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Who is Following the Money? COVID-19 Stimulus Programs and Oversight in Latin America

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As Latin American governments implement stimulus packages and tax relief programs to combat COVID 19, FTI Consulting is launching a series of articles – Who is Following the Money? – to analyze the structure and potential effectiveness of oversight protections accompanying these programs. The previous piece analyzed Brazil. This article takes a look at Mexico, with a review of Colombia up next.

Introduction

The impact of COVID-19 on Latin America is coming sharply into focus. The health consequences are devastating, with 1,083,341 and 180,545 confirmed cases in Brazil and Mexico, respectively, as of June 21, 2020. There is an expected upward trend in the number of cases across the entire region. The economic impact is also crystallizing. A recent IMF forecast estimated that the global economy will shrink by 3.0 percent in 2020, with Latin America contracting by 5.2 percent. This crisis is expected to plunge 29 million Latin Americans into poverty. In response, governments across Latin America have proposed a range of emergency funding and stimulus packages to bolster their fragile economies, already weakened by depressed global demand, low commodity prices and decreased foreign direct investment.

Concerns over oversight remain highly relevant, as Latin America has long been plagued by wasteful and corrupt spending. In the region, 18 former presidents or vice-presidents have been involved in recent corruption scandals. And now, in a time of crisis, we remain concerned that government action requiring nimbleness and speed may trample oversight. Checks and balances to ensure spending to designated recipients in authorized amounts may be criticized as slow, bureaucratic and cumbersome. Importantly, these attacks may be leveled by populist presidents in the region with immediate needs to prop up health delivery systems, national economies and safeguard their own political survival.

But watchdogs are critical for a number of reasons salient to our clients and their operations in the region:

- First, for many multinationals, it is important to ensure full compliance with any funds received and the proper application of tax benefits granted under stimulus programs.
- Second, transparency matters because of basic trust in government. According to Latinobarómetro, support for democracy in Latin America has fallen from 61 percent in 2010 to 48 percent in 2018. Inefficient, corrupt government spending further undermines faith in the ability of governments to address societal ills and, ultimately, democracy itself.
- Finally, the success of stimulus programs may be outcome determinative, either buttressing health care systems to benefit patients directly or mitigating the economic and humanitarian impact of stay-at-home measures in a region where over half of workers are engaged in the informal economy. No matter the outcome, a central question remains: will the stimulus benefits be distributed broadly or limited to certain powerful, connected players that have long benefitted from close ties to the state?

In this piece, we take a look at Mexico's response to the pandemic and accompanying oversight protections.

Mexico

The Plans

In response to COVID-19, the Mexican federal government has announced a series of measures, including:

— On April 3, President López Obrador canceled the distribution of funds from 281 public trusts (fideicomisos públicos) worth more than USD$10 billion and ordered the money be redirected to the Federal Treasury for use in social programs, economic recovery and credit lending, support for Pemex, and public debt payments. Although the precise distribution of these resources has not been disclosed, President López Obrador has provided preliminary details on his plans in recent statements, with money to be spent by the Federal Treasury and, in the specific case of credit lending, resources to be managed by the Mexican Institute of Social Security (IMSS). But many details remain unclear.

— On April 13, the IMSS announced that companies can defer their payroll health and social security taxes for up to 48 months.

— On April 16, Zoé Robledo, head of the IMSS, provided details about the distribution of approximately USD$1 billion in credits to small businesses that have not dismissed any employees or cut salaries during the crisis. This extension of credit will be offered at rates ranging from 6.5 percent to 10 percent (depending on each company's number of employees) over 36 months with an initial three-month grace period. This measure has been criticized as insufficient as it intends to grant only USD$1,000 to one million businesses. The Ministry of Economy reported that, as of June 12, the IMSS had delivered 191,000 of these "solidary credits."

— On April 21, Mexico's Central Bank announced a USD$31 billion stimulus package and cut its benchmark interest rate by 50 basis points. According to the Central Bank, the measures were implemented to "foster an orderly behavior of financial markets, strengthen credit channels and provide liquidity for the sound development of the financial system." The package amounts to approximately 3.3 percent of Mexico's GDP in 2019. The Central Bank stated that around USD$10.3 billion of the total amount would be directed to commercial and development banks to boost lending to individuals and small and medium-sized businesses.

— On April 22, President López Obrador announced an 11-point economic plan which includes measures such as 25 percent pay cuts for high-level public officials, the distribution of USD$3 billion in credits for small businesses, and the elimination of 10 deputy minister offices. The president did not specify if these credits are independent or in addition to the USD$1 billion announced on April 16. Moreover, President López Obrador reiterated his administration's commitment to austerity, while continuing with major infrastructure projects such as a refinery, an airport and a tourist train, as noted below.

— On May 13, President López Obrador announced the details of a plan to gradually resume social and economic activities starting on June 1. The plan follows a "stoplight" system, establishing four reopening degrees that vary geographically according to the prevalence of active COVID-19 cases. In red areas, only essential economic activities will continue operating. Areas coded yellow will restart 30 percent of their non-essential economic activities, and a complete reopening of the economy will occur in the green zone. Through June 15, approximately half of the country's states were coded orange, with the other half remaining red. Importantly, Mexico City remains a "red" area.

- On May 13, Mexico City's local government announced that it would couple the reopening measures with an economic stimulus package directed to vulnerable populations (defined by low-income or prevalence of COVID-19 comorbidities). The package provides monthly payments of USD$100, and the plan estimates a monthly minimum of 100,000 payments, which will be made directly through ATMs. The total cost of the scheme, which would be in place for three months starting on June 1, is estimated at USD$31 million.
- On June 7, Mexico took out a USD$1 billion loan from the World Bank's Development Policy Operations program. Although the government promptly clarified that the loan was not contracted for COVID-19 relief purposes specifically, it came at a time when, as a consequence of the pandemic, the country is registering record-setting job losses, a steep decline in industrial activity and a predicted GDP contraction ranging from 4.6 to 8.8 percent, according to Mexico's Central Bank.

Importantly, aside from the Central Bank's stimulus package announced in April (which was designed to stabilize the financial system) and the USD$1 billion World Bank loan announced in June, the Mexican government's economic relief measures are not targeting any large private sector organizations or any specific industry. Additionally, President López Obrador has been criticized for moving forward with his administration's flagship infrastructure projects — the Dos Bocas Refinery, Santa Lucía Airport, and Maya Tourist Train— while continuing to face opposition demanding the suspension or even cancellation of these projects. In response, the Business Coordinating Council (CCE), a conglomerate of industry groups, proposed an economic plan of its own, calling for a "national deal" with unions, companies, and civil society to preserve jobs. However, the CCE did not follow up on the proposal and ultimately reversed course, publicly approving of the measures adopted by the Central Bank on April 21.

The Oversight

The credits for small businesses will be managed by the Mexican Institute of Social Security and, as every other public spending program, will be audited by the Chief Audit Office (ASF) and the Ministry of Public Administration (SFP). In addition, the heads of the Banco Azteca and Banorte banks (and the Spain-based head of Santander) offered to oversee the commission-free distribution of the government's credits. On April 8, President López Obrador confirmed that the distribution would be carried out by the three banks, which would receive around USD$332 million each to start distributing on May 4.

The Concerns

In Mexico, the key concern around misuse of funds centers around the diversion of public resources for electoral objectives. The significant new governmental spending may create opportunities for additional abuse and reinforce existing disenchantment among Mexican citizens.

For example, the credit program for the COVID-19 response will be available only to businesses listed in the Welfare Census registry, which is used for the delivery of some of the current administration's social programs and has been criticized for its lack of transparency and its alleged clientelism. Concerns over electoral abuse have been accelerated since President López Obrador stated that credits would be granted through minimal bureaucratic procedures to expedite their distribution, which would potentially reduce the transparency and accountability of the program. According to data presented by the federal government in late May, loans with such characteristics account for more than 60 percent of the 4 million credits the federal government expects to grant during 2020.

Other areas of concern have also bubbled up. On April 13, an investigation revealed that the Ministry of Defense purchased 1,330 ventilators for approximately USD$56 million from a company partially owned by José María Tapia Franco. Mr. Tapia Franco is a former official with the Ministry of the Interior and also worked as a campaign manager for José Antonio Meade (the PRI presidential candidate in 2019). Two other former officials with the Ministry of the Interior and collaborators of Mr. Tapia Franco are listed as shareholders of the company. Moreover, an independent investigation by watchdog organization MCCI published in early June pointed out that during 2019 direct contract awards (as opposed to transparent public biddings) accounted for 78 percent of the federal government purchases, the highest percentage in nearly a decade.

Likewise, the IMSS topped the list of directly awarded government purchases in 2019, with almost 40,000 orders. Direct contract awards, which sidestep the more rigorous public bidding processes, raise concerns about directing contracts to favored providers.

In early May, a group of well-regarded civil society organizations (Impunidad Cero, Justicia Justa, Tojil and Transparencia Mexicana) issued a joint press release pointing out the need for tougher oversight and auditing of government purchases amid the acquisition of goods and services related to the COVID-19 relief efforts. According to the group, public spending related to the relief efforts (at the federal and state levels) amount to approximately USD$26 billion. In Mexico City alone, the local government will spend around USD$130 million, most of which is delivered through direct transfers that lack any kind of accountability or effective evaluation measures.

Conclusion

Oversight concerns in Mexico remain anchored in the potential misuse of funds and diversion of public resources for electoral objectives. Previous crises, such as the earthquake that hit central Mexico in 2017, have proven to be fertile ground for such abuse, and the magnitude of the pandemic and of the government's relief measures only increases the incentives for an opaque handling of public resources. Moreover, the lack of clear criteria for the delivery of economic support and the use of the Welfare Census (widely criticized for its potential clientelist objectives) in COVID-19 relief measures remain causes for concern.

Recent worries expressed by civil society do little to ameliorate those longstanding doubts around public spending in Mexico. We will update our views on Mexico's performance periodically as part of this series.

Next Up? Colombia

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