

The Challenges of Global Economic Insertion for Latin America and the Caribbean

During the 1990s, Latin America and the Caribbean focused not only on recovering from the "lost decade" of the 1980s, but also on establishing new areas of specialization that would enable them to participate successfully in the globalized economy. This shift implied profound changes in economic policy, important institutional adjustments and expensive restructuring programs, all of which had a high social cost. Just when the path toward these transformations seemed clear and several countries, including Mexico and Chile, began to show impressive results, financial vulnerabilities and the realities of market access and unemployment threatened to halt and even reverse the progress.

José Antonio Ocampo, director of the Economic Commission for Latin America and the Caribbean (ECLAC), has synthesized the results of the organization's various research projects on the challenges facing Latin America. Below is a summary of some of his conclusions, along with a few commentaries.

Changes to the Economic Model

The crisis of the 1980s was followed in all countries of the region-albeit a bit later in Brazil and Colombia-by drastic transformations of their commercial and currency regimes under the broader framework of macroeconomic structural reform. The short-term goal was controlling inflation or hyperinflation. This target was met successfully, but the medium to long-term goal was more ambitious: competitive insertion in the global economy.

Average tariff rates in the region fell from 45% in the mid 1980s to 12% in 1999. Tariffs were made more consistent and non-tariff barriers and export subsidies reduced, the latter due to the fiscal crisis. As a result, regional production was abruptly exposed to intense external competition, without favorable microeconomic policies and in the midst of adverse macroeconomic conditions.

The expected positive effects of economic reform never materialized, in spite of the availability of cheaper imports. To the factors mentioned above, Ocampo adds the problem of currency valuation. Latin American exports may have increased in the 1990s, but regional GDP growth was mediocre at best. Imports outpaced exports, increasing the region's external vulnerability.

However, the trend toward regional openness sustained and even deepened the process of commercial and macroeconomic reform. In addition to unilateral trade liberalization, the 1990s were a period of bilateral, multilateral and regional trade agreements in Latin America. Under the framework of the World Trade Organization, four imperfect customs unions emerged, all of them intended to evolve into common markets: MERCOSUR, the Andean Community, the Central American Common Market and CARICOM. All of these blocs are committed to

ensuring trade liberalization, facilitating capital flows and, in some cases, the free movement of persons. In addition, Latin America and the Caribbean have taken on the challenge of hemispheric integration under the Free Trade Area of the Americas (FTAA) by 2005.

Policy Effects and International Specialization

The results of the new economic policies have been uneven and in some cases alarming. Among the problems Ocampo highlights:

1. Between 1990 and 1999, Latin American and Caribbean exports grew by 7.9% annually. At the same time, however, imports grew by 12.1%. Interest rates on the external debt and foreign investment also increased. The net result has been a deterioration in the current account of the balance of payments, especially in the balance of services.
2. Mexico accounted for almost 50% of the region's total exports in the 1990s.
3. Mexico's owed most of its success to exports that incorporate inputs from the United States. The same was true for Central America and the Caribbean, but Mexico developed more links to internal production. All three regions depend on the maquila industry. For Central America, agricultural commodities remain a key export, and tourism has maintained its importance for the Caribbean. In the first half of 2001, reduced US demand has directly affected employment levels in these economies.
4. South America followed a different pattern of specialization that relied on natural resource-heavy primary or industrial exports. South America also developed more diversified intraregional trade and labor-intensive manufacturing exports (and, in the case of Brazil, high-tech exports as well).
5. Panama and other small Caribbean economies specialized in services exports (financial, tourism and transportation).
6. Between 1990 and 1998, trade within subregions grew by an annual rate ranging from 19% (Andean Community) to 22% (MERCOSUR). But in 1999, intraregional trade in Latin America and the Caribbean accounted for only 15.2% of the region's total trade. The equivalent figure for the European Union is 60%.
7. Foreign direct investment in the region took off in the 1990s, growing from \$9 billion in 1990 to \$77 billion in 1999 (dropping to \$57 billion in 2000).

Forty percent of FDI went toward the acquisition of existing (privatized) assets and 60% toward the creation of new assets.

In the last decade, according to Ocampo, national and transnational companies adopted a globalized approach to commercial specialization, taking advantage of macroeconomic incentives and systemic efficiencies within countries to improve their own efficiency.

Two different business strategies seem to have emerged. In the countries further north, US companies invested or formed joint ventures with local firms, especially in Mexico, with production oriented mostly toward the North American market. MERCOSUR followed a second strategy, attempting to defend its control of local markets from global competition. MERCOSUR also took advantage of the privatization of services, infrastructure and extractive industries.

The first strategy boosted exports but did not generate synergies among the economies of the region-as has been achieved in Asia, for example-because it penalized the incorporation of domestic inputs and countries competed to attract FDI.

The second strategy improved efficiency in telecommunications, financial services, electrical energy (before the energy crisis in Brazil), and extractive industries. But transnational companies did not concern themselves with strategic local gains, such as research and development.

A few figures stand out among the many data presented in the ECLAC study. Between 1990 and 1992, for example, of the 500 largest companies in Latin America, foreign-owned companies accounted for 27.4% of total sales, state-owned companies for 33.2%, and privately-owned domestic companies for 39.4%. By 1998-1999, however, foreign-owned companies represented 43.1% of sales, state-owned companies were down to 19.1%, and privately-owned domestic companies held on to 37.2%. In other words, the region's state capital-and, to a lesser degree, its private capital-lost ground to foreign capital. This is another effect of the structural transformations brought about by regional and global pressures.

Even more serious, although Ocampo doesn't mention it explicitly, is Latin America's growing financial vulnerability. Five points stand out. First, external financial cycles have an immediate impact on domestic credit and exchange rates. Examples are the Asian and Russian financial crises, or the current external debt crisis affecting Argentina. Second, external debt and returns on investment are more closely linked than in the past decade to financial margins and government budgets. Third, globalization sets objective limits to national autonomy; in particular, financial vulnerability erodes confidence in the authorities. Fourth, companies react to external vulnerability by reducing their fixed capital investments, leading to unemployment and the destruction of human capital. And

fifth, unilateral trade liