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FINANCIAL LESSONS FROM THE PANDEMIC

Impact of Economies

In many countries, the COVID-19 pandemic and the restrictive measures adopted by governments worldwide to curb its impact resulted in a steep economic toll alongside the tragic human capital cost.

In the June 2020 *World Economic Outlook Update*, the International Monetary Fund (IMF) downgraded its global growth projections to –4.9% for 2020 from its April 2020 forecast of -3.0% i.e. 1.9 percentage points lower as the COVID-19 pandemic has more negatively impacted economic activity in the first half of 2020 than previously anticipated. In addition, the IMF also projected a more gradual recovery than previously forecast as 2021 global growth is now projected at 5.4%, which overall is 6.5 percentage points lower than the pre-COVID-19 projection indicated in January 2020.

Focusing specifically on Latin America and the Caribbean, the IMF also projected that these regions would experience a deep decline in their economies this year with an average fall of -9.4%, which is 4.2 percentage points lower than the April forecast. On the other hand, the IMF projections for 2021 increased by 0.3% from the April forecast as it expects the region to rebound by 3.7%.

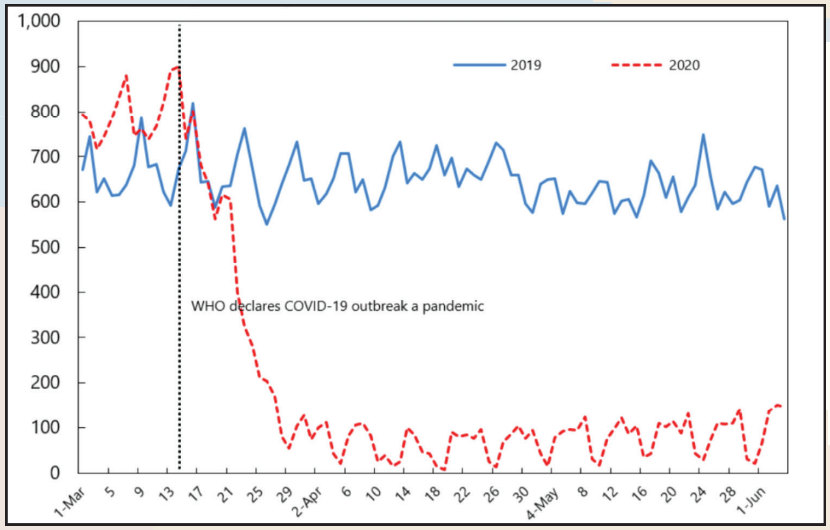
The IMF stated that even though Caribbean economies have managed to flatten the COVID-19 curve, their key lifelines have collapsed. With tourism coming to a virtual standstill and key source markets in advanced economies plunging into deeper recession, the region is likely to experience a very sharp and protracted contraction in economic activity. The lack of tourism is highlighted in Figure 1 which shows the drastic decline in the number of flights arriving in the Caribbean since the World Health Organization (WHO) declared COVID-19 a pandemic.

However, despite downgrading many territories, in its June report, the IMF's projection for the Trinidad & Tobago economy remained unchanged as it forecast a decline of -4.5% for 2020 and growth to rebound in 2021 to 2.6%. However, the Minister of Finance, Colm Imbert, in his mid-year budget review in June, stated that the decline for 2020 was expected at -2.4% which would be followed by accelerated growth of 4.7% in 2021.

Impact on Households

The impact of COVID-19 was not only restricted to the world's economies and no one could have predicted with certainty how quickly the COVID-19 pandemic would have drastically impacted the daily lives of people all over the world. One can always learn one or two financial lessons from any situation and the pandemic is no exception. As COVID-19 rapidly slowed the economy disrupting many businesses and jobs, the importance of an emergency fund became extremely apparent.

Figure 1: Number of Flights Arriving in the Caribbean

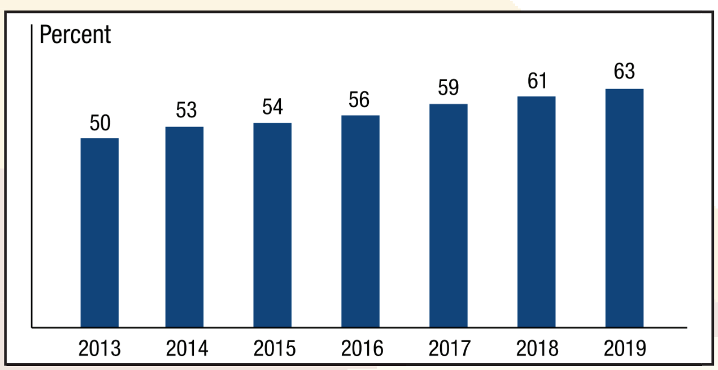


Source: International Monetary Fund

The US Federal Reserve report on the Economic Well-Being of US Households in 2019 published in May 2020 found that many adults were not well prepared to withstand even small financial disruptions in 2019, though the ability to handle unexpected expenses had improved markedly since 2013.

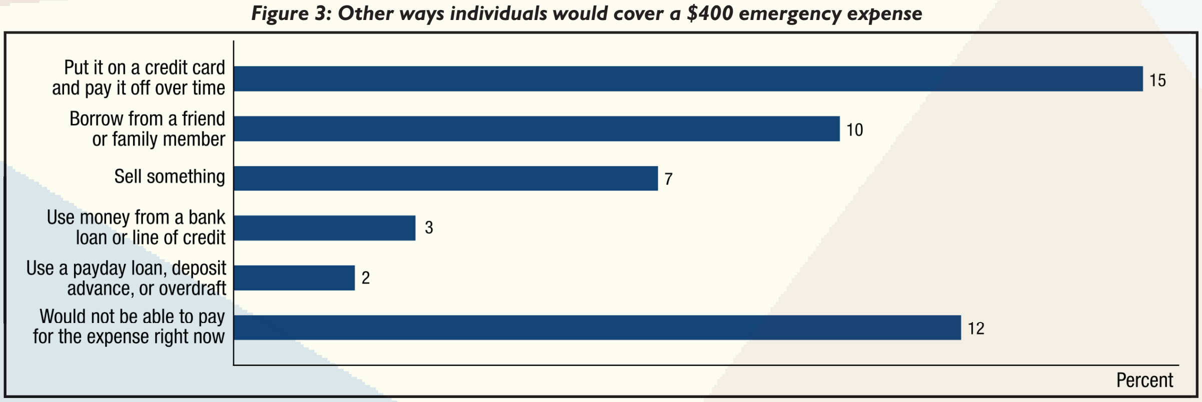
Figure 2 shows that in 2019, 63% of adults stated they would cover a hypothetical expense of US$400 exclusively using cash or its equivalent up from 50% in 2013. The remaining persons stated they would have had more difficulty covering such an expense. Figure 3 illustrates that the most common approach was to pay for the expense using a credit card and then carry a balance while 12% stated that they would be unable to pay the expense by any means.

Figure 2: Would cover a $400 emergency expense completely using cash or its equivalent (by survey year)



Source: US Federal Reserve Report on the Economic Well-Being of US Households in 2019 - May 2020

Figure 3: Other ways individuals would cover a $400 emergency expense



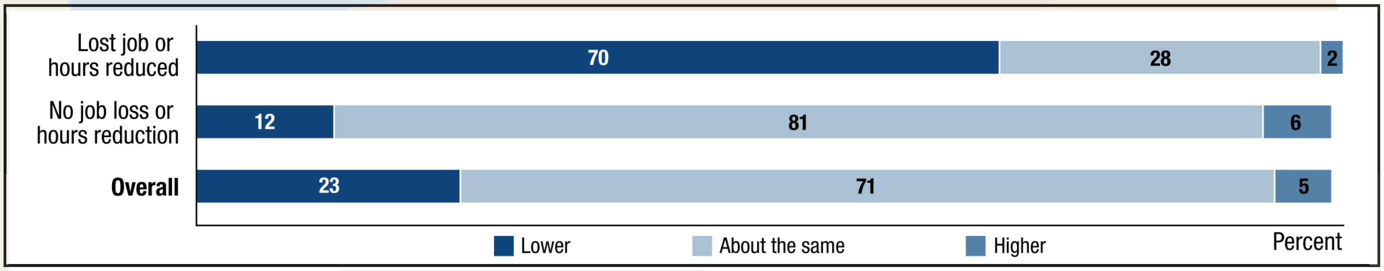
Source: US Federal Reserve Report on the Economic Well-Being of US Households in 2019 - May 2020

Note: Respondents could select multiple answers

The report also looked at some of the financial repercussions from COVID-19 and stated that from the start of March through early April 2020, 19% of adults reported losing a job, being furloughed, or having their hours reduced. These job losses were most severe among workers with lower incomes.

Consistent with March's employment declines, many people experienced reduced income. Figure 4 shows that 23% of adults overall stated that their income in March was lower than in February, while 5% said their income increased and the rest indicated it was about the same. However, amongst those who lost a job or had their hours reduced, 70% reported that their income declined.

Figure 4: Income in March 2020 Relative to February (by employment disruptions since March 1)



Source: US Federal Reserve Report on the Economic Well-Being of US Households in 2019 - May 2020

Note: Respondents could select multiple answers

Impact on Companies

HRC Associates conducted surveys on the local and regional impact of the COVID-19 pandemic which provided the following insights into concerns and expectations as it relates to the pandemic.

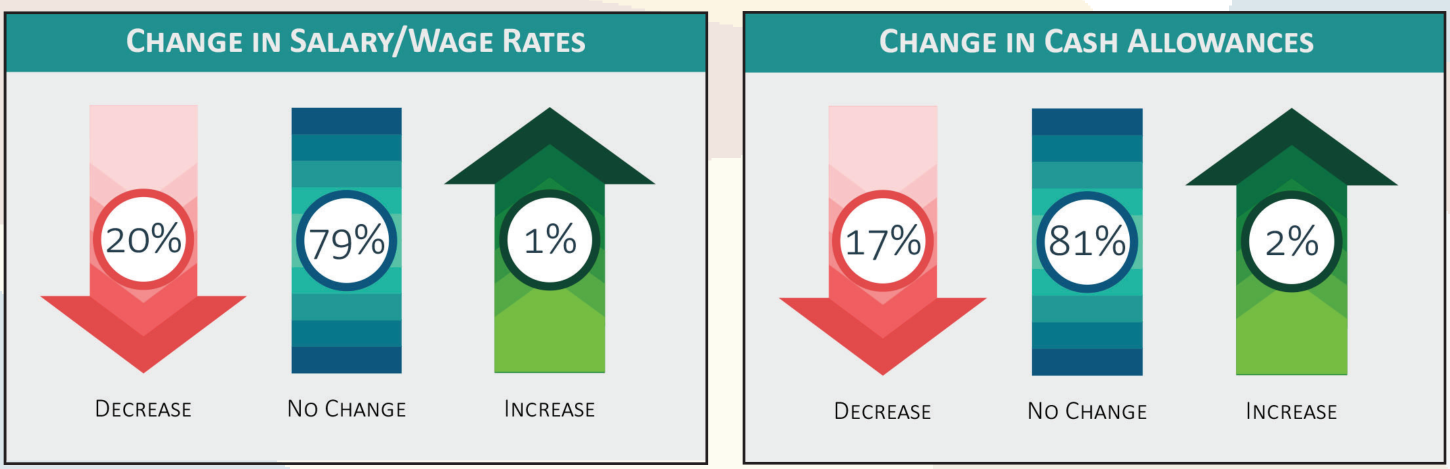
The survey conducted in April centered around CEO's concerns and expectations and stated that 83% of the organisations surveyed were experiencing a decrease in consumer spending and demand and as a result, 76% of executives expected that there would be a decrease in projected 2020 revenues.

In contrast, the May survey focused on the employee's perspective and surveyed just under 2,500 persons. Since the beginning of the pandemic, 88% were still employed, 8% were temporarily laid off, and 4% were retrenched. However, the majority, 74%, of persons still employed were at least somewhat concerned about job security.

The executive survey highlighted the fact that 91% were implementing some form of cost containment measures to better manage cash flow and safeguard their organisation's financial position along with reviewing their HR strategy to optimise workforce capacity and productivity. One such measure would be to reduce employees' salaries. However, 79% of employees surveyed stated that there had been no change to their salary/wage rate and 81% indicated that there was no change to their cash allowances.

Additionally, from the April survey, 55% of Executives anticipated that a reduction in total employee work hours would continue or become necessary. This was seen in the employee survey as 34% of persons who were still employed had their work hours decreased but at the same time, 24% reported increased hours.

Figure 5: Change in Salary/Wage Rate and Change in Hours of Work



Source: HRC Associates - COVID-19 Survey: The Employee Perspective

A major takeaway from the pandemic is that emergencies can happen at any moment and without notice, but that does not cause expenses to automatically disappear. It is therefore important to have a dependable source of liquidity in facing the unknown because even those with seemingly reliable income streams are not immune from income disruptions.

Lessons/Strategies in withstanding the Impact of the Pandemic

It has been extremely challenging for both individuals and businesses alike to successfully manage their financials during the lockdown period with the general uncertainties, especially around revenue, in this rapidly evolving global financial environment.

At an individual level, it became enormously apparent that an emergency fund is a critical component to any financial plan as it acts as the first line of defence and can provide some much-needed security in times of uncertainty as it creates a financial buffer. Having a liquid emergency fund to rely on if an unpredictable, catastrophic event occurs is imperative in surviving the aftermath, especially if there is household debt because it can help avoid borrowing more.

It can sometimes be tricky to figure out exactly how much money should be set aside in an emergency fund. There are varying opinions amongst experts, and it can range anywhere between three months to a year of expenses or even income. It is essential to understand that what works for one person may not necessarily be the best option for all as it is strongly associated with personality – what one person considers a comfortable safety net may feel like an inefficient over or under allocation of cash to the next person.

The ideal location for an emergency fund is a savings account with a relatively high interest rate and easy access. This account, however, should be separate from the day-to-day account so that there is no temptation to use reserves for non-emergency needs.

An emergency fund is also extremely essential for businesses. Despite the fact that businesses tend to have more assets than you would hold in your personal capacity, very few of those assets are liquid and would not be very helpful during a financial dilemma.

The term emergency fund is not reported on a company's balance sheet, but one can consider the company's retained earnings. Retained earnings are the profits retained, or held back, from the shareholders and not paid out as dividends, it is redistributed into the business and can either be used to invest or pay off debt. However, it can also come in handy as it is a supply of cash that will enable your business to continue operating in lean times or an emergency. These funds allow your business to keep providing services while making payroll, paying bills, and purchasing supplies. This buffer also decreases the likelihood of the company increasing its debt burden.

Similar to personal emergency funds, the amount that is placed aside for emergencies will determine if a company has the wherewithal to respond to bumps in the economy – or big, unexpected expenses – without falling behind on bills or resorting to measures such as discounting to generate cash or employee layoffs to slash expenses.

Businesses throughout various life cycle phases have felt the impact of COVID-19. Unfortunately, startups or smaller businesses would have borne the brunt of it as they have scarcer cash reserves and have a smaller margin for managing sudden slumps. Unsurprisingly, organisations that were furthest along the digital transformation journey appeared to have adapted better than their peers as they were able to pivot and make necessary adjustments to their business models.

