improved to (-14%) from (-16%) in the previous year.

Despite the slowdown during the year, the outlook for BRICS in 2020 was moderately optimistic at the end of 2019, as trade tensions had reduced, fears of a disorderly Brexit outcome had faded, and the world economy was cautiously expecting to embark on the path to recovery. In January 2020, the *IMF* expected almost all BRICS countries to grow faster than they did in 2019, with only China moderating by a 0.1 percentage point compared to 2019 numbers.

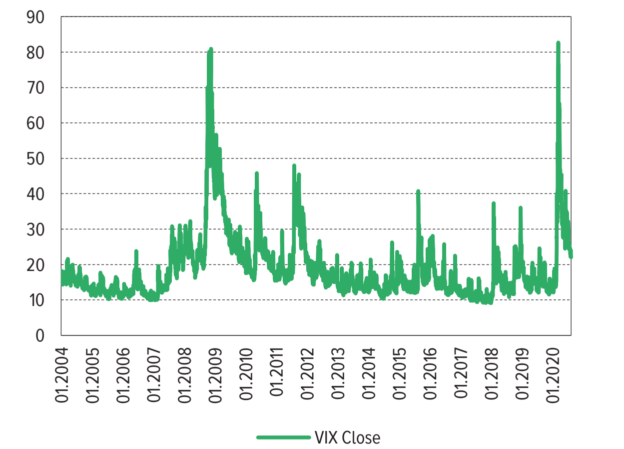
The key global risks to the BRICS growth identified at that time were similar to the factors which affected the economies in 2019 – possible escalation of trade and geopolitical tensions, a no-deal Brexit, followed by increases in policy uncertainty, deterioration of financial market sentiments, and tightening financial conditions. The coronavirus was only mentioned as a minor factor, and overall, the start of the 2020 calendar year was perceived as quite smooth, with risks and their mitigation strategies if not yet certain, but at least broadly visible.

COVID-19: Black Swan Has Landed

On the last day of 2019, the novel coronavirus, COVID-19, was identified officially. It was not considered to be a global threat until March 11, 2020, when *the World Health Organization (WHO)* characterized the outbreak as a pandemic. The coronavirus spread rapidly around the world, raising uncertainty and volatility to nearly unprecedented heights: equity markets recorded sharp sell-offs, demand for safe-haven assets surged, EMDEs sovereign bond yields widened and risk spreads jumped, leading to severe tightening of global financial conditions.

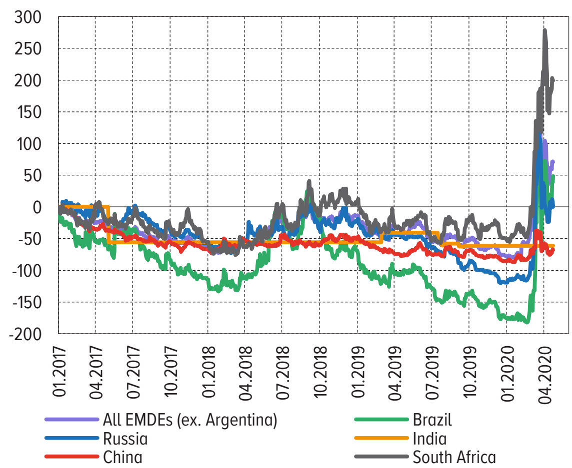
The pandemic and related containment measures, especially pertaining to in the aviation and the automotive industry, which account for about 60% of oil consumption, caused a collapse in demand for oil, driving volatility indices further up. The energy market experienced one of the biggest price shocks since 1973. Oil prices dipped below USD 20 per barrel (all grades), losing nearly 70% in value, with some benchmarks becoming negative, while the storage capacity was approaching its limits. The *International Energy Agency (IEA)* was projecting the oil demand to fall by a historically unprecedented 9.3 million barrels per day[5] in 2020 from the level of 100 million barrels in 2019.

VOLATILITY SPIKED TO THE LEVELS HIGHER THAN IN 2008 *Chart 7*
POINTS



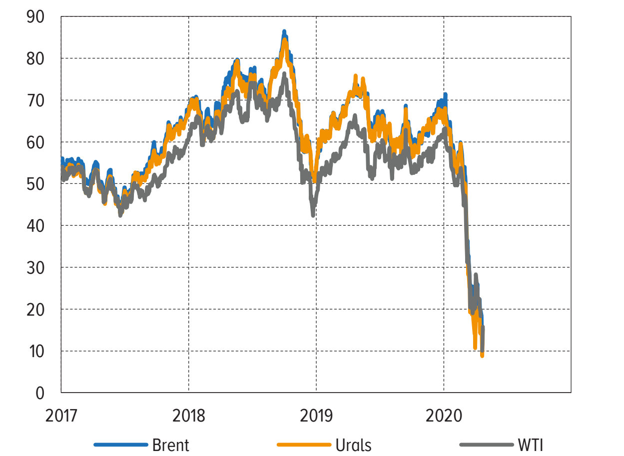
Source: Chicago Board Options Exchange.

BRICS CDS ROCKETED *Chart 8*
CHANGE TO 02.01.2017, BASIS POINTS



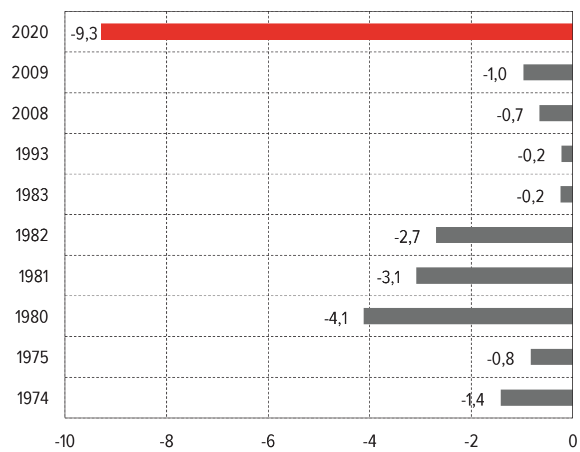
Source: Reuters.

OIL PRICES DIPPED BELOW USD 20 *Chart 9*
PRICE PER BARREL, US DOLLARS



Sources: Thomson Reuters, Bloomberg.

DROP IN OIL DEMAND IS HISTORICAL* *Chart 10*
PERCENTAGE CHANGE, YEAR-ON-YEAR

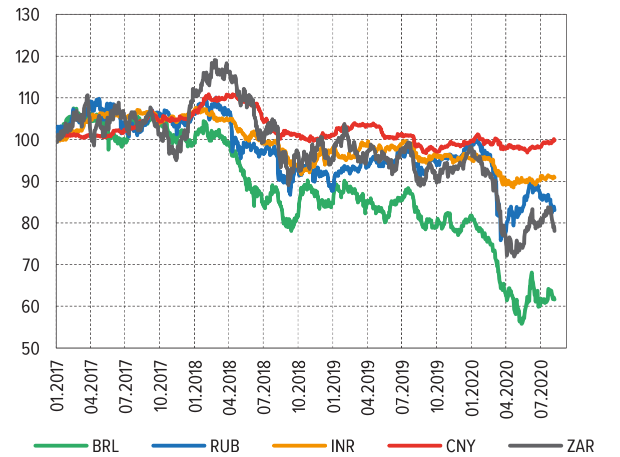


** Data for 2020 is based on IEA estimates.*
Source: IEA, the World Bank.

[5] *In August 2020, the IEA slightly raised the forecast to 8.1 bbl/day.*

BRICS EXCHANGE RATES VS US DOLLAR *Chart 11*

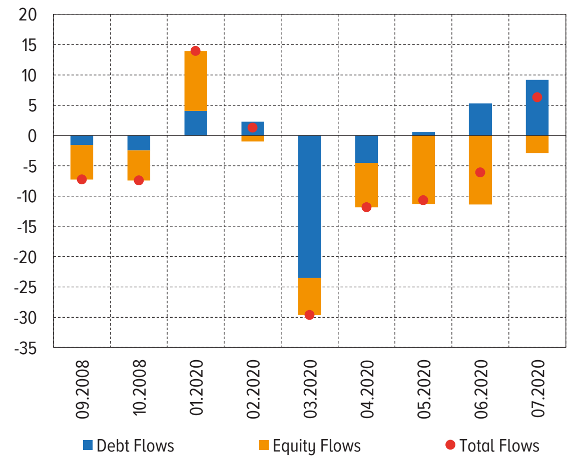
100 = 02.01.2017



Source: Bloomberg.

CAPITAL FLOWS TO BRICS REVERSED *Chart 12*

BILLION US DOLLARS, BRICS TOTAL



Source: Emerging Portfolio Fund Research.

Despite substantial inflows to BRICS in the first half of Q1 2020, the increased risk aversion among global investors led to massive capital outflows at the end of Q1 which continued in the beginning of Q2 2020. Available high-frequency data on portfolio flows indicate that outflows exceeded those during the early stages of the GFC in US dollar terms. The speed of reversal was also exceptional, posing challenges for countries with large external financing needs.

BRICS currencies subsequently depreciated, although with substantial variation across economies. The currencies of commodity exporters with flexible exchange rates, including Brazil, Russia, and South Africa, fell in value especially sharply, reflecting the movements in commodities markets. The US dollar liquidity deficit in mid-March added to the deceleration dynamics of EMDEs' currencies.

BRICS governments and central banks swiftly and decisively reacted to the rise in market volatility and emerging risks to the economy, brought about by the continuing spread of the virus. The measures, undertaken by governments and monetary authorities, were unprecedented both in numbers and in volume. Their composition and structure were also historically unique.[6]

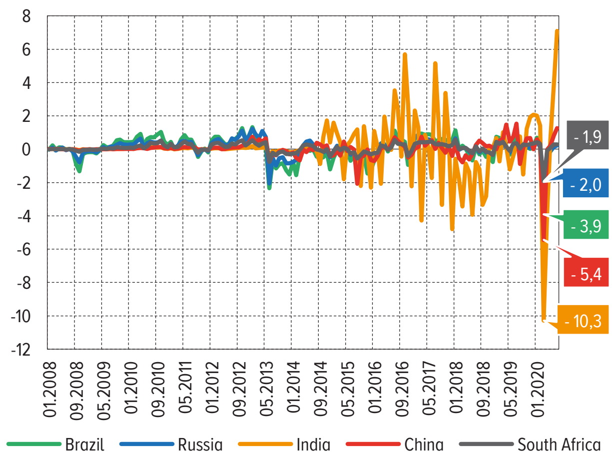
Briefly, measures, undertaken by **fiscal authorities** and general governments included, though not were limited to, employment support, tax deferrals and cancellations, spending on medical equipment and new hospitals, transfers to households and firms as a temporary replacement of lost income, and loan guarantees for SMEs and most affected industries. According to the IMF, the total fiscal response in the BRICS countries may be estimated to be split almost evenly between compensation of foregone revenues and provision of guarantees.

Policy responses from **central banks** were aimed at easing short-term funding strains, providing liquidity, and restoring the normal functioning of markets, and included policy rate cuts, expansion or implementation of asset purchase programmes, expansion of liquidity-providing operations, reduction of regulatory requirements (countercyclical capital buffers, capital and provisions and reserve requirements), as well as lending support (concessional lending to banks to increase lending to particular industries or market segments).

Central banks of reserve currency countries provided additional support to markets. In particular, in response to the stress in the offshore US dollar market, the US Federal Reserve extended the US dollar swap lines to foreign central banks (among the BRICS countries, the Central Bank of Brazil established an up to USD 60 billion swap line with the US Fed).

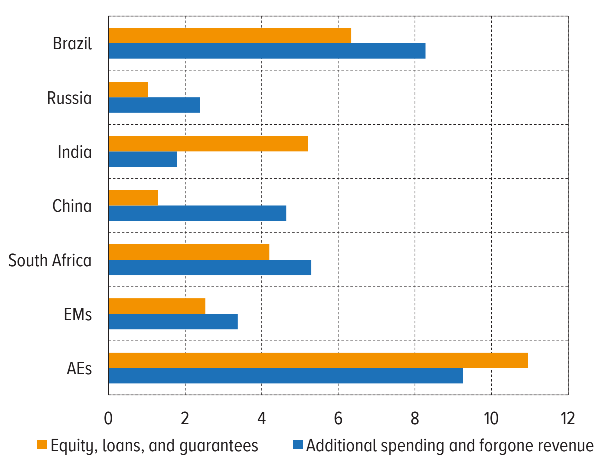
[6] *Information on the various measures can be found at the websites of the IMF (focus on fiscal measures), the OECD (broad set of measures, including non-financial), the WTO (trade and trade-related measures), KPMG (with focus on tax measures), and Institute for International Finance (with focus on international financial organizations response), among others.*

DEBT OUTFLOWS EXCEEDED HISTORICAL RECORDS *Chart 13*
IN MILLION US DOLLARS



Source: Emerging Portfolio Fund Research.

BRICS FISCAL POLICY RESPONSE *Chart 14*
IN PERCENT OF GDP



Source: IMF Fiscal Monitor Database, October 2020.

The BRICS central banks' policy responses are summarized in the table below, with more details provided in the Boxes section of the Bulletin.

Exceptional monetary and fiscal policy support helped to improve risk sentiment. Equity prices started to recover their losses, credit spreads narrowed, global financial conditions eased and volatility declined substantially, though staying above the "pre-COVID" levels. Capital flows to BRICS have stabilized and currency shifts were at least partially unwound. Nevertheless, despite the upswing in markets, the deep structural shocks that caused by the COVID-19 outbreak, may not be entirely eliminated even by prompt and targeted policy actions, and could lead to long-lasting effects on the economies.

SUMMARY OF CENTRAL BANK AND PRUDENTIAL MEASURES IN THE BRICS COUNTRIES *Table 1*

Type of tool	Measures	Brazil*	Russia	India	China	South Africa
Interest rate	Policy rate cut	X	X	X	X	X
Lending/ liquidity	Gen. liquidity provision	X		X	X	X
	Specialised lending	X	X	X	X	
Asset purchases/ sales	Government bonds	X		X		X
	Commercial paper	X				
	Corporate bonds	X				
	Other private securities	X				
FX swap/ intervention	USD swap line	X				
	FX intervention	X		X		
Prudential rules and regulations	Capital requirements	X	X	X	X	X
	Liquidity requirements	X	X	X	X	X
	Payout restrictions	X	X	X		
	Market functioning	X	X	X	X	

** Before the crisis, the Central Bank of Brazil had the authorization to buy government bonds for monetary policy purposes. But in 2020, it was also authorized by the congress to purchase government bonds for financial stability purposes and to purchase private securities as well, but only while the calamity state is effective.*

II. ANALYSIS: GROWTH SEVERELY AFFECTED, WHILE BALANCE OF PAYMENTS HELD STEADY

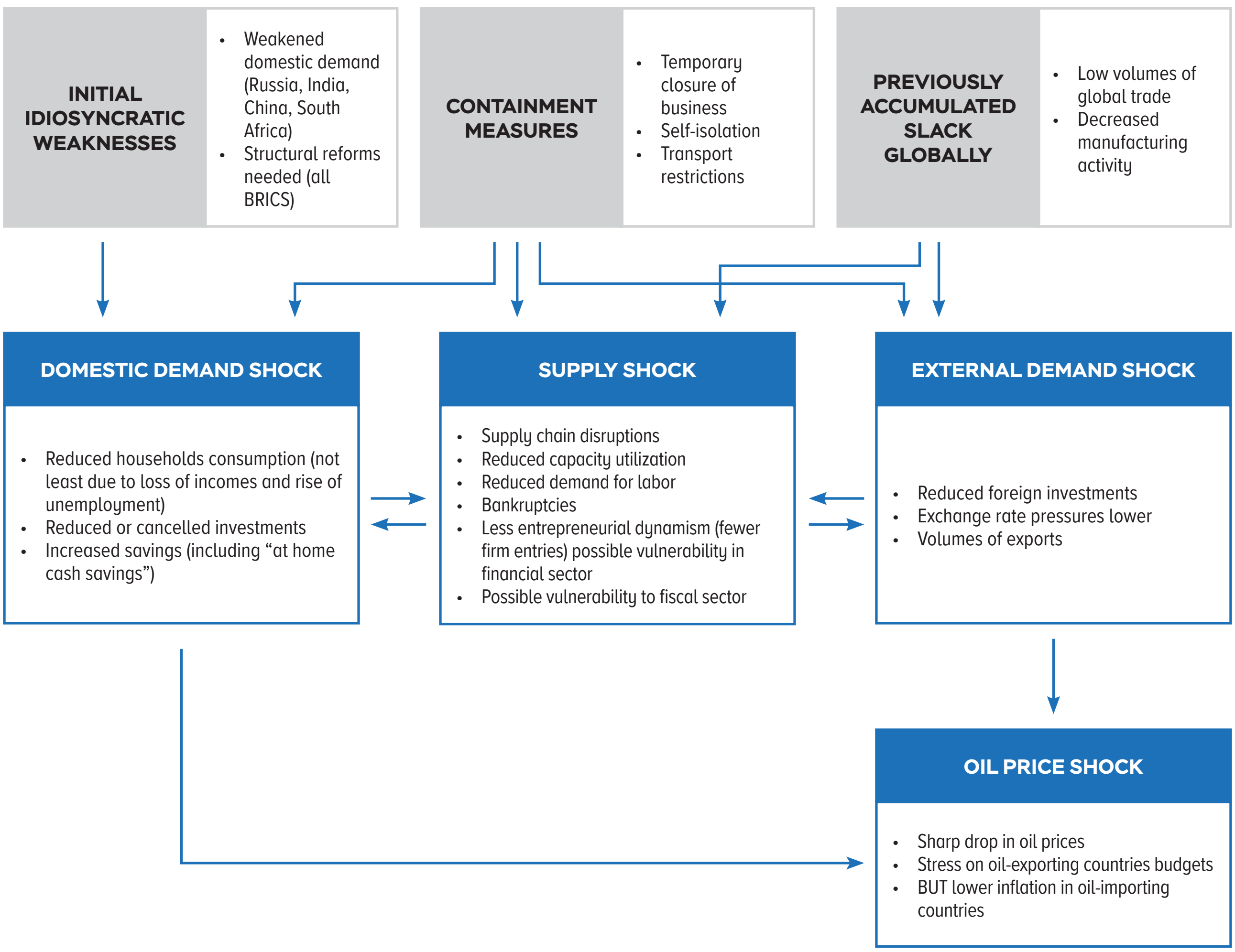
Economic Growth: What Was the Major Drag?

The COVID-19 outbreak and subsequent containment measures, which were implemented around the world to curb the spread of the virus, induced several shocks in the global and individual economies – domestic demand shock, external demand shock, supply shock, and oil price shock. These interconnected shocks, while being already severe on their own, exacerbated the already accumulated weaknesses.

Lockdowns led to closure of almost all businesses in the restricted areas, changing work routines and distorting normal consumer behavior, bringing on both domestic demand and supply shocks.

Value chain disruptions around the world, combined with domestic demand shocks led to a massive external demand shock. International trade, being already on a downward trend due to higher tariffs and uncertainty over trade policies in 2019, suffered further. In April, the *WTO* predicted that global trade would shrink by 13 to 32 percent in 2020 due to the pandemic. More recent projections indicate that the contraction may be close to 13-14 percent, but the number is still among the worst in history.

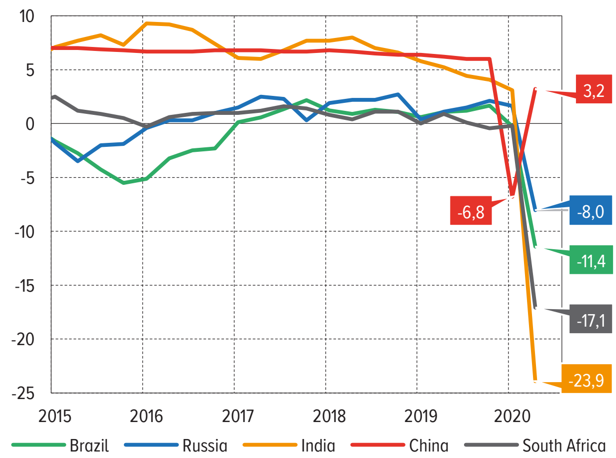
COVID-19 INDUCED MULTIPLE SHOCKS IN THE ECONOMIES *Chart 15*



Source: Compiled by the CRA Research Group.

BRICS GDP PLUNGED *Chart 16*

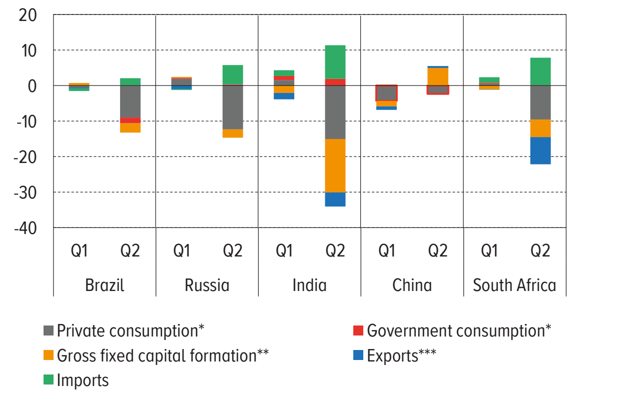
QUARTERLY, YEAR-ON-YEAR



Source: Bloomberg.

CONSUMPTION AND INVESTMENTS DROPPED *Chart 17*

QUARTERLY, YEAR-ON-YEAR, PERCENTAGE CHANGE



** For China Private consumption bar shows total consumption.*
*** For China Gross fixed capital formation bar shows Gross capital formation.*
**** For China Exports bar shows Net exports.*
Source: CRA Research Group.

BRICS economies reacted to the combination of these dramatic shocks with similarly deep contraction as in the rest of the world. Most BRICS countries entered national lockdowns late in Q1 2020, so the effects were most prominent in Q2 2020. In China, which faced the COVID-19 outbreak earlier than other countries, the hardest quarter was the Q1 2020, while in Q2 2020 the economy started to recover.

In the quarter before the outbreak, BRICS countries had been demonstrating mixed dynamics. While Russia, India and China continued to grow, though at a decelerated rate, Brazil and South Africa witnessed slightly negative growth rates. The losses in GDP growth, which the economies experienced due to the COVID-19 outbreak, were the worst in history for Brazil, India and China. Russia and South Africa showed the lowest readings since Q1-Q2 2009.

On the **demand side**[1], the biggest drop in all countries was recorded in household consumption. A general fear of contagion and containment measures established restricted buying practices, while unemployment, lost income and uncertainty about the future significantly constrained household expenditures. Spending on restaurants, hotels, and recreational facilities ground to an almost complete halt. In China retail purchases declined by 19.0%, in Brazil household consumption dropped by 13.5%, in Russia by 22.2%, in India by 26.7%, in South Africa by 15.7%. The household demand did not drop further only thanks to the extraordinary fiscal measures, which provided support to families and firms.

Investments also declined substantially on a combination of general slowdown in economic activity, considerable uncertainty and reduced opportunities to sell products on the market. Gross fixed capital formation declined by 15.2% in Brazil, by 11.7% in Russia, by 47.1% in India, by 16.1%, in China, and by 25.8% in South Africa.

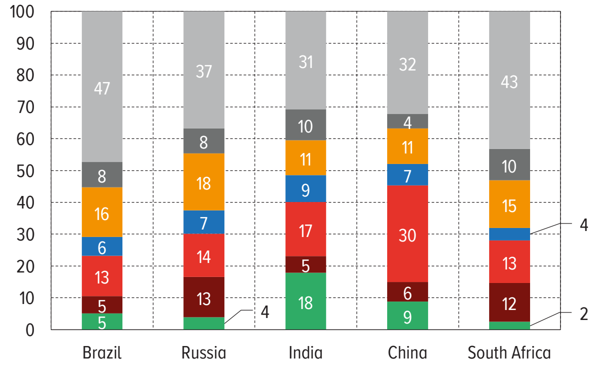
Subdued demand led to a decline in imports, which was the only supporting factor for growth in all countries.

On the **supply side**, almost all industries experienced a massive drop in output in the “pandemic” quarter. Travel, logistics, tourism, leisure, hospitality, off-line retail and labor-intensive manufacturing businesses have been severely impacted, other sectors – such as automotive industry and electronics – experienced supply chain disruptions. A relatively favorable impact could have been felt by pharmaceuticals, e-commerce, online entertainment, and insurance, but the share of those industries is too small to offset the losses in all other sectors.

A notable feature of the COVID-19 crisis is the sharp decline in the services sector, which drove the global growth in 2019 and kept labor markets buoyant and wages growth relatively healthy,

[1] *Here and below, if not mentioned specifically, the comparison refers to the quarter, the most affected by the pandemic in the country: Q1 2020 in China, and Q2 2020 in all other countries (sometimes called in the text as “pandemic” quarter). Numbers are given on a year-on-year, non-seasonally adjusted, constant prices basis. For India, calendar quarters are taken.*

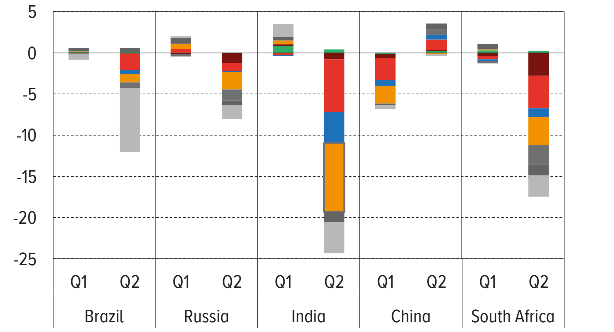
INDUSTRIES, PROVIDING MOST VALUE ADDED IN BRICS ECONOMIES, ... *Chart 18*
IN PERCENT OF GDP, AVERAGE 2010-2018



Other Activities
Transport, storage and communication
Trade, restaurants and hotels
Construction
Manufacturing
Mining, Utilities
Agriculture, hunting, forestry, fishing

Source: UN Statistics.

... WERE HIT THE HARDEST *Chart 19*
IN PERCENT, YEAR-ON-YEAR



Other components
Finance, real estate, business services
Transport, storage, communication*
Trade, restaurants, hotels*
Construction
Manufacturing
Mining, Utilities
Agriculture, hunting, forestry, fishing

** For India, "Transport, storage, communications" and "Trade, restaurants and hotels" are shown combined on a single bar.*
Source: CEIC.

and which constitutes a substantial share of the BRICS value added. Once the pandemic started, many people in the services sector lost their jobs and part of the sector came to a standstill. Transportation, trade and personal services were among the most affected industries.

Despite services being severely affected, the major contribution to decline in BRICS can be attributed to industrial activities, especially manufacturing, mining, utilities and construction. In Brazil, industries were down by 12.5%, while services declined by about 11%; in India, industries dropped by 33.8%, while services declined by 24.3%; in China, industries dropped by 8.4%, while services declined by 3.8%; in South Africa, industries dropped by 31.3%, while services declined by 11.8%. Only in Russia, did the services decline more than industries: a 9.2% decline in services vs a 8.0% decline in industries.

Agriculture was the only sector that holded firm in all BRICS countries, as it was mainly exempted from the lockdown restrictions, while increased home cooking supported domestic and even some external demand for agricultural products. In Brazil, Russia and China financial services also provided some support to growth.

The COVID-19 shocks also affected **inflation** dynamics in the BRICS economies. While at the early stage of the pandemic the disinflationary effects of the fall in demand and lower commodity prices were outweighing inflationary pressures from the supply disruptions, driving inflation down in all BRICS countries, by the end of Q2 2020, inflation started to pick up due to the combination of a rise in commodity prices, exchange rate depreciation and effects of supply disruptions. The most notable pick up was in India, where a rise in food prices has put additional pressures on the CPI dynamics. Nevertheless, despite an acceleration of the inflation rate at a later stage of the pandemic, it remained within the acceptable range in all BRICS countries, and would likely remain so until the end of 2020 due to substantial negative output gaps, caused by the COVID-19 combination of shocks.

Balance of Payments: Sailed Through the Storm Well?

On the eve of the pandemic, BRICS balance of payments had been following recent years' trends and did not have any major weaknesses. The shocks, induced by the pandemic, had an impact on both current and financial accounts of BRICS countries both in Q1 and Q2 2020. Presently, only partial assessment of their effect on balance of payments is feasible, while significant uncertainty remains.

BRICS' real exchange rates showed mixed dynamics. According to [the BIS database](), the real effective exchange rate index in Q1-Q2 2020 compared to the 2019 average was lower in Brazil (by

16%), in Russia (by 4%) and in South Africa (by 10%). At the same time, it was marginally higher in China (2%) and remained almost flat for India (0.2%).

Current Account

Among the BRICS countries, Brazil, India and South Africa have persistent current account deficits, which are justified by their demographic trends, development needs and favorable growth prospects. Russia and China have current account surpluses, though Russia has a non-oil current account deficit, and China's current account surplus had been excessive for some years. The pandemic has temporarily narrowed both current account deficits and surpluses.

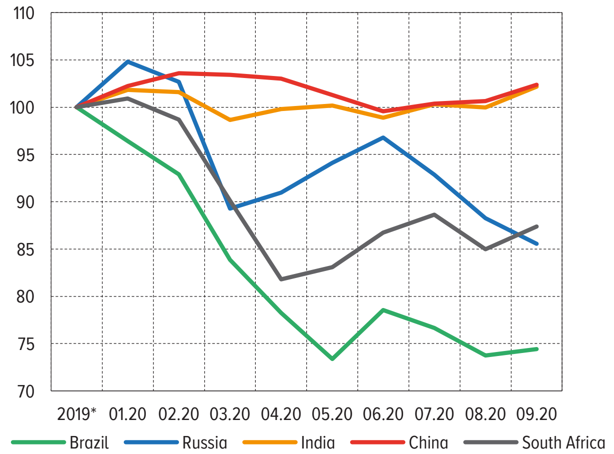
Suppressed demand and lower supply due to the disrupted value chains affected the countries' trade balances. The global volume of merchandise trade in the first half of 2020 was about 20% lower than in 2019, according to the *IMF*. As BRICS exports to each other is relatively small – with only Brazil reaching almost 30% – it can be concluded that BRICS trade balances depend a lot more on the trade with the rest of the world than on intra-group transactions, and, thus the effect of the external demand shock on current account balance could not be mitigated inside the group.

Trade balances in the "pandemic" quarter in most BRICS countries reflected the effects of production disruptions and lower demand associated with lost jobs and income. The most notable is the significant decline of imports of services due to the travel restrictions introduced around the world.

- In **Brazil**, after registering a current account deficit of -5.4%[2] of GDP in Q1 2020 (USD 19.6 billion), the balance has changed to a 1.8% surplus in Q2 2020 (USD 6.0 billion). This change reflected reductions in net expenditures in the services and primary income accounts, as well as an improvement in the trade balance. The deficit in the services account receded markedly, mainly due to a sharp reduction in net expenditures on tourism. Regarding the improvement in the primary income account, the crisis weighed on the profits of firms, which reduced their remittances. Finally, concerning the trade balance, the change was mainly due to a reduction of imports.

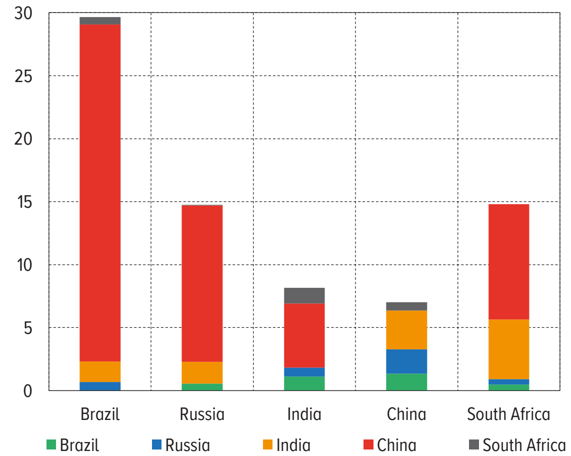
- In **Russia**, current account balance worsened in both Q1 and Q2 compared to the 2019 levels, reflecting lower oil prices and subdued external demand. The current account balance, after a surplus of 5.8 % of GDP (USD 22 billion) in Q1 2020, recorded a deficit of 0.2% of GDP (USD 0.5 billion) – for the first time since Q3 2017. Merchandise exports declined 14% in Q1 and

BRICS REAL EFFECTIVE EXCHANGE RATES NEGATIVELY AFFECTED BY THE PANDEMIC *Chart 20*
2019 AVERAGE = 100



Source: BIS, CRA Research Group.

BRICS DO NOT TRADE MUCH WITH EACH OTHER *Chart 21*
IN PERCENT TO TOTAL COUNTRY'S EXPORT



Source: World Bank, CRA Research Group

[2] *For all countries, numbers are calculated on a quarterly, non-seasonally adjusted basis.*

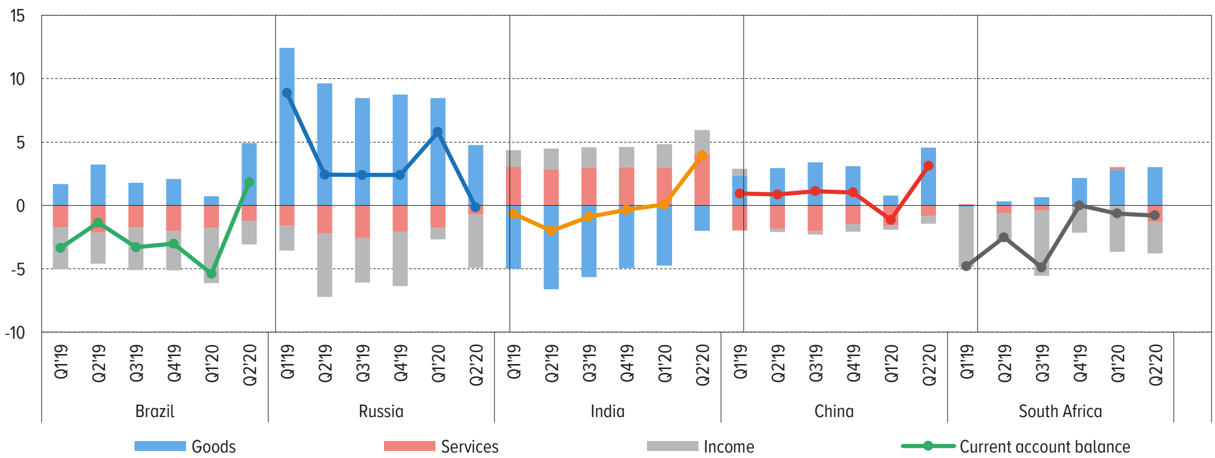
32% in Q2 on a year-on-year basis, despite an increase in gold exports in Q2 2020. Merchandise imports, after a year-on-year growth of 1% in Q1 2020, declined by 13% in Q2 2020 year-on-year, as domestic demand contracted due to the pandemic-related restrictions. Deficit in services account, while still up by 14% in Q1 2020, decreased sharply by 74% in Q2 2020 on a year-on-year basis. The biggest contributor to the decline in services deficit was the deficit in travel, which contracted by 90% in Q2 2020 on a year-on-year basis. The deficit on income account (primary and secondary combined) plunged by 53% in Q1 and by 34% in Q2 2020 from the level recorded a year ago, mainly due to contraction of investment income deficit on lower dividends, payable on direct and portfolio equity investments to non-residents.

- In **India**, current account balance recorded a surplus of 3.9% of GDP (USD 19.8 billion) in Q2 2020 on top of a surplus of 0.1% of GDP (USD 0.6 billion) in Q1 2020. The surplus in the current account in Q2 2020 was on account of a sharp contraction in the trade deficit to USD 10.0 billion due to steeper decline in merchandise imports relative to exports on a year-on-year basis. Net services receipts remained stable, primarily on the back of net earnings from computer services. Private transfer receipts, mainly representing remittances by Indians employed overseas, amounted to USD 18.2 billion, a decline of 8.7% from their level a year ago. Net outgo from the primary income account, primarily reflecting net overseas investment income payments, increased to USD 7.7 billion from USD 6.3 billion a year ago.

- In **China** the current account balance recorded a deficit of USD 33.7 billion (1% GDP) in the Q1 2020, as trade in goods, impacted by the outbreak of COVID-19, decreased sharply – export were down by 11%, import was down by 2% on a year-on-year basis. In Q2 2020, the current account balance turned back to a surplus, to the amount of USD 110.2 billion (3% of GDP), supported by a rising demand for goods including medical supplies and falling imports. Additionally, the deficit in services narrowed substantially compared to Q2 2019 (down by 55% year-on-year), which was mainly attributed to the sharp decline in outbound travel. The deficit in transport was USD 7.4 billion, down by 51% year-on-year, mainly due to a drop in the imports under trade in goods Meanwhile, some sectors benefited from the crisis – the IT related services and the fees for the use of intellectual property rights (some of credit and debit) have grown 18% and 4% in Q1-Q2 2020 year on year, respectively. Overall, the current account surplus, recorded in Q2 2020 was the highest since 2008, while the surplus in goods trade balance was the highest since 1998 and the deficit in the services was the smallest since 2013.

BRICS CURRENT ACCOUNTS DIVERGED DURING THE PANDEMIC
IN PERCENT OF GDP

Chart 22



Source: IMF, CRA Research Group.

