Latin America and the world towards the year 2000

*Miguel de la Madrid**

This is a shortened version of an address delivered by former President Miguel de la Madrid at the Conference on the Opportunities for Canada and Latin America of May 6th 1991, at the University of Calgary, Alberta, Canada. After speaking about Latin America's "lost decade" -the 1980's- he goes on to suggest what is needed now and in the year 2000.

The lost decade

For Latin America, the 1980's were a decade with a double meaning: the worst crisis the region had experienced in recent years (people speak of the *lost decade* because of the drastic drop in standards of living and the decline of many of the economic structures) and a structural reorganization of Latin America's economies, societies and states.

The *lost decade* was also one of reform, with the resurgence of democracy in some countries and the beginning of stabilization and adjustament policies, which created new groundwork for other, later phases of development.

Although adjustment policies and structural change are underway, their results vary from country to country; the effort made has yet to show the positive results corresponding to its magnitude. Meanwhile, international conditions have hindered the region's economic progress rather than helping it.

To change this adverse environment into one that favors development, more cooperation from the industrialized countries is needed, since they are Latin America's main creditors and trade partners, as well as the main source of advanced technology and capital resources.

Until the later 1970's, Latin America was a region of accelerated growth, based on a development model that maintained high rates of investment, fueled by state intervention, protected industralization, wide availability of external resources and a favorable exchange rate. This made it possible to improve infrastructure, expand economic activity and exports, create more jobs and raise the general standard of living. We saw accelerated urbanization, a broadening of the middle classes and unequal distribution of development and income.

State intervention in the economy was useful for creating and sustaining new economic activities. However, it meant an over-centralization, leading to inefficiency, stagnation, budget deficits and macro-economic imbalance. Protection raised the social cost of industrial development.

Foreign loans played an important role in economic progress, but they soon exceeded manageable limits and made negative trends still worse. Terms of trade which were positive for decades were finally reserved only for manufactured goods, principally affecting raw materials, Latin America's main exports.

Thus, by the end of the 1970's, the industrialization and growth pattern which had produced a rate of expansion of about 6% annually ever

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since 1950 was exhausted, a dilemma further complicated by the negative economic environment characterized by weakened exchange rates and the shrinking of markets. This meant fewer possibilities of fresh loans. The international financial markets hiked the cost of credit and then halted the flow of resources to the region, plunging it into the debt crisis.

Therefore Latin America entered the 1980's with great domestic and external imbalances; enormous deficits in foreign trade, current account and public finances. Investment dropped, unemployment rose, inflation accelerated, private capital was invested abroad, resources dried up and the servicing of the debt became a huge burden.

The governments of the region drew up adjustment and stabilization policies. Fiscal, monetary and exchange rate measures later led to broader structural change and search for new forms of industrial development and a redefinition of the state's role in the economy.

Imports were restricted and the production of export goods was encouraged. Tariff reforms helped to eliminate quotas and non-tariff barriers. Drastic cuts in the exchange rates helped to turn trade deficits into surpluses.

The public sector made susbstantial cuts in its investment and current spending, state-owned assets were sold off to the private sector, prices of public services were raised and subsidies slashed in order to reduce the budget deficits.

Tax reform brought the system into line with the inflationary processes and made tax evasion more difficult. Exchange rates were set in accordance with the logic of the money markets and interest rate subsidies were gradually eliminated to encourage greater competition in credit markets.

“Adjustment and stabilization policies, followed by structural reform”

The aim of these reforms was to stress competitiveness, enhance the role of the market as a mechanism for assigning resources, reduce the role of the state in the economy and stimulate the private sector as the driving force for growth.

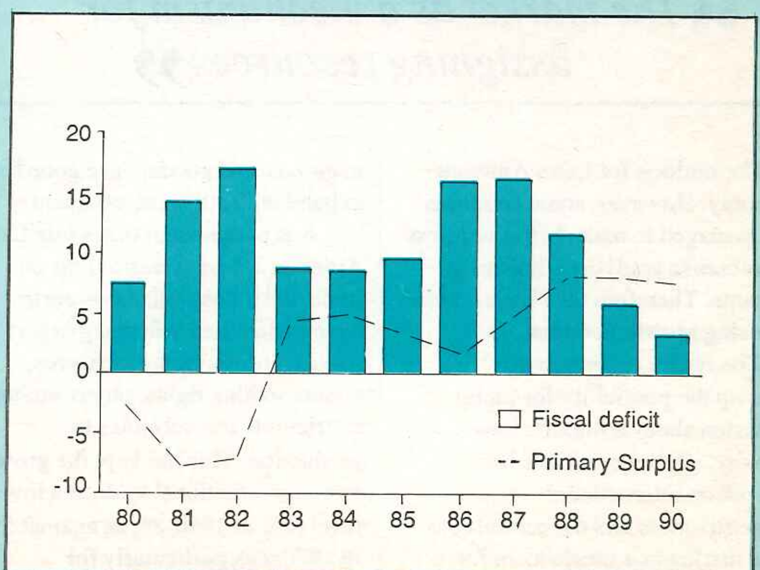
During the 1980's the Latin American economies had very sluggish growth rates of 1.2% annually, in comparison with 5.8% in 1960-1980. At the same time, population grew at an annual average of 2.2%, driving per capita income down more than 10% to its 1977 level.

Real available income experienced a 20% drop in terms of foreign exchange from 1980 to 1989.

Looking at the overall deficit reduction, visible progress was made in 1983 and 1984, but a setback occurred in 1985 due, in part, to unexpected outlays to repair the damage inflicted on Mexico City by the earthquake that hit the country in September. In 1986, further complications arose as a result of the collapse of oil prices in international markets. Together these circumstances produced a loss of hard currency income, equivalent to Mexico's entire agricultural output, and a devastating cutback in oil-related public revenues. Full budgetary control was finally regained in 1988, with the deficit falling to a level 3.5% of GDP by 1990, the lowest level since 1971.

Source: MEXICO: AN ECONOMY ON THE MOVE
Department of Economic Studies
BANAMEX (Banco Nacional de México).

Fiscal deficit and primary surplus
(as a percentage of GDP)



Transfers of funds abroad for the servicing of the debt represented a drain of about 4% of the region's annual global trade.

There was also a severe drop in capital formation. Investment fell from 24% of the gross product in the last half of the 1970's to 16% in 1983-1989.

Many countries are now facing the growing obsolescence of their production plant, decline in physical infrastructure and average standards of well-being.

Real per capita income was negative in 19 out of the 25 Latin American countries in 1981-1989. Structural imbalances and inequality in income distribution worsened and the real minimum wage dropped from an index of 100 in 1980 to 75 in 1989. Thus the number of people living below the poverty line rose to 164 million in 1986 (38% of households, whereas the 1980 figure was 112 million, or 35% of families).

This poverty has not yet been reflected in the basic indicators (life expectancy, illiteracy and infant mortality) because these repercussions always lag behind.

The progress in reducing the burden of Mexico's external debt measured as a ratio to GDP can be closely matched with the behavior described for the fiscal deficit: a gradual reduction from 1983 to 1985, with a major setback in 1986 explained by a deterioration of our terms of trade and a sharp reduction in output. Debt reduction was resumed in 1987 and culminated with the agreement reached between the Mexican government and its foreign commercial creditors in February 1989: the accord amounts to a total of 48.5 billion dollars and entails a relief of the country's external debt equivalent to 15% of the total amount in today's dollars, and additional financing for 1.5 billion to be disbursed between 1990 and 1992. The payment schedule of all credits covered by the agreement has been extended over a period ending by the year 2019. Between 1982 and 1990 the value of the country's external debt at constant dollars dropped 53%.

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Changes around the world

Throughout the last decade, the international context was unfavorable for Latin America and this remains one of the main obstacles for the recovery of growth.

Relationships between the great powers made for instability and uncertainty about the behavior of the world economy. Imports, with different rates for primary and manufactured goods, have gone hand in hand with stiff protectionism.

"The market as a mechanism for assigning resources"

The outlook for Latin America is gloomy. However, some countries have managed to make better progress than others in applying adjustment programs. Therefore they have a more promising growth potential.

The return to democracy opens up the possibility for plural discussion about economic issues. Likewise, greater emphasis has been put on international competitiveness and the central role of the market as a mechanism for assigning funds.

It is paradoxical that while Latin America is easing restrictions on trade, the industrialized countries have maintained voluntary export quotas, anti-dumping measures, countervailing rights, phyto-sanitary restrictions and subsidies to production. This has kept the growth rate of international trade at a low level (3% in 1980-86, as against 5% in 1970-79), particularly for agricultural and manufactured goods from the developing countries which encounter greater trade barriers.

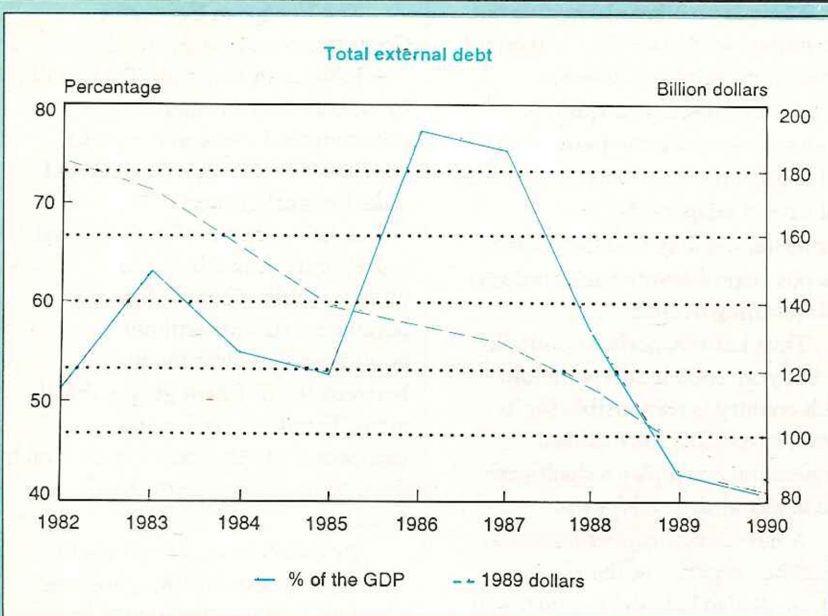
Latin America needs to incorporate more technology into its exports. However, this requires a more favorable attitude on the part of the industrialized countries.

In the sphere of capital movement there is still instability of foreign exchange in the industrialized countries which, with varying rates for the dollar, alters the competitiveness of our exports.

The development of international liquidity fluctuates widely and private and transnational agents do not always respond to development needs, and even less to those of the developing countries.

The fact that the United States is the main debtor nation and the center for direct investment tends to keep interest rates high. The servicing of the debt is therefore more burdensome and discourages investment. The region has become a net exporter of capital since 1982.

Likewise the flow of capital to the region has fallen. Latin America's share in direct investment has dropped substantially since the



beginning of the debt crisis (5.3% in 1986-87 in comparison with 12.5% in 1977-81). Nevertheless, recent developments might either reinforce or counteract such tendencies.

A new technological model, centered on micro-electronics and information, must become a driving economic force, but this requires new forms of labor planning and new conditions for production. In this sense, it may be both a threat and an opportunity for Latin America.

First, a threat to our present comparative advantages, as automation does away with manual labor. Secondly, because new uses for raw materials and the development of new ones affect the volume and price of our exports.

However, increased flexibility of labor offers new opportunities for boosting efficiency and competitiveness and for overcoming the limitations of the domestic market. Computers, in particular, make for more administrative efficiency, while progress in bio-technology opens up a wide range of new horizons. Technological progress is a double-edged weapon for Latin America, as is the end of the cold war and the regionalization of markets.

The end of the East-West conflict has some positive aspects. Discussion may now take place within a framework of political options and no longer be subject to bi-polar tensions. An eventual cut in military spending might free resources for the development of Latin America. On the other hand, a world order based on U.S. military supremacy and the multi-polar division of economic power increases the likelihood of greater U.S. hegemony in the hemisphere, offset perhaps by increased interest in the region's economic recovery.

"164 million people living below the poverty line"

The attitude of a unified Europe will determine whether its markets open up to trade with Latin America, or whether it continues the trend toward relatively isolated economic blocs. The Pacific Rim countries, especially Japan, will also be an important element for aiding or preventing Latin American recovery.

Finally, regionalization and increased competitiveness may enhance Latin America's relative economic importance. However, there remains much uncertainty, and the outcome of external processes will be fundamental in determining how we fare.

Perspectives and needs

The economic recovery of Latin America is still uncertain since our international adjustment efforts remain insufficient and the conditions that gave rise to the crisis are still with us.

For domestic reasons, the region must recover its growth; the world economy too could become more stable and dynamic if Latin America were able to make its contribution.

In 1989 the region's population totalled 422 million (8.75% of the world's population); with an annual growth rate of 1.8% it is projected that by the year 2000 there will be 514 million, twice the number of people in the European Economic Community.

In 1980 Latin America's share in the world product was 7%; due to the crisis this had dropped to under 5% by 1988. Latin American imports and exports accounted for 6% of world trade in 1980, dropping to 3.9% and 3.3% respectively in 1988.

The foreign debt problem calls for an urgent and effective solution. In 1982-1990, Latin America transferred more than $240 billion abroad; in 1990 it had run up a backlog of $11 billion. This cannot continue; adjustment policies are reaching their limit. We need measures to cut the cost of the foreign debt or there will be increasing delays in payment and our countries will no longer be considered credit-worthy.

A reduction in the debt would enable our governments to ease pressure on public finances and control inflation. This would be a more consistent step toward structural change and would put the region back on the path to economic recovery.

There is a need for meaningful changes in the world economy with regard to easing protectionist tendencies, liberalizing trade and renewing flows of productive investment and transfer of technology.

