

Fact Sheet

Economic Survey of Latin America and the Caribbean 2012:

The Countries of the Region Have Enough Fiscal Space for Facing External Adversity

(2 October 2012) In the last years, Latin America and the Caribbean has coped with three different kinds of adverse external shocks, which the region addressed through a number of policies and measures. This adversity has mainly translated into volatility – both regarding economic growth and investment (see the attached graph). Based on the experience gained since the policies applied between 2008 and 2009, the region learned important lessons that allow facing current turbulences with several advantages.

The [*Economic Survey of Latin America and the Caribbean 2012*](#), presented today by **ECLAC**, shows the measures adopted by the countries between 2008 and 2012, as well as future challenges linked to the region's macroeconomic policy.

The three main difficulties that the region has seen are 1) the increase of food and fuel prices in 2008; 2) the world financial crisis, having its hardest consequences between september 2008 and the end of 2009; and 3) internacional uncertainty and the world economic slowdown from the second half of 2011.

The countries' response has mainly included the adoption of a countercyclical fiscal policy. Between 2003 and 2008, the fiscal policy focused on the generation of primary surpluses and the reduction of national debt. Also in that period, countries sought to redirect expenses and taxes in order to avoid the counterproductive effects of price increases. In 2009, public expenses increased to stabilize internal demand and, as of 2010, several tax reforms were made for consolidating public finance.

The survey states that difficulties coming up between 2008 and 2012 were faced through a) a combination of restrictive monetary policies and currency appreciation against food and fuel price increases in 2008; b) an increase in liquidity, a reduction in the reference interest rate and currency depreciation during the world financial crisis in 2009; and c) a cautious performance since the second semester of 2011 until today.

Labour and social policies were strengthened during the most intense period of the crisis, between 2008 and 2009, through measures such as temporary tax reductions, employer contributions, transfers, subsidies, increases in minimum wages, training programmes, temporary enhancement of pensions, programmes for food and social housing support, as well as bonds for vulnerable people or households.

Concerning trade and sectoral policies, tariffs were reduced and the agriculture sector was provided with support in 2008. In 2009, there was a temporary reduction in taxes and financial incentives for housing and small and medium-sized enterprises, whereas in 2011 and 2012, the industry sector has been granted incentives and protection.

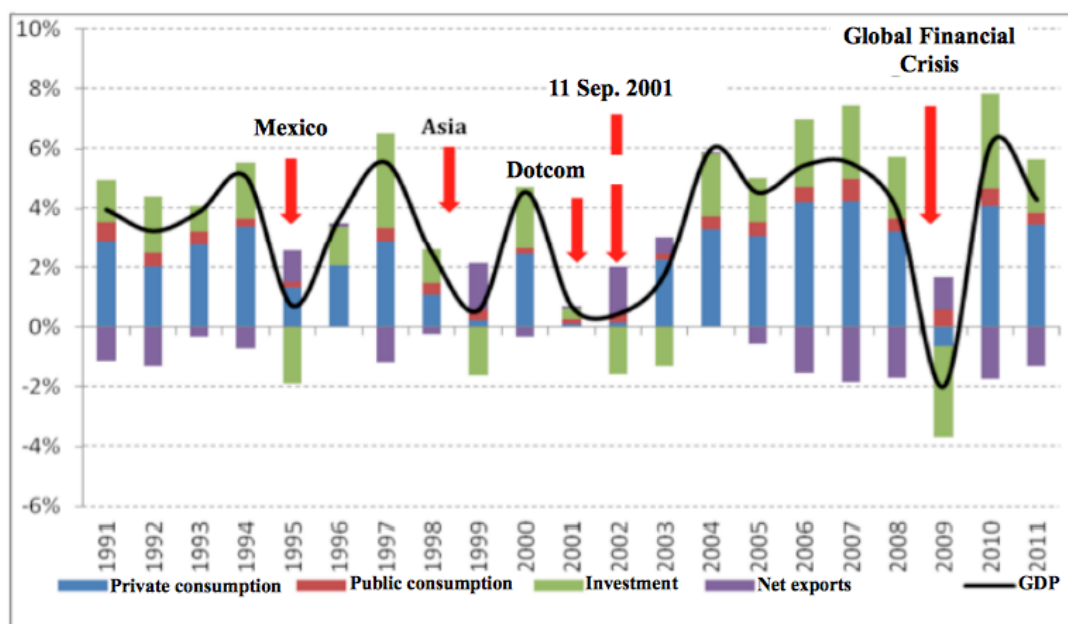
In the report, **ECLAC** shows that investment in the region has been vulnerable to external shocks. Likewise, it elaborates on future challenges for the region's macroeconomic policy to contribute to development, investment and employment.

In order to address these challenges, the survey presents six lessons learned from the region's experience when facing adverse external scenarios: 1) before leveraging the fiscal space resulting from the intense impairment of external demand, the limitations of a countercyclical fiscal policy must be identified in an extended growth scenario; 2) it is convenient to strengthen (before instability and inequality) automatic fiscal stabilizers, such as broad-based and progressive taxes; 3) it is advisable to establish automatic fiscal standards for deficit adjustment only if fiscal strength is guaranteed in a context of financially sound subnational governments, budgetary flexibility and a fiscal covenant ensuring that standards are observed; 4) labour policy must be coordinated with fiscal policy in order to avoid that contradictions in domestic consumption have a negative impact in growth and income distribution; 5) it is justified to

implement macroprudential measures and reserve management measures for managing capital accounts and stabilizing currencies; and 6) it is convenient to integrate a stabilizing policy into other policies that influence external supply and demand, such as industrial, labour, financial and trade policies.

With only a few exceptions – especially in the Caribbean and some Central American countries, the governments of the region have fiscal space for facing adverse scenarios, as claimed by **ECLAC**. The Organization adds that there are financial cooperation actions that could enhance national efforts, such as the countercyclical action of development banks, the reduction of insurance costs by using reserve funds, payment systems that reduce transaction costs and dialogue and information exchange spaces.

LATIN AMERICA AND THE CARIBBEAN: GDP VARIATION RATE AND CONTRIBUTION TO AGGREGATED DEMAND COMPONENTS
(in constant Dollars from 2005, percentages, estimate averages)



Source: The Economic Commission for Latin America and the Caribbean (ECLAC) based on official figures.