Nevertheless, they have all to relook their operating policies and procedures to adjust to the new normal. During uncertain times, such as these, there are many things out of your control, but there are steps which can be taken to help prevent organisations from becoming financially crippled. Experts have recommended the following:

- **Tracking expenses versus revenue**
  It is essential to conduct a proper assessment of the expenses, both fixed and variable, as well as the actual revenue streams. This will provide a clear picture of the company's financial position and help keep track of crucial financial metrics.
- **Checking the feasibility of the business model**
  Considering the volatile nature of market, it is imperative that companies reconsider their business model and reassess and revise any assumptions concerning revenue and cost as well as reevaluate the impact of sales, collections, credit cycles and any potential bad debts.
- **Plan policies for next 3 months/ 9 months/ 18 months**
  It will be quite difficult to gauge the extent and the length of the effect of the pandemic, but companies need to be prepared for all scenarios. In the short term, i.e. 3 months, measures such as halting variable expenditures such as travel can be implemented. If however, the crisis continues for 9 months to a year, a business may need to further reevaluate and reconfigure

their strategy as well as an additional reduction in variable expenses alongside possible renegotiation of fixed expenses (e.g. rent, salaries, equipment lease payments, etc.), and focus only on the crucial essentials for survival. If it continues for even longer, serious considerations around amendments to the operating plan may be necessary.

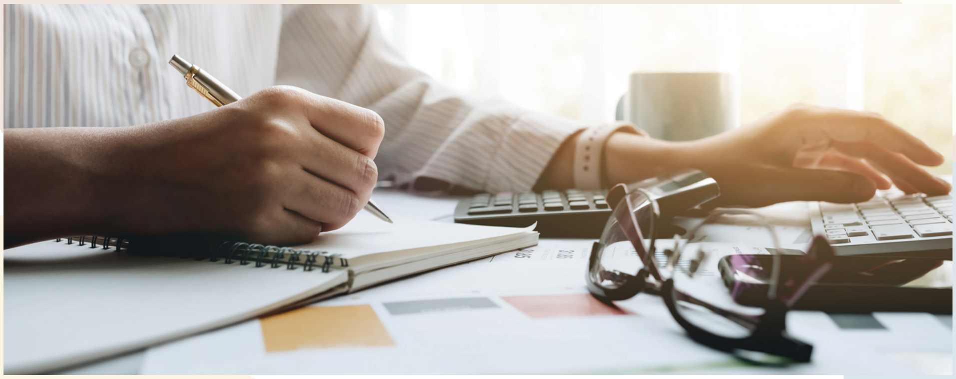
- **Embrace the cultural and behavioural shift**
  It has been seen that technology has emerged as the common denominator for many organisations' resilience amid the crisis. The availability and accessibility of online sales and services which were already experiencing rapid growth was further accelerated as a result of the pandemic.

Also apparent were significant cultural shifts, such as people working from home and connecting with colleagues via video-conferencing platforms and collaboration tools. Organisations have a valuable opportunity to capitalise on the transformation and adjust their business model and improve their digital capacity.

Investment Checklist

Many times, investors ignore their financial advisor's guidance to build an emergency fund as they are mainly focused on investing in their long-term financial goals. However, an emergency fund can help you to continue to contribute to your financial goals if you are experiencing any temporary loss of income.

It would have been ideal to start an emergency fund when you had a consistent income stream so that deposits became habitual and withdrawals were few and far between. However, the following steps can help you to build your emergency fund at any time.



1. **Formulate a plan**
   Firstly, you need to determine how much money you feel comfortable having as a cushion in an emergency. Ideally, it should be no less than three months' expenses. Then you need to disaggregate it into an affordable monthly savings goal that fits within your budget. This will make the task more attainable.

2. **Automate your savings**
   It can be quite easy for the money that was originally set aside to be spent on other competing expenses, especially during these times. In order to remove that temptation, set up to have your savings automatically transferred into your emergency fund.

3. **Use only for emergencies**
   You may be tempted to dip into your emergency fund for a variety of reasons but if you continuously keep depleting the fund for everyday life expenses, it will not available when really need it. It is essential when you are setting up your fund, to predetermine what type of known expenses the money can be used for along with the unexpected ones.

4. **Assess and adjust contributions**
   As with everything in financial planning, it may be necessary to make adjustments to your plan as your financial situation changes. Just remember that having a reserve can mean the difference between weathering a short-term financial storm or going deep into debt.

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