- In **South Africa**, a surplus on the current account of 1.2% of GDP was recorded in the Q1 2020, marking the first surplus since Q1 2003 or the "pre-pandemic" era. During Q2 2020 the current account switched back to a deficit of 2.4% of GDP. With the domestic lockdown restrictions only effective from late-March, the effects of the COVID-19 pandemic on South Africa's imports and exports were mainly evident in Q2 2020. South Africa's trade surplus more than halved from Q1 to Q2 2020. The narrower trade surplus reflected a fall in the value of exports of goods that exceeded the decline in imports of goods. The lower value of exports and imports of goods reflected lower volumes. The shortfall on the services, income and current transfer account widened substantially from Q1 to Q2 2020: from 2.7% of GDP in Q1 2020 to 4.5% of GDP in Q2 2020.

Financial and Capital Account (excluding Reserve Assets)

Capital flows to BRICS in Q1 and Q2 2020 generally reflected swings in global risk sentiments – from an inflow at the beginning of the year, to sharp portfolio reversal towards to the end of Q1 2020 and, finally, to a stabilization closer to the middle of Q2 2020. At the same time, for meaningful inflows to re-emerge, more time is needed, with uncertainty reduced.

- In **Brazil**, net portfolio outflows accelerated sharply in early 2020, but FDI inflows have been stronger than in the same period of 2019, supported by high intercompany lending. In Q2 2020, net foreign direct investment (FDI) at USD 24.1 billion (7.4% of GDP) was higher than both a year ago in Q2 2019 (USD 8.8 billion or 1.9% of GDP) and in Q1 2020 (USD 18.9 billion or 5.2% of GDP). Foreign portfolio investment (FPI) in Q2 2020 declined less than in Q1 2020: USD 7.0 billion (2.2 % of GDP) in Q2 2020 after a decline of USD 24.3 billion (6.7% of GDP) in Q1 2020 and decline of USD 7.7 billion in Q2 2019 (1.7% of GDP).

- In **Russia**, net FDI investments in Q1 2020 recorded an outflow of USD 4.4 billion (1.1% of GDP) after four consecutive quarters of inflows in 2019. In Q2 2020, net FDI investments returned back to inflows of USD 1.5 billion (0.5% of GDP) due to substantial inflow of capital in debt instruments, while equity instruments still demonstrated outflows. In particular, in Q1 2020 debt instruments recorded a net outflow of USD 3.2 billion, followed by a net inflow of USD 5.8 billion in Q2 2020. At the same time, net equity outflows increased in Q2 2020 by almost four times, compared to Q1 2020. Net portfolio investments recorded an outflow both in Q1 and Q2 2020, increasing from 1.7% of GDP in Q1 2020 to 4.9 % of GDP in Q2 2020, due to both increase in acquisition of equity investments and a decrease in equity investment liabilities. Other investments (incl. financial derivatives) switched from net outflow of USD 6.2 billion in Q1 to a minor inflow of USD 0.3 billion in Q2 2020, mostly due to a decrease in debt assets, combined with a decrease in debt liabilities of other sectors.

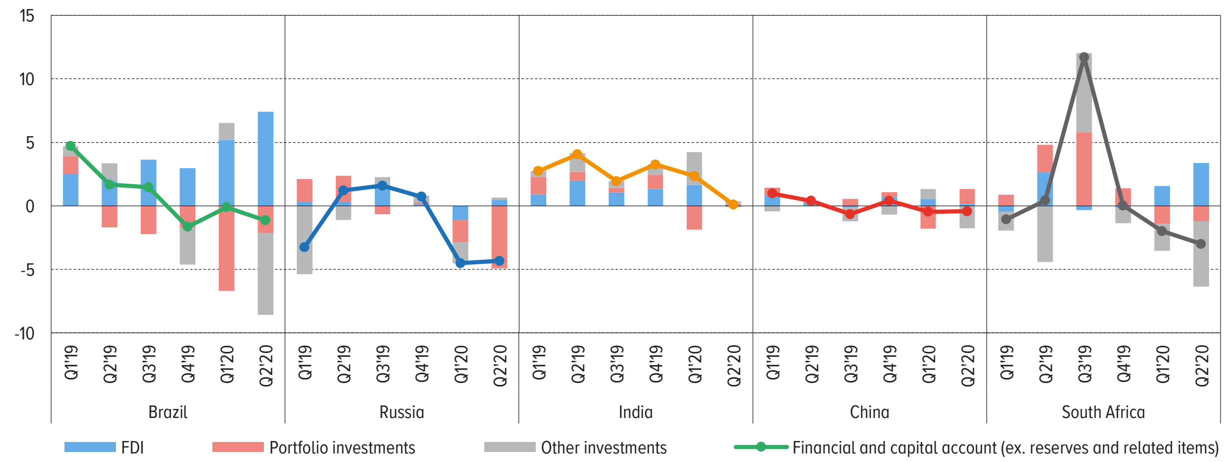
- **India** faced a drastic reversal of portfolio flows in Q1 2020 amid the COVID-19 shock, while FDI inflows continued. In Q1 2020 net FDI inflows at USD 12.0 billion (1.6% of GDP) were higher than USD 6.4 billion (0.9% of GDP) in Q1 2019, while in Q2 2020 net FDI recorded outflow of USD 0.4 billion as against inflows of USD 14.0 billion in Q2 2019. Net FPI in Q1 2020 declined by USD 13.7 billion (1.9% of GDP) as against an increase of USD 9.4 billion in Q1 2019 (1.3% of GDP) – on account of net sales in both the debt and equity markets due to the COVID related uncertainties. Further, net inflows under "other capital" surged during Q1 2020, reflecting inter alia the FPIs' outstanding balances with custodian banks and pending issuance of shares by FDI companies. In Q2 2020 net FPI was USD 0.6 billion as compared with USD 4.8 billion in Q2 2019 as net purchases in the equity market were offset by net sales in the debt segment. Inflows on account of external commercial borrowings registered a sharp increase to USD 9.4 billion (1.3% of GDP) in Q1 2020, which was close to 30% increase from Q1 2019 (USD 7.2 billion or

1.1% of GDP). In Q2 2020, with repayments exceeding fresh disbursals, external commercial borrowings to India recorded a net outflow of USD 1.1 billion in contrast to an inflow of USD 6.0 billion a year ago. Net inflow on account of non-resident deposits increased to USD 3.0 billion in Q2 2020 from USD 2.8 billion in Q2 2019.

- In **China**, the direct investments recorded a net inflow in both Q1 and Q2 2020 (USD 16.3 billion and USD 4.7 billion, respectively), which mainly consisted of equity investments. Among them, the outward direct investment recorded USD 18.0 billion in Q1 2020 (down 14% from Q1 2019) and USD 29.2 billion in Q2 2020 (up 14% from Q2 2019), not disturbed too much by the crisis. Inward FDI registered almost equal amounts in Q1 and Q2 2020: USD 34.3 billion and USD 33.9 billion, respectively. Compared to the levels of Q1 2019 and Q2 2019, the numbers were down by 28% and 1%, reflecting the downward impact of COVID-19 on global investment. The majority of FDI goes to non-financial sectors, among which manufacturing, information technology services, and the business services ranks as the top 3, accounting for 22%, 20% and 15% of the total FDI, respectively. The two-way capital flows remained active on the securities market. Net portfolio investments in Q1 2020 recorded outflows of USD 53.2 billion, compared to an inflow of USD 19.5 billion in Q1 2019 and inflow of USD 14.9 billion in Q4 2019. In Q2 2020, inward portfolio investment recovered, reaching historically high level, with a net inflow of USD 66 billion. Net outflow in equity securities in Q1 2020 was seven times higher than that of debt securities, while in Q2 2020 the inflow in debt securities was one-and-a-half times higher than that in equity investments.

- **South Africa** recorded a reversal of other investment liability flows to an outflow in Q2 2020 compared to an inflow in Q1, while portfolio liability outflows continued. Net FDI at USD 2.0 billion (0.7% of GDP) in Q2 2020 was higher than USD 1.3 billion (0.4% of GDP) recorded in Q1 2020. Inward FPI recorded outflows of USD 3.1 billion (1.1% of GDP) compared to an outflow of USD 6.4 billion (1.9% of GDP) in Q1 2020 – on account of continued net sales of both the debt and equity securities due to risk aversion by international investors. Net outflows under other investment increased during Q2 2020, reflecting the repayment of short-term loans by the domestic banking sector as well as the repatriation of deposits from the domestic banking sector by non-residents. Furthermore, domestic banking sector granted more short-term loans under repurchase agreements to non-residents, which was partly offset by the domestic banking sector's repatriation of deposits from non-resident banks.

BRICS FINANCIAL ACCOUNTS DETERIORATED MARGINALLY *Chart 23*
IN PERCENT OF GDP



Source: IMF, CRA Research Group.

Change in Reserve Assets (within Balance of Payments Accounts)

Despite the volatility, reserve coverage of BRICS countries remains adequate. In the "pre-pandemic" period Russia and India were building reserves, while Brazil, China and South Africa had negative changes in reserve assets within balance of payments accounts.

In **Brazil**, reserve assets increased by USD 3.4 billion in Q2 2020, partially offsetting the USD 20.2 billion decrease recorded in Q1 2020. Those movements partially reflect the BCB's actions in the FX market, aimed at reducing the excessive volatility experienced. The BCB provided liquidity to the markets by using a wide range of policy tools, concentrating its interventions during the onset of the market turbulence (March and April).

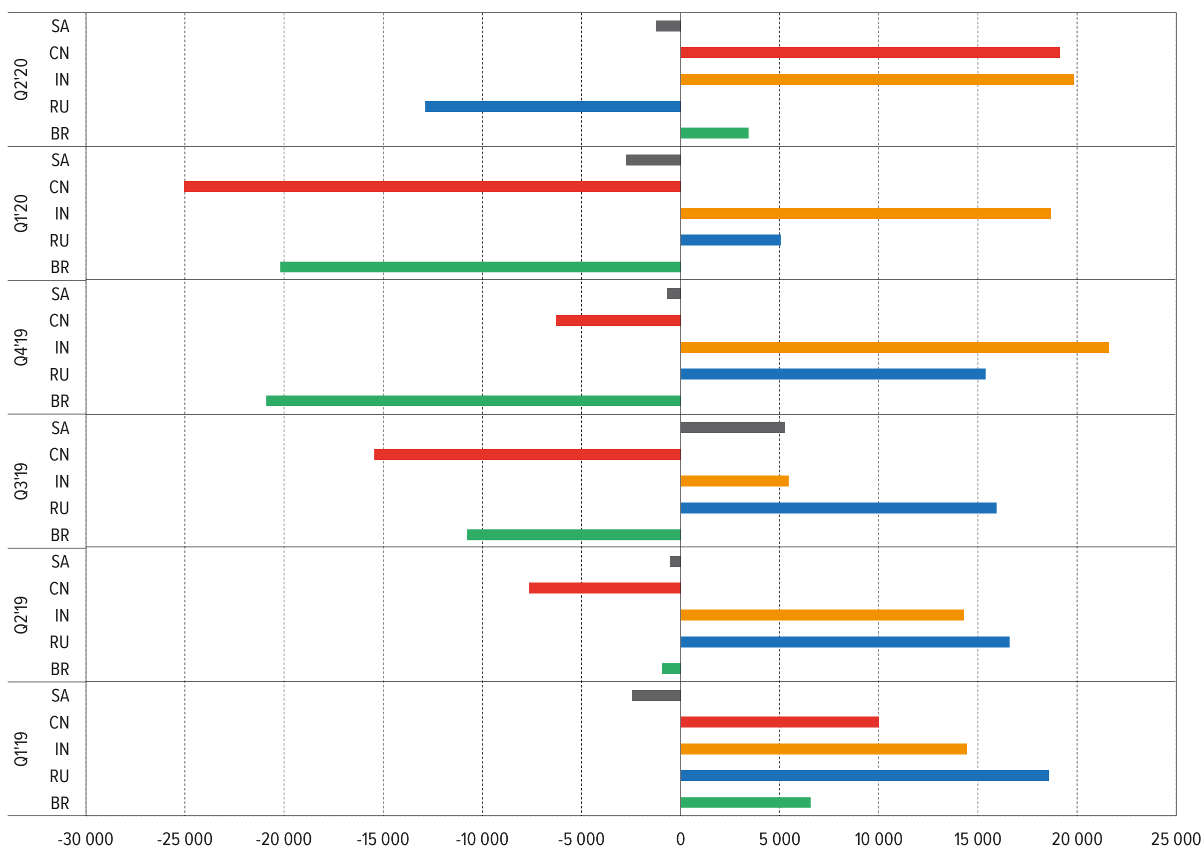
In **Russia**, reserve assets decreased by USD 12.9 billion in Q2 2020 after an increase of USD 5 billion in Q1 2020. Both increase and decrease of reserves mainly reflected operations in accordance with the fiscal rule – the FX purchases, when the oil price was above the benchmark, and the FX sales, when the oil price dropped below the benchmark.[3]

In **India**, reserve assets expanded by USD 18.8 billion in Q1 2020 on account of robust FDI and external commercial borrowing flows along with marginal current account surplus, as compared with an accretion of USD 14.2 billion in January-March 2019. The reserves increased by USD 19.8 billion in Q2 2020 primarily driven by the current account surplus, as compared with that of USD 14.0 billion in Q2 2019.