This need for positive changes does not exempt the Latin American nations from proceeding with their adjustment programs and structural reforms. Recent experiences have differed widely from country to country. Unfortunately only a few of them have made substantial progress, while most of them have had to cope with hyperinflation, economic stagnation and deterioration in their social development. The economic crisis is still with us and increases the risk of political instability.

There is no other alternative but to continue with our effort to reorient our economies and undertake structural reforms. The world is heading toward a more intregated and competitive economy. Countries that cannot adapt to the new circumstances may find themselves in a position of severe backwardness and spiralling decline.

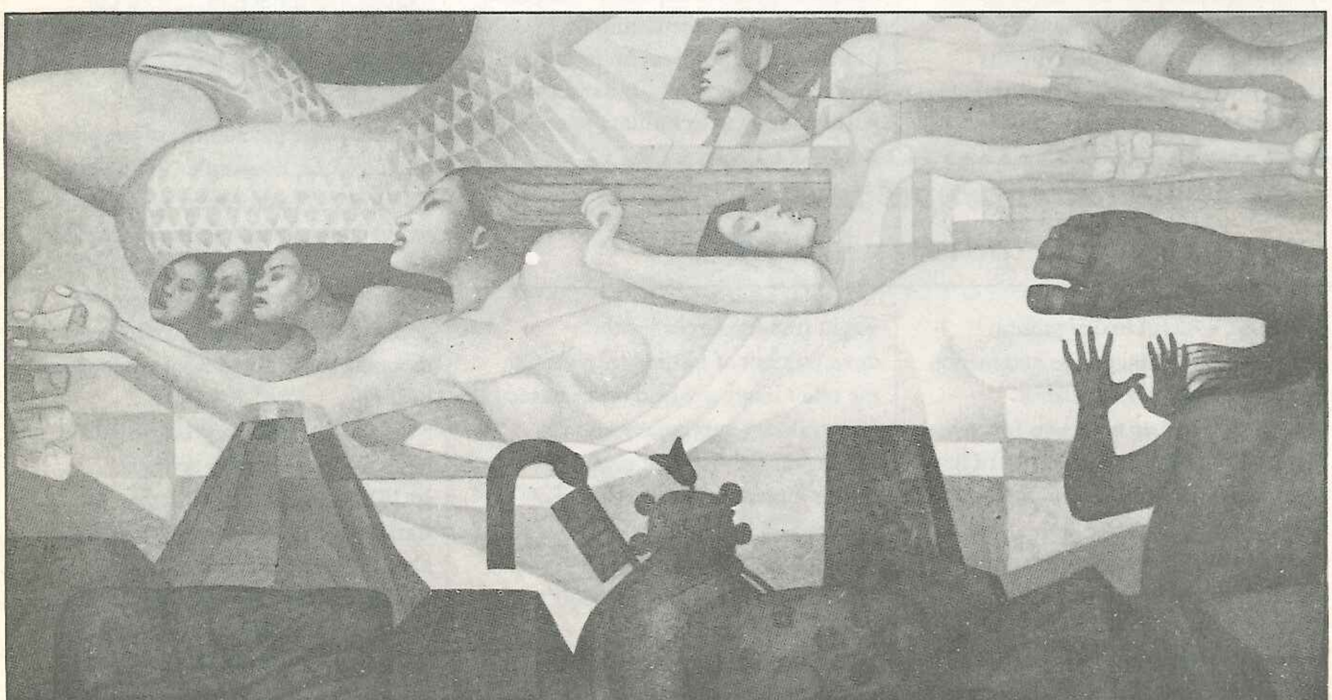
Thus Latin America's outlook for the year 2000 is still uncertain. Each country is responsible for its own recovery, but international cooperation could play a significant role in restoring development.

A new dynamism will not only favor the countries of the region, but it will also help the international economy. Canada and the United States could help us in this effort. The industrialized countries of this hemisphere are interested in having a prosperous, economically sound and politically stable, secure and democratic continent. This calls for a new stage of growth with fairness and productivity.

The European Economic Community and Japan should not overlook Latin America. There will be no benefit from stagnant and impoverished areas, and regional conflicts which create poverty and risks for world peace.

A new scheme of international collaboration has become indispensable. There will be no permanent success without equilibrium and less inequality between the different geographical areas. Freedom, justice and democracy are the values upon which the international system should be founded.

Regional blocs should avoid isolationism and hostility, because these do not favor the new arrangements that are to be introduced. We must strengthen the rule of international law, and our world and regional organizations, aware that the world is home to all of us and that we cannot remain aloof from whatever happens in any region



Jorge González Camarena, Mexican Women.