THE ECONOMIES OF LATIN AMERICA AND THE CARIBBEAN: SITUATION AND PROSPECTS

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Regional GDP was up by 4.6% in 2008, completing a sixth consecutive year of economic growth.

The Latin American and Caribbean region’s per capita GDP grew by more than 3% for the fifth year in a row.
Higher growth rates, lower unemployment and better-quality jobs have helped improve poverty indicators.
IN 2008, POVERTY LEVELS DECREASED SLIGHTLY, BUT NO REDUCTION WAS SEEN IN INDIGENCE...
The economies of the developed countries are showing clear signs of deterioration

Although indicators have yet to fully reflect the impact of the post-Lehman crisis, they already show a sharp drop in demand caused by the combination of:

- Wealth effect (housing and equity values)
- Job destruction and the rise in unemployment
- Tighter credit
- These factors generate negative expectations, which then cause the situation to deteriorate further (vicious cycle)
The developed countries have entered a recession.
The international crisis is being transmitted to the region through various channels, though not to the same extent in all the countries.

One by one, the engines of growth are shutting down:

- **The real-economy channel**
  - Slowdown in exports
The slowdown of the developed economies will have a negative impact on trade flows.
The international crisis is being transmitted to the region through various channels, though not to the same extent in all the countries.

One by one, the engines of growth are shutting down.

- The real-economy channel
  - Slowdown in exports
  - Falling commodity prices
Commodity prices are falling but they may remain relatively high
The region’s terms of trade continued to improve in 2008 but are expected to worsen in 2009.
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One by one, the engines of growth are shutting down.

- The real-economy channel
  - Slowdown in exports
  - Falling commodity prices
  - Lower remittances
Remittances are very important, especially in the Caribbean and Central America
... and in a number of countries they have already begun to decelerate or even decrease.

**REMITTANCES**

*Interannual growth rates (%)*
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- The real-economy channel
  - Slowdown in exports
  - Falling commodity prices
  - Lower remittances
  - Reduced revenues from tourism
The Caribbean and Central America will suffer the most from the expected drop in tourism revenues.
The international crisis is being transmitted to the region through various channels, though not to the same extent in all the countries.

One by one, the engines of growth are shutting down

- The real-economy channel
  - Slowdown in exports
  - Falling commodity prices
  - Lower remittances
  - Reduced revenues from tourism
  - Smaller inflows of foreign direct investment (FDI)
The significance of FDI varies from country to country.

**LATIN AMERICA AND THE CARIBBEAN: NET FOREIGN DIRECT INVESTMENT, 2008**

(Percentages of GDP)

The bar chart shows the net foreign direct investment as a percentage of GDP for various countries in Latin America and the Caribbean for the year 2008.

Countries listed include:
- Antigua and Barbuda
- Grenada
- Saint Vincent and the Grenadines
- Saint Kitts and Nevis
- Dominica
- Belize
- Panama
- Bahamas
- Costa Rica
- Chile
- Peru
- Dominican Republic
- Honduras
- Uruguay
- Nicaragua
- Colombia
- Mexico
- Bolivia
- Guatemala
- Brazil
- Argentina
- Ecuador
- Paraguay
- El Salvador
- Haiti
- Venezuela (Bol. Rep. of)

The percentage values range from -1.2% to 16.0%.
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The real economy
- Slowdown in exports
- Falling commodity prices
- Lower remittances
- Reduced revenues from tourism
- Smaller inflows of foreign direct investment (FDI)

The financial sector
- Higher cost of external credit
Amidst increased volatility, the perceived risk associated with emerging economies is on the rise.

Latin American: EMBI+ spread, 1996-2009
(Basis points, figures for the end of each period)
(First quarter 2009: figure as of end of January)

Risk has increased less than in other crises.
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- Slowdown in exports
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- Reduced revenues from tourism
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The financial sector
- Higher cost of external credit
- Reduced availability of international financing
Reduced availability of foreign exchange resulted in dramatic devaluations in a short space of time.

With a varying impact on competitiveness, balance sheets and inflation.
The region is better prepared than in previous crises, but some indicators are already worsening...
LATIN AMERICA (6 COUNTRIES): BREAKDOWN OF THE VARIATION IN RESERVES, 2005-2008

(Millions of dollars)

Includes Argentina, Brazil, Chile, Colombia, Mexico and Peru.
This crisis, unlike others, has left the private sector with the greatest exposure.

(Percentages of GDP)

- Peru: 7.9% (Private: 9.0%, Public: -1.3%)
- Mexico: 1.2% (Private: 1.2%, Public: -1.4%)
- Colombia: 2.5% (Private: 2.5%, Public: 1.0%)
- Chile: 4.3% (Private: 4.3%, Public: 2.0%)
- Brazil: 3.8% (Private: 3.8%, Public: -1.5%)
- Argentina: 2.0% (Private: 2.0%, Public: -1.5%)

This chart shows the variation in external debt for selected countries in Latin America and the Caribbean, comparing public and private external debt from 2006 to June 2008.
The response capacity to the crisis is also different

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(*) Does not include central bank interventions through sales of foreign exchange on currency markets
The depth and duration of the crisis are still uncertain

- They depend on the effectiveness of measures to boost demand, sectoral policies (in the automobile industry, for instance) and the normalization of the financial markets.
- The measures adopted by the United States Federal Reserve and other central banks are expected to contain systemic risk...
- ... and the worst of the crisis is expected to be over by the end of the second half of 2009.
In 2009, the region’s growth is expected to slow dramatically

The region continues to “fly”, but in glider mode, as the engines of growth have shut down
The deteriorating economic environment will have a negative impact on income distribution

- The slowdown in growth could push up unemployment from 7.5% in 2008 to between 7.8% and 8.1% in 2009.
- Informal employment will rise.
- The rise in unemployment will have a more severe impact on low-income households.
- Rising informal employment will reduce the average income of informal workers.
- The fall in remittances will mainly have an impact on low- and lower-middle-income households.
- Poor households have been the hardest hit by the increase in inflation during 2008 (because of food prices).
Lessons learned

- Countercyclical policies are needed
- Steps should be taken to prevent the crisis from increasing inequity as a result of biased measures
- The countries’ capacity to maintain social spending, especially spending aimed at building human capital, must be safeguarded
- Investment in infrastructure should not be neglected
- Protectionism should be avoided
Global problems require a coordinated solution

- In the recent period, developed countries consumed while emerging economies saved to shield themselves from the effects of a crisis.
- This is no longer feasible in the present climate, and some of the stimulus for demand must come from the developing world.
- However, the resources remain in the hands of developed countries.
- International financial institutions must provide resources to finance countercyclical policies.
The regional dimension is vital...

- Coordinated macroeconomic policies and commitment to integration can leverage strategies.
- Intraregional trade is knowledge-intensive and involves many SMEs, which means it has a greater impact on the production fabric and on employment and equity.
- However, intraregional trade is heavily procyclical and therefore needs to be backstopped by a special financial support strategy.
- Regional financial institutions have an important role to play.
- The regional institutional framework needs to be strengthened.
Beyond the current phase of the cycle

- This crisis opens the way for a reassessment of prevailing economic development paradigms.
- Now is the time to consider a new international financial architecture...
- And a new role for the State:
  - In protecting the most vulnerable sectors to ensure inclusive development
  - In fostering a production fabric that incorporates more knowledge and prioritizes innovation
  - In regulating economic activity so that profit-seeking in the private sector does not conspire against society’s general well-being.
**IN SHORT:**

- Poverty and indigence rates declined by over 9 and 6 percentage points, respectively, between 2003 and 2007.
- Indigence levels rose in 2008, and both poverty and indigence rates will climb in 2009.
- The effects of the crisis will differ from one group to another:
  - Employment levels will fall and unemployment rates will be higher.
  - Jobs in the informal sector will be hurt the most.
  - Real wages and salaries will not rise.
  - The incomes of independent workers will fall.
  - Remittances sent home by migrant workers will decline.
- The impact on groups of countries will differ according to their degree of export diversification (Central America vs South America).
PROMOTING POLICIES TO PREVENT THE EFFECTS OF THE CRISIS FROM BEING SHOULDERED BY LOWER-INCOME SECTORS

- Mitigate the impact of slacker labour demand through public investment in infrastructure
- Expand unemployment insurance coverage
- Maintain current levels of social spending, with emphasis on expenditure to combat child undernutrition, on social assistance and in other areas that will help protect poor and indigent people from the effects of the crisis.

- In the long term, it is extremely important to:
  - Develop new socio-political contracts so that fiscal pacts involving a greater solidarity component can be achieved
  - Establish regional and international strategies for curtailing the deterioration of the real economy.
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