In **China**, reserve assets contracted by USD 25.1 billion in Q1 2020 and expanded by USD 19.1 billion in Q2 2020.

In **South Africa**, reserve assets decreased by a USD 1.2 billion in the Q2 2020 following a decrease of USD 2.7 billion in Q1 2020.

BRICS RESERVE ASSETS WITHIN BALANCE OF PAYMENTS ACCOUNTS CHANGED IN BOTH DIRECTIONS *Chart 24*
IN MILLION US DOLLARS



Source: IMF, CRA Research Group.

[3] *More details are provided in the Boxes section of the Bulletin.*

Net International Investment Position

In Q1-Q2 2020, the net international investment position (NIIP) improved substantially in South Africa, and moderately in Brazil, Russia and India, while remaining almost unchanged in China. Substantial improvement of the NIIP in South Africa was a result of valuation changes due to the depreciation of the rand exchange rate.

Regarding the long-term structure of NIIP by country, it could be noted that gross assets in Brazil, Russia, India and China rely on a combination of reserve assets and FDI, and in South Africa – on a combination of FDI and portfolio investments. With regard to gross liabilities, they are split almost equally between FDI and portfolio liabilities in Brazil and India, while in Russia and China the share of FDI liabilities is almost twice as that of portfolio liabilities, and in South Africa portfolio liabilities exceed FDI liabilities.

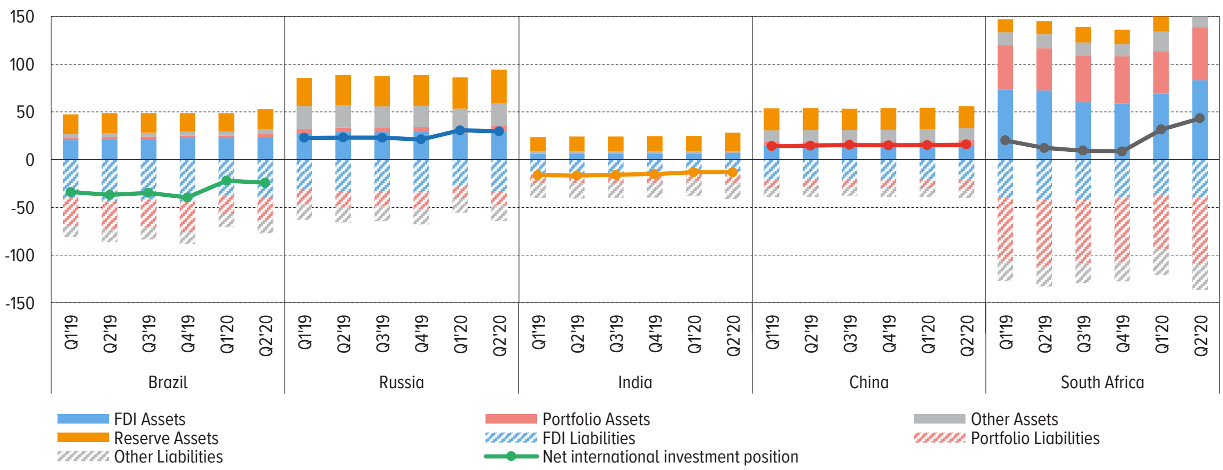
In Q1-Q2 2020, the ratio of gross assets to GDP[4] increased in all other BRICS countries, compared to the average ratio in 2019. The most notable increase of gross assets ratio to GDP has been recorded in South Africa, mostly due to revaluation effects (gross assets up by 38% in Q2 2020 relative to the 2019 average). In Brazil, the growth in gross assets ratio to GDP was driven by a moderate expansion of the FDI assets ratio to GDP, and in Russia and India the main driver was the stock of reserves. In China the growth of gross assets ratio to GDP was attributable to minor increase in FDI and portfolio assets.

Gross liabilities ratio to GDP in Brazil were less than the 2019 average in both Q1 and Q2 2020 due to a drop in FDI and portfolio liabilities. In Russia and India, gross liabilities ratio to GDP, dropped in Q1 2020 relative to the 2019 average, yet in Q2 2020 it almost restored its position to the levels of 2019 average. In case of Russia, the ratio of portfolio liabilities to GDP was slightly lower than 2019 average. In case of India, while portfolio liabilities to GDP was marginally lower, the ratio of FDI liabilities to GDP remained higher in Q2 2020 as compared with the 2019 average. In South Africa, the gross liabilities ratio to GDP also dropped in Q1 2020, but in Q2 2020 expanded substantially (by 7%) relative to its 2019 average, due to growth in both FDI and portfolio liabilities. In China, gross liabilities ratio to GDP remained unchanged in Q1 and increased slightly in Q2 2020 relative to the 2019 average on account of both FDI and portfolio liabilities' expansion.

The stock of reserves in BRICS economies remained at a healthy level in all countries: Brazil – 20%, Russia – 35%, India – 19%, China – 23%, South Africa – 18% of GDP.

BRICS NET INTERNATIONAL INVESTMENT POSITION IMPROVED
IN PERCENT OF GDP

Chart 25



Source: IMF, CRA Research Group.

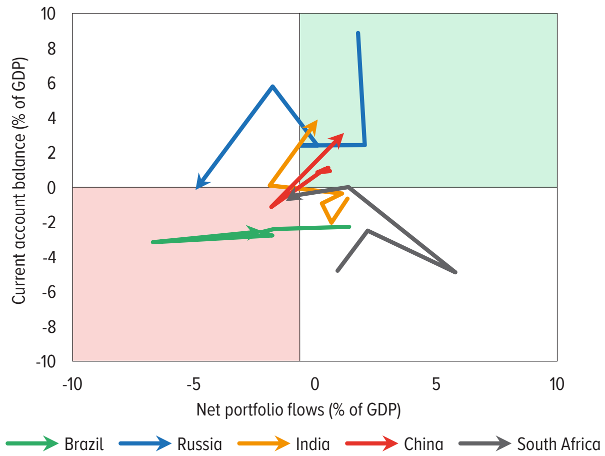
[4] *The ratios to GDP, used in the NIIP section, reflect the non-seasonally adjusted four-quarters-moving-sum USD GDP as a basis.*

Balance of Payments Stress

The potential build-up of balance of payments pressures could be gauged through a combination of dynamics of current account balance and net portfolio flows ratios to GDP, placed on the same chart.[5]

Points recorded below the diagonal line are indicative of build-up of balance of payments stress. In this region, capital (portfolio) inflows are insufficient to finance the current account deficit, or conversely capital outflows are in excess of the current account surplus. In particular, readings in the bottom left quadrant indicate a scenario of capital outflows coupled with a current account deficit. This is commonly referred to as the "pre-crisis" region and, if sustained for long periods, can result in a balance of payments crisis.

MEASURE OF BALANCE OF PAYMENTS STRESS IN Q1 2019 – Q2 2020 INDICATES NO MAJOR RISKS *Chart 26*



Source: CRA Research Group.

According to this metric, India's and China's positions improved substantially in Q2 2020, while Russia's and South Africa's position deteriorated. Brazil has remained in the "pre-crisis" area for several quarters, but strong FDI inflows allow it to assume the absence of any major risks to balance of payments.

Outlook: Will Structural Shocks Have Long-Lasting Effects?

A comprehensive evaluation of the effect of the shocks on the economies is quite difficult at the moment, as changes are still underway. Some of the effects will last well beyond the initial easing of the containment measures, leading to irrecoverable losses in businesses, reduced productivity and impaired human capital and, hence, a permanent damage to potential output.

Self-isolation measures, mandatory requirements of physical distancing and general fear of contracting the virus may have changed consumers' preferences along with work patterns and social behaviors. People may reduce their use of shopping malls, theaters, and other crowded places for a long time. The shift to remote work in some industries is also shaping new medium-term consumer habits.

Some of the longer-term consequences may include reshaping of supply chains, if firms, witnessing the vulnerability of cross-border trade, want to choose both more local, and more diversified contractors after the pandemic. Such processes could further constrain global trade. Manufacturing investments may remain sluggish for a long time, as businesses would be uncertain about the strength of future demand, and would be cautious of new safety requirements in production and transportation processes.

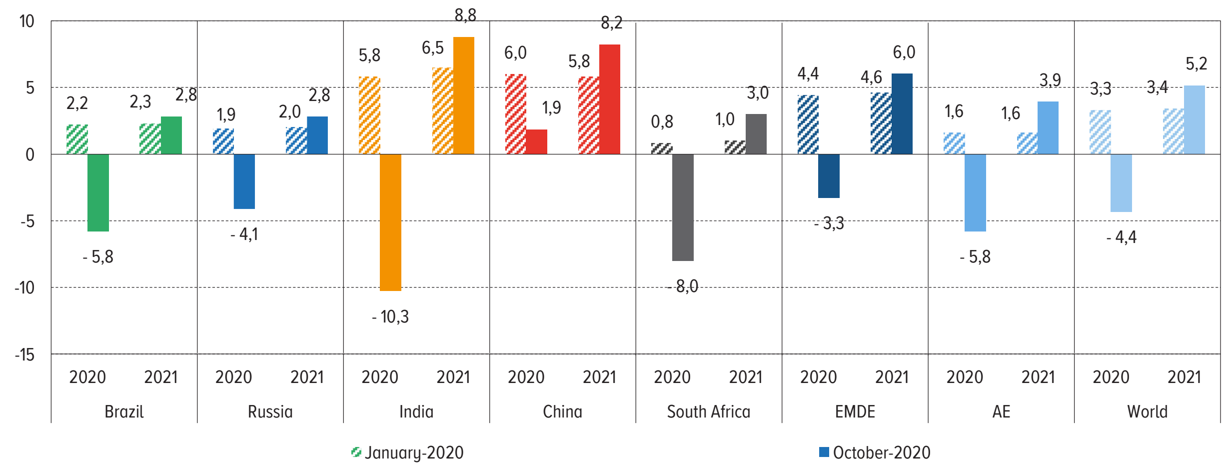
At the same time, new opportunities may come with forced digitalization, which all industries have experienced during the lockdowns. Investments in digital technologies such as online offerings, or new financial or professional services, may be on a rise. However, this may lead to structural mismatches in the economies due to the need to rebalance capital stock between tangibles and intangibles, impeding the smooth functioning of the economy.

The IMF projections for global growth in 2020 have shifted from a growth rate of about 3.3%, published in January 2020, to a sharp contraction of 4.4%, published in October 2020 – the most

[5] *Current account balance ratio to GDP is shown on Y-axis, net portfolio flows ratio to GDP is shown on X-axis.*

IMF PROJECTIONS ASSUME COMPENSATORY RECOVERY IN 2021
IN PERCENT, YEAR-ON-YEAR

Chart 27



Source: IMF.

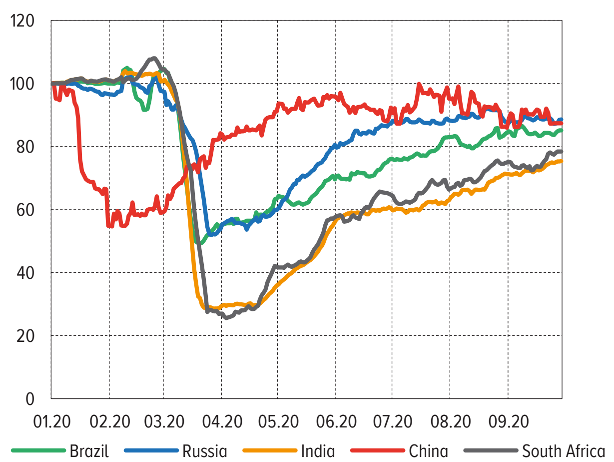
significant fall since the Great Depression. Almost all BRICS countries are expected to have a negative GDP growth in 2020, except for China. The growth numbers for 2021 are pointing to a speedy recovery, but despite the growth rate being higher than before the pandemic, the economies will need considerable time to get back to the level of GDP they had at the end of 2019.

Currently, the BRICS countries are in different stages of the fight against the pandemic. For some countries, the peak of new cases is behind, and the restrictions have already been lifted. For others, the number of active cases continues to grow or is growing again, which leads to at least partial constraints on the economic activity.

Nevertheless, the initial shock from the coronavirus has faded and with progress in reopening, economic indicators have improved gradually. This growth is fragile, and high frequency indicators show that the recovery has started to slow down. The real-time indicator Bloomberg Daily Activity Index indicate that by September the recovery pace moderately weakened in all BRICS countries. At the same time, the PMI indices look stronger and for most countries the numbers in September exceed 50-level threshold with a healthy margin. However, recent re-emergence of large-scale infections and partial re-introduction of restrictions in some countries may hinder recovery dynamism in the coming quarters.

BLOOMBERG DAILY ACTIVITY INDEX SHOWS THE RECOVERY IS SLOWING DOWN

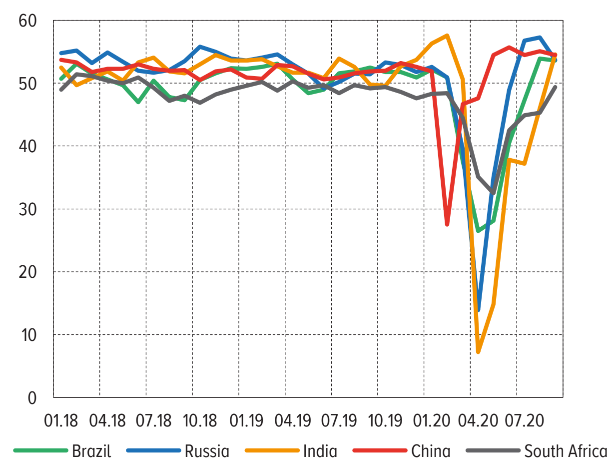
Chart 28



Source: Bloomberg.

BRICS PMI COMPOSITE INDICATE THE RECOVERY PROCESS IS NOT QUITE SMOOTH

Chart 29



Source: Bloomberg.

The BRICS current account balances would be affected by changes in economic activity, global trade and global financial conditions as well as swings in commodity prices.

As countries gradually reopen their borders, international supply chains are being re-established, allowing foreign demand to accelerate slightly. Nevertheless, the pre-existing conditions of trade relations, as well as different timing of lifting restrictions in various countries may lead to a prolonged period of subdued global demand, which may result in limited opportunities for the BRICS countries to expand their exports.

If global health conditions deteriorate, new spikes of volatility on the financial market will lead to a renewed tightening of global financial conditions for emerging markets, retriggering capital outflows and currency pressures, as well as deepening the decline in global trade. A more persistent tightening of financial conditions would hinder a recovery of capital flows and constrain the financing of current account deficits.

The *IMF* projects that current account balances of most BRICS countries will narrow in 2020 due to the contraction in economic activity, tighter global financial conditions, lower commodity prices, contraction in tourism and decline in remittances. At the same time, China's current account surplus may expand in 2020 if domestic consumption fails to recover quicker than external demand, and precautionary savings will rise. In 2021, BRICS current account balances would still be narrower than they were in 2019.

It is not yet clear which factors will prevail and how they will shape the outlook. If negative factors appear to be more persistent than currently assumed, the associated effects on current account balances could be larger. The overview of possible risks to BRICS countries' external positions is provided below.

EXTERNAL RISKS MATRIX

Table 2

Sources of External Risk	Potential Impact	Mitigation Factors and Strategies
Swings in energy commodities prices	Opposite impact within the BRICS group. In case of a drop, positive impact on CAB in India, China, South Africa, negative impact on CAB in Russia and Brazil. A surge in oil prices will have a reverse effect. For Russia, additional negative impact of lower oil prices would materialize in slower pace of reserve accumulation under the fiscal rule.	Seeking opportunities to build FX reserves. Floating exchange rates as shock absorbers.
Swings in non-energy commodities	Opposite impact within BRICS group. In case of gold prices, Russia and South Africa will benefit from higher prices, while India and China will experience negative impact on CAB. In case of other commodities (such as metals, iron ore) Brazil and Russia will benefit from higher prices, while other countries will experience negative impact on CAB.	The impact of non-energy commodities is generally less than that of energy commodities, but building additional buffers in good times may be useful.
Sharp tightening of global financial conditions	An abrupt change in global market sentiments may lead to sharp increase in risk premia and associated tightening of financial conditions, as well as may put pressures on currencies and cause capital flow reversals. Additionally, prolonged period of higher risk premia may lead to higher debt service and refinancing risks, as well as put stress on leveraged firms and households. All BRICS members are prone to this risk, with some countries likely to be more affected than others, given the composition of countries' financial accounts.	Seeking opportunities to build FX reserves. Floating exchange rates as shock absorbers. Monetary policy and macroprudential measures, providing liquidity and intervening to counter disorderly market conditions. Strengthening domestic banking systems. Deleveraging in case of high debt levels to reduce susceptibility to external shocks. Attracting more stable sources of financing to reduce vulnerabilities
Escalation of geopolitical tensions, rising protectionism	This risk may be both global and country specific. Global impact could materialize through depressed business confidence and investments, heightened risk aversion, disruption of trade flows. Country-specific impact could materialize through limited access to international financial markets, and reduced capital inflows, especially FDI.	Strengthening policy and crisis management frameworks. Large FX reserves serve as a cushion.

III. COOPERATION: PROPOSING STEPS TO ENHANCE FUTURE RESILIENCE

Overview of International Cooperative Response to the COVID-19 Shocks

The COVID-19 has turned a health crisis into a deep global economic and financial crisis. All the countries including advanced, emerging and low income economies have suffered the adverse impact of the current crisis in varying degrees. The BRICS countries also got a serious hit from the COVID-19. A global crisis of this magnitude warrants a concerted and well-coordinated policy response amongst countries and various international financial institutions (IFIs).

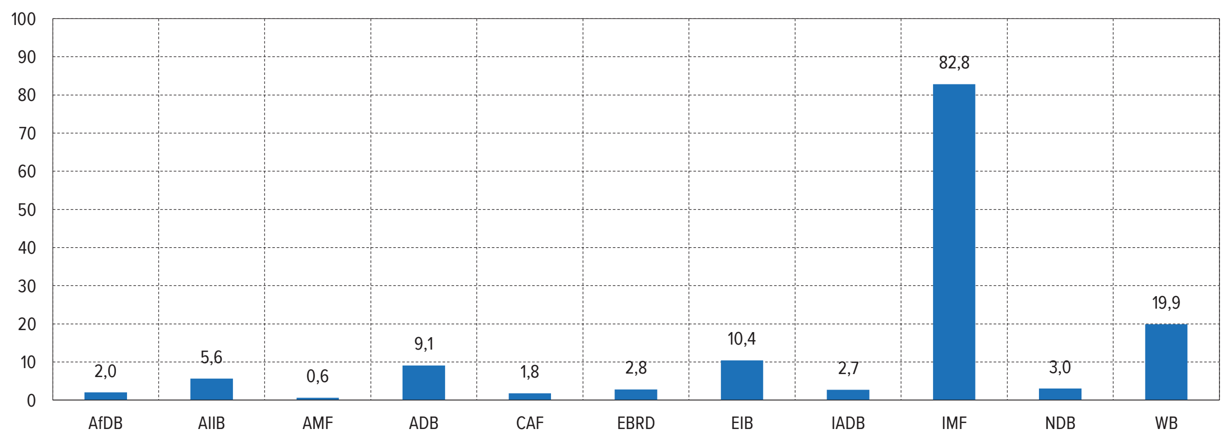
According to *the Center for Strategic and International Studies (CSIS)*, IFIs have approved financial support to the tune of USD 140.7 billion from January to mid July 2020 to meet the COVID-19 crisis. Out of this, the IMF has provided a lion's share of USD 82.8 billion (or 60%) followed by the World Bank (WB), the European Investment Bank (EIB) and the Asian Development Bank (ADB). The IMF has provided support to around 80 countries in the wake of the pandemic prominently through its two instruments, viz., Rapid Financing Instrument (RFI) and Rapid Credit Facility (RCF). The BRICS countries, some of whom have benefitted during the COVID-19 pandemic from multilateral lending facilities, have also contributed to the resource mobilization efforts of the IMF and the World Bank to the tune of approximately USD 274 billion.

According to CSIS, out of the five RFAs, only the Arab Monetary Fund has approved and disbursed financial support (to the tune of USD 0.6 billion) in response to the current crisis. Other prominent RFAs like the Chiang Mai Initiative Multilateralization (CMIM), Eurasian Fund for Stabilization and Development (EFSD), European Stability Mechanism (ESM), BRICS Contingent Reserve Arrangement (BRICS CRA) and Latin American Reserve Fund (FLAR) have not approved and disbursed any financial support yet. In fact, the bilateral swap arrangements have been accessed more frequently to provide short-term liquidity, especially dollar liquidity. Case in point are the US Fed-central bank swap lines, SAARCFINANCE Swap Arrangement, etc.

In light of the above, prima facie, it seems that the three pillars of the global financial safety net (GFSN), viz., forex reseves, bilateral arrangements and the IMF have been much more active than the RFAs in supporting the member countries during one of the worst economic crisis of the

FINANCIAL SUPPORT APPROVED BY MAJOR IFIS
IN BILLION US DOLLARS

Chart 30



Source: Center for Strategic and International Studies (CSIS), African Development Bank (AfDB), Asian Infrastructure Investment Bank (AIIB), Arab Monetary Fund (AMF), Asian Development Bank (ADB), Development Bank of Latin America (CAF), European Bank for Reconstruction and Development (EBRD), European Investment Bank (EIB), Inter-American Development Bank (IADB), International Monetary Fund (IMF), New Development Bank (NDB, BRICS Bank) and the World Bank (WB).

humankind. Possible reasons for less uptake of crisis financing from RFAs could lie in the profile of membership, familiarity of countries with the IFI/bilateral procedures, faster and smoother drawals with less stringent pre-conditions, the fact that the stigma factor would be less predominant in a pandemic situation to deter countries from approaching IFIs, proactive stance of IFIs including introducing new instruments and less exacting eligibility criteria and conditionalities, the size of funding, extraordinary factors (such as sanctions blocking the free operation of RFAs), etc. Therefore, it is an opportune time to assess the structure and operationalisation of the RFAs and to find out what best efforts could be made to make it an effective pillar of the GFSN. With rapid financing instruments and short-term swap facilities of the IMF, RFAs are likely to be less attractive for the member countries. It is also equally important to remove the apprehensions regarding the involvement of multiple countries, time required for sanctioning the request, higher interest rate and other operational difficulties.

Proposed Steps for the Upcoming BRICS Chairs

While there was no disruption of communications with BRICS partners once the COVID-19 pandemic started to develop, in view of the above, BRICS CRA technical teams can undertake a collaborative research study covering the role of RFAs during COVID-19 pandemic, examine whether member countries of RFAs sought help outside their RFAs, potential role of RFAs in the future and suggestions to improve structure and operations of RFAs to make it an effective pillar of the GFSN. The upcoming BRICS Chairs can undertake this study by forming a team of collaborators for it. The team may consider seeking information/inputs from other RFAs. Based on this research study, the team can make concrete proposals for improving the effectiveness of BRICS CRA.

In addtion to that, it might be of use to get a sense of how much liquidity injection BRICS countries needed or might need during the peak of the pandemic and whether the CRA resource capacity of USD 100 billion is sufficient should the shortage in dollar liquidity persist. The upcoming BRICS Chairs could conduct a survey on liquidity shortage in BRICS countries.

Another way of enhacing co-operation is to deepen current exchange of macroeconomic information including vulnerabilities. The quarterly teleconferences and economic notes have to be continued. The coming issues of this Bulletin can take up some relevant sections that would provide information on global and individual early warning signals and macroeconomic vulnerabilities based on published data. Indicators of external and domestic debt, reserves adequacy, financial soundness and corporate sector indicators along with developments in the global economy, and political risk could inform our assessment.

The test run of the CRA must be continued by involving more complications and untested matters. Since BRICS central banks successfully conducted three test runs under the delinked part of the CRA, now priority must be given to the IMF linked portion. BRICS central banks should also consider testing more complications in coming years which could include opting out, novation, imposition of late fee for non-repayment, settlement in bilateral trade due to the repayment default and local curency settlement. If any further gaps are noticed in the CRA or ICBA to handle certain situations, these may be flagged for an amendment of the document/s. These measures will improve the efficiency and crisis-readiness of BRICS CRA.

Overall, all co-operation efforts should be directed in such a manner that with every passing year BRICS central banks must be in a a better position to respond to members' financing needs and enhance their financial soundness in a smooth and timely manner.

KEY POLICY RESPONSES OF BRICS COUNTRIES TO MITIGATE THE ADVERSE ECONOMIC IMPACT OF COVID-19 SHOCKS

Brazil

Brazil adopted a comprehensive set of measures dealing with multiple fronts of this crisis. That includes bolstering liquidity in domestic and in foreign currency, reducing its policy rate (Selic) to its lowest historical level, taking credit to where it is most needed, and ensuring business and financial services continuity of banks and the Central Bank. Along with monetary and financial sector policies, the Federal, State and Local Governments are also taking actions in the fiscal front, especially to help those most affected by the crisis. This box underscores selected measures involving the financial sector *taken* by the Central Bank of Brazil (BCB) and the CMN (the National Monetary Council).

Liquidity Support

The measures aim at ensuring that financial institutions have sufficient funding to meet market's liquidity needs, providing financial institutions with confidence to maintain and expand credit. These measures imply a BRL 1,274 billion potential expansion in the system liquidity, reaching about 17.5% of GDP.

Liquidity Support (in BRL billion) Data until 09/25	**2020 – Potential**	**2020 – Implemented**	**2008**
Reserve requirements + change in LCR regulation	135	135	–
Additional reduction in reserve requirements	70	70	82
Regulation flexibility on Agribusiness Credit Bills (LCAs)	2.2	2.2	–
Loan backed by Financial Letters (FL)	670	50.5	–
One-year term repos backed by government bonds	50	23.2	25
New term deposit with special guarantees (NDPGE)	200	18	10
Loans backed by Debentures	91	3	–
Change in reserve requirements on saving deposits	55.8	40	–
Total	**1,274**	**341.9**	**117**

Capital Relief

The National Financial System (SFN) presents a comfortable level of capital. Nevertheless, financial institutions may have to face losses amid the COVID-19 crisis. To mitigate the effects of the crisis, regulation on capital requirements was adjusted to provide financial institutions with better conditions to sustain credit flow. These measures have the potential to increase credit supply by BRL 1,348 billion, reaching about 18.4% of GDP.

Potential Impact on Credit Provision (in BRL billion) Data until 09/25	**2020 – Potential**	**2020 – Implemented**
Overhedge	520	520
Reduction of the Additional Principal Capital (ACP) factor	637	637
Reduction in capital requirements for credit operations to SMEs	35	35
Reduction in capital requirements for S5 segment (simple risk profiles)	16.5	16.5
Reduction in capital requirements for DPGE exposure	12.7	12.7
Working capital for business preservation (CPGE)	127	127
Total	**1,348**	**1,348**
More flexibility for credit renegotiations	3,200	857,9

Other Measures

Other Measures (in BRL billion) Data until 09/25	**2020 – Potential**	**2020 – Implemented**
Asset purchases in secondary markets	n.a.	–
Swap lines with Federal Reserve	60	–
Creation of special credit lines for SMEs	40	5.3
Real estate backed loans	60	In progress

Credit Granting

It is important to note that the evolution of credit depends on the risk appetite of financial institutions. Economic agents' risk appetite is influenced by macroeconomic and financial conditions and expectations about these conditions over time. The BCB works to encourage these conditions and expectations, but risk-taking is the responsibility of the Financial Institutions' managers.

In this regard, measures implemented by the BCB and CMN fostered the credit channels to keep them functional and effective during the pandemic. In view of the adverse scenario resulting from the effects of the COVID-19 pandemic, the trend would be for credit to shrink, as in the case of the recent Brazilian recession of 2015/2016. However, credit granting to households and corporates in 2020 remained at higher levels than those observed in the same period of 2019.

The evolution of non-earmarked credit granting reached a significant increase of 26.9% for firms and 8.3% for households, considering the twelve-month period from August 2019 to July 2020. The table below shows the growth of total credit, by company sizes, with higher growth rates observed for small and micro entities.

Size	**Jul-2020/ Dec-2019**	**Jul-2020 / Aug-2019**
Large	12.6%	13.5%
Medium	10.6%	17.9%
Small	17.0%	24.8%
Micro	24.4%	28.7%

In addition, the BCB has been observing that, on average, interest rates are falling for new transactions and renewals to both household and corporate borrowers, and also by different types of credit.

Takeaways

Timely measures taken by the BCB and the CMN have been successful in maintaining liquidity and the fluidity in the credit market, benefiting households and companies of all sizes, with an increase in credit granting and reduction in average interest rates. The BCB is continuously monitoring all measures and constantly receives proposals for improvements in current policy measures, both by its staff and by the market. If necessary, the Central Bank will adopt new measures and use all tools available for the proper functioning of the Brazilian Financial System and to foster financial stability.

Russia

In Russia, COVID-19 started to spread in late February 2020, and the tightest restrictions were in force approximately from late March to mid-July, depending on the region. The restrictive measures included mandatory self-quarantine, closed schools, theaters, and sports facilities, as well as remote work requirements. The Government of the Russian Federation together with the Bank of Russia implemented a set of measures, that provided prompt and multifaceted support to households and businesses during the most challenging period of the crisis.

Measures by the Government of the Russian Federation

The Government of the Russian Federation approved three packages of anticrisis measures in March – May 2020 and National economic recovery plan in September 2020. All aimed at supporting households and businesses.

The overall set of the measures implemented in 2020 was unprecedented. It is estimated at 4,5% of GDP in value terms (taking into account tax breaks).

Generally, measures were focused on supporting health care system and maintaining households' incomes, employment. As for businesses the support was provided both directly (e.g. as subsidies and preferential loans) and indirectly, namely through a temporary reduction or suspension of mandatory payments to the budget.

The largest part of the direct aid to businesses was aimed at maintaining employment in the industries that were most severely affected by the pandemic[1]. Alongside with that, the Government introduced additional measures in those industries, including construction, air transportation, tourism and others. In order to support housing construction the Government expanded the preferential mortgage lending programmes to keep up housholds' demand for housing amid declining incomes. Moreover, to help business go through the relaunch processes in the aftermath of the pandemic, the Government implemented temporary measures to reduce the administrative and supervisory burden.

Measures by the Bank of Russia

The Bank of Russia (BoR) also implemented *a set of measures* aiming to support individual and corporate borrowers, as well as to maintain the lending activity in the economy, and reduce the regulatory and supervisory burden.

After COVID-19 started to spread widely across the country and the economic conditions started to deteriorate, the BoR, though being close to a neutral stance, decided to continue the accommodative policy: over the period of January – July 2020, the policy rate was gradually cut from 6.25% to 4.25%, while the inflation rate remained close to the target. At the same time, despite some volatility on the EMDEs currency market, the BoR did not exercise any FX operations beyond what was required by the existing macroeconomic framework. The BoR started to sell reserves on March 10th in accordance with the fiscal rule due to low oil prices. Additionally, there were FX sales due to the deal, on the Government's purchase of the controlling stake in Sberbank, but the deal itself was agreed before the pandemic.

Considering borrowers' support, the BoR helped to facilitate the loan restructuring process (including the postponement of repayments and loan extension) for both corporate and individual borrowers. In particular, the BoR recommended that credit institutions do not downgrade borrowers' credit scores, including the assessment of borrowers' financial position (especially of companies in the COVID-hit industries), the quality of debt servicing, or the quality of loans. Affected individuals

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[1] *Motor transportation, air, water and rail transport; tourism; exhibition and conference activities; hotels; culture, entertainment and leisure; catering trade; personal services; physical culture and sports; retail trade; dental care services; extended education; mass media.*

and small and medium-sized enterprises (SMEs) could receive deferrals of loan payments for up to six months and banks were allowed not to classify such loans as restructured for loan loss provisioning purposes. Moreover, to provide long-term refinancing to banks and ease maturity mismatch of their assets and liabilities, the BoR launched long-term repo auctions (1 month and 1 year), which also served as a source of financing for banks offering loan restructuring options to their clients. To ensure gradual recognition of loan quality deterioration and maintain credit activity, the BoR has undertaken extensive relax measures in relation to creating provisions for borrowers whose financial situation has worsened following the pandemic. These measures apply to 85% of loans to corporate borrowers including SMEs, as well as loans to individuals affected by the pandemic[2]. In order to support mortgage lending segment, add-ons to risk weights for mortgage loans issued before 1 April 2020 were canceled and add-ons to risk weights for mortgage loans issued after 1 April 2020 were lowered. Similarly, add-ons to risk weights for unsecured consumer loans issued beginning on 1 September 2020 have been reduced and add-ons to risk weights for ruble-denominated unsecured consumer loans issued until 31 August 2019 have been cancelled.

The BoR also established temporary preferential SME funding facility with a limit of 500 billion rubles. The interest rate on this instrument during the period of April-July 2020 was cumulatively reduced from 4 to 2.25%, following the key rate reduction. The regulation for banks granting loans to SMEs has also been relaxed.

Considering the macroprudential and supervisory policy, the BoR decided to keep the countercyclical capital buffer at 0% and reminded banks that they are allowed not to comply with requirements on the capital conservation buffer and on the buffer for systemic importance (in that case they are prohibited to distribute profits and pay dividends). The conditions of irrevocable credit lines (ICL) as part of complying with Liquidity Coverage Ratio (LCR) have been eased. The threshold for the right to use an ICL has been lowered from 0.5% to 0.15% and the maximum limit of ICL has been raised to 5 trillion rubles, thus offering systemically important credit institutions more opportunities to manage their liquidity amid the elevated volatility. Financial institutions have been allowed to temporarily have their LCR ratio fall below 100%, given that this reduction was a result of the deficit of highly liquid assets and other alternative instruments due to limited options to prolong or attract funds for more than 30 calendar days. In addition, the BoR suspended introduction of new regulatory requirements until the economy gets back to normal.

Besides the above, the BoR suspended its inspections of all financial institutions and extended the deadlines for fulfilling a range of requirements for credit institutions, financial market participants, collective investment entities and microfinance institutions. Furthermore, to minimize possible face-to-face contacts between bank employees and customers, the BoR temporarily alleviated the strictness of certain customer identification procedures, so that banks could provide services remotely. Credit institutions were also allowed to extend the deadlines for residents to submit certificates of confirming documents, as well as documents on foreign exchange operations.

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[2] *It is allowed not to increase provisions for loans to individuals with the coronavirus infection and for individuals whose loans were restructured due to a decrease in income and were not overdue as of March 1, 2020.*

India

In order to limit the contagion of the COVID-19 pandemic, a nation-wide lockdown was imposed from March 25, 2020 by the government and immediate relief was announced, under the *Pradhan Mantri Garib Kalyan Yojana*, to prevent cash and food crisis. The economic fallout of the prolonged standstill in all activity was addressed, by the national authorities with measures being undertaken, under the *Atmanirbhar Bharat Abhiyan* (ABA), in five tranches mainly focusing on rural employment generation, infrastructure, liquidity support, micro, small, and medium-sized enterprises (MSMEs), non-bank financial companies (NBFCs), migrant workers and ease of doing business. These measures, covering the announcements by both the Government of India and the Reserve Bank of India, aggregate around ₹20 lakh crore or 10% of GDP. The measures, both short-term and long-term in nature, endeavour to make India self-reliant in numerous sectors with global quality and competitiveness.

Fiscal and Structural Measures by the Government of India

India's fiscal support measures can be broadly divided into direct spending, foregone or deferred revenue and below-the-line measures designed to support businesses and shore up credit provision to several sectors. The key fiscal measures include, cash and kind (food, cooking gas) transfers to lower-income households; insurance coverage for health workers, fund allocation on health infrastructure, concessional credit to farmers, credit support to poor households, businesses and electricity distribution companies, wage support and employment provision to low-wage workers. Sector-specific packages were announced for MSMEs, NBFCs and agriculture, viz., partial credit guarantee scheme for NBFCs, collateral free loans, additional fund allocation for rural employment, measures to provide relief to contractors, insolvency related measures, relaxation for real estate projects and measures to enhance ease of doing business.

The structural reforms, under the ABA, aimed to promote businesses, attract investment and strengthen manufacturing in India, covered policies related to the core sectors like coal, minerals, defence production, civil aviation, power, social infrastructure, space and atomic energy. The other structural reforms included supply chain and price realisation reforms for agriculture, contract farming reforms, relaxation in stock-holding limits easing of the tax compliance (direct and indirect taxes), relaxation in labour laws and simplification of laws.

Monetary and Regulatory Measures by the Reserve Bank of India

Measures taken by the Reserve Bank can be broadly categorized as (i) monetary policy measures; (ii) liquidity measures; (iii) regulatory and supervisory measures; and (iv) business continuity plans.

The conventional and unconventional monetary policy and liquidity measures by the Reserve Bank have been aimed at restoring market confidence, alleviating liquidity stress, easing financial conditions, unfreezing credit markets and augmenting the flow of financial resources to those in need for productive purposes. The deteriorating outlook for growth, with the outbreak of the pandemic, necessitated off-cycle meetings of the Monetary Policy Committee (MPC) in March and May 2020. The MPC cumulatively cut the policy repo rate by 115 basis points since March 2020 till October 2020, resulting in a total policy rate reduction of 250 basis points since February 2019 to 4.0 percent. It was also decided to continue with the accommodative stance as long as it was necessary to revive growth and mitigate the impact of COVID-19 on the economy, while ensuring that inflation remains within the target.

The liquidity measures announced by the RBI during February to end-September 2020 aggregate to about ₹11.1 trillion (equivalent to about 5.5% of 2019-20 nominal GDP).These liquidity measures broadly include, long-term repo operations, targeted long-term repo operations, liquidity adjustment facility, open market operations, special refinance facilities for all India financial institutions, special liquidity facility for mutual funds and cut in cash reserve ratio and are expected to sustain high liquidity in banking system and de-stress financial markets. The Reserve Bank undertook two six-month USD-INR swaps of total USD 7 billion in March 2020 to infuse dollar liquidity. In response, financial conditions have eased considerably, as reflected in the spreads on money and bond market instruments.

Banks and other lenders have been allowed to extend term loan repayment schedule and moratorium and defer interest on working capital repayments. In September 2020, the Reserve Bank, advised all lending institutions to mandatorily consider the key financial ratios (recommended by an expert committee) while finalizing the resolution plans in respect of eligible borrowers. As the lock-down had limited on-site supervision, the off-site surveillance mechanism was enhanced. The Reserve Bank has taken proactive measures immediately after the outbreak of the pandemic to avoid any disruption to the payment system in the country. Regulatory forbearances were given towards easing the situation with the required caveats so that only the genuinely distressed cases are placed under restructuring while the banking sector is ring-fenced from potential losses.

The Reserve Bank activated an elaborate business continuity plan for its own operations for critical operations in banking and financial market operations and payment systems, at the same time ensured that banks also activate their own business continuity plans. All regulated entities were also advised to assess the impact of COVID-19 on their balance sheet, asset quality and liquidity, and take immediate contingency measures to manage their risks.

The securities market regulator, Securities and Exchange Board of India, introduced measures aimed at containing market volatility and improving market integrity, in the wake of uncertainties prevailing in the markets amidst the COVID-19 pandemic. These included enhanced margins, reduced market-wide position limits and curbs on short-selling. At the same time, relaxations were given to market participants with regards to various compliance requirements and extension of validities.

China

Since the outbreak of the COVID-19 in China, People's Bank of China (PBC) has carried out monetary policy measures with proper hierarchy and pace, based on the stages and characteristics of the epidemic containment and economic recovery. These policy measures are implemented in a timely and powerful manner, with appropriate funding. The sound monetary policy and proactive fiscal policy matches well and provides solid support to the epidemic containment and economic recovery.

Sound Monetary Policy that was More Flexible and Appropriate

By the end of October 2020, PBC provided liquidity of over 9 trillion RMB (about USD 1.4 trillion) or 9% of GDP, with a full package of quantitative, price, and structural toolkit. These measures included open market operation, central bank loan and discount, as well as targeted reserve rate cut. PBC cut reserve rate three times, released long term capital 1.75 trillion RMB, to keep liquidity adequate at a reasonable level. In particular, to mitigate the negative sentiment in the market after the traditional lunar new year of China, PBC conducted 1.7 trillion RMB short-term repos through open market operations (OMOs) from Feb 3 to 4, thus supporting the stable operation of the financial market.

In the early stage of the outbreak, the PBC provided special central bank lending amounting to RMB 300 billion on January 31, which was intended to provide low-cost funds to banks, and enable them to provide credit support at preferential interest rates to major enterprises that participated in the production, transportation, and sales of medical supplies and daily necessities for epidemic containment. After the 50% of fiscal subsidies, the real corporate financing cost has been lowered significantly. At current juncture, the bunch of central bank lending has been fully under a listed-based management, providing targeted and solid support to over 7,600 enterprises participating in epidemic containment.

At stage two, in which the spread of the epidemic has been initially under control and the production has resumed orderly, the PBC raised the quota for central bank lending and central bank discounts by a total of RMB 500 billion on February 26. Meanwhile, the lending interest rate of commercial banks declined to no more than one-year loan prime rate (LPR) plus 50 bps, and the average actual interest rate was nearly 4.4%. The 500 billion RMB has been used out also, supporting nearly 0.6 million enterprises to resume their production.

In the latest stage, in which the epidemic containment achieved significantly progress, with production recovered with a greater speed, PBC introduced another 1 trillion RMB of inclusive central bank lending and central bank discounts quotas in April 20, to support the banks to extend credit supply designated for agricultural entities, medium and small business, and private businesses, and the average financing cost declined to about 5.5%. This measure was to support over 2 million enterprises.

PBC paid-high attention to supporting SMEs. In particular, the policy banks increased 350 billion special credit line to private SMEs, which has been totally used by the end of June. Besides, on June 1st, the PBC introduced two innovative monetary policy tools, which provided direct support for the real economy. These tools promote the banks to grant time-limited deferment of loan principal and interest repayments for the micro and small businesses (MSBs), and provide inclusive unsecured loan to MSBs. By the end of August, commercial banks have finished the deferral of loan principles repayment for 1.6 million market entities and deferral of loan interest repayment for 0.8 million market entities with a total amount of 3.7 trillion yuan. From March to August, the banks issues over 30 million batches of inclusive MSBs unsecured loan which amounts to 1.9 trillion RMB, an increase of 63 billion RMB year on year.

In addition, PBC also employed supportive price policy tools to lower the social financing costs. The rates for MLFs and OMOs were guided to drop 30 basis points, which brought down the loan prime rate (LPR). The PBC pushed ahead with the shift in the pricing benchmark for outstanding floating-rate loans so as to reduce interest payments for outstanding loans. Also, PBC cut the central bank lending rate on loans supporting the agricultural sector and small businesses by 0.25 percentage points to 2.5 percent.

Other Policy Measure to provide Special Efficient Financial Services to Support Epidemic Containment

To support the epidemic containment, PBC opened "fast track" to make sure the basic financial services are functional and enables the production for medical facility and life's necessities.

On February 1st, PBC carried out 30 financial supportive measures jointly with Ministry of Finance, China Banking and Insurance Regulatory Committee (CBIRC), China Securities Regulatory Committee (CSRC), and State Administration of Foreign Exchange (SAFE). These measures include issuing credit at preferential rates to enterprises producing epidemic containment facilities and providing differentiated and preferential financial services to the regions, industries and enterprises which are heavily affected by the COVID-19.

Green channels were set to ensure the epidemic containment related clearance and settlement remain unaffected. From January 24 to May 10, the payment system of PBC processed 8,153 tranches of large amount special payment (over 10 million per tranche), totaled 549.4 billion RMB. Green channels were also set to ensure the functional operation of foreign exchange business and protect the epidemic containment related trade.

During the crisis, four groups of people were hit the most: patients of COVID-19, the quarantined people due to the requirement of disease control, people involved in the containment work and people who lost their income due to the health crisis. PBC enhanced the flexibility of the credit information collection by deferring the repayment deadline of mortgage and credit card, waiver the overdue repayment of the four groups of people and remove them out of the default list; not including the enterprises hit heavily by the epidemic into the blacklist of credit information.

Green tracks in debt issuance were introduced to lower the comprehensive financing cost. PBC enlarged the effective period of issuance quota, adjusted the information disclosure limit, and supported online processing, and lower the fees for the debt issuance of areas and enterprises hit heavily by the crisis.

South Africa

National State of Disaster

The COVID-19 pandemic developed later in South Africa than was the case elsewhere. The 100th reported case was recorded on March 18, 2020, which was between two to four weeks later than in most of the large Western European countries. The South African authorities were thus able to learn from the experiences of other countries. Containment efforts were speedily introduced which included a strict nationwide lockdown that came into force on midnight of March 26, 2020. This facilitated a gradual and cautious re-opening of the economy with the decisions on the lifting of restrictions on sectors being undertaken in five stages on the basis of health and socio-economic considerations. Evidence indicates that the lockdown and other containment measures was effective in "flattening the curve" of infections and casualties.

In early May 2020, a phased lifting of the lockdown began in line with the deceleration in the rate of infections amid stringent adherence to safeguard measures by both businesses and the community at large. Additional restrictions were relaxed at the beginning of September 2020 as the infection curve flattened, allowing for the upliftment of almost all restrictions including international travel to certain countries.

Monetary Policy and Financial Responses

Like other countries, the action of the South African authorities have been directed at protecting both lives and livelihoods. In essence, this has entailed ensuring that the health system can cope with a rising number of COVID-19 patients while limiting the economic fallout by protecting jobs and preventing an escalation in the levels of inequality and poverty.

Since the beginning of March 2020, the South African Reserve Bank (SARB) has reduced its policy rate by a cumulative 275 basis points, a move that has been made possible by a continued decline in both short-term price pressures and longer-term inflation expectations. Given that monetary policy takes some time to transmit to the real economy, rates were reduced before the full force of the shock appeared in the data, so as to provide maximum support to the economy early on.

While this stimulus had limited effects in the first stages of the lockdown, given the restrictions on most forms of economic activity, it has underpinned the subsequent recovery. In particular, low rates have increased household demand for credit, with mortgage applications and grants, for instance, now at 10-year highs. Low short-term rates have also helped corporates through a period of stress, while allowing government to fund emergency spending via cheap short-term debt. Following the large reduction in the repo rate in March, April and May 2020, the Monetary Policy Committee has adopted a "wait and see" strategy, by lowering the policy rate in July 2020 for the last time and leaving it unchanged in September 2020 at 3.5%.

Monetary policy implementation has also been supported by the SARB's use of its balance sheet as an active policy tool. Since March 2020, the SARB embarked on measures to ease liquidity constraints observed in funding markets, including the purchases of government bonds in the secondary market across the entire yield curve to ensure continued liquidity and proper functioning of debt capital markets. The SARB has, since August 2020, reduced the scale of bond purchases amid restored financial stability in the domestic market.

Macroprudential Measures

The Prudential Authority of the SARB acted speedily to monitor the impact of the virus and the lockdown on all regulated institutions and provided regulatory relief to banks and offered guidance on how to manage the crisis from regulatory and accounting perspectives. Measures to provide temporary capital and liquidity relief to banks in a manner that complied with the internationally agreed framework were implemented and included:

- Reducing the systemic risk add-on, commonly referred to as the Pillar 2A add-on, from 1% of total capital to 0%,
- Providing clear criteria on how banks can utilise their capital conservation buffer, i.e., the loss absorbing capital built up by banks for periods of economic stress,
- Reducing the minimum liquidity coverage ratio requirement from 100% to 80%,
- Amending a Directive whereby loans that were restructured as a result of the impact on COVID-19 will not attract a higher capital charge relating to the resultant credit exposures,
- Guidance to the banking sector on factors to consider in accounting for and calculating the expected credit losses over its business cycle during this time and,
- Guidance with recommendations for payment of bonuses for material risk takers and executives; and the distribution of dividends on ordinary shares.

Fiscal Policy Responses

Government concurrently responded to the pandemic in a phased manner:

Phase 1 aimed to preserve the economy through a set of immediate, targeted and temporary responses. The measures were directed at mitigating the effects of the pandemic on businesses, on communities and on individuals and included inter alia, tax relief, the release of disaster relief funds, emergency procurement, wage support through the UIF and funding to small businesses.

Phase 2 aimed at stabilising the economy by addressing the extreme decline in supply and demand and protecting jobs. In this regard the President announced social and economic support packages to redirect resources to fund the health response to the pandemic, provide direct support to households and individuals for the relief of social distress and provide assistance to companies in distress to protect jobs by supporting workers' wages.

Phase 3 focused on positioning the economy for the higher growth trajectory needed to restore the country's long-term prosperity. Central to the recovery strategy are measures to stimulate demand and supply through interventions such as a substantial infrastructure build programme, the speedy implementation of economic reforms, and other efforts to ignite inclusive economic growth.

On July 27, 2020 the IMF approved emergency assistance under the Rapid Financing Instrument (RFI) equivalent to USD 4.3 billion to South Africa which will be used to address the financing constraints currently faced by the fiscal authorities in addressing the effects of the pandemic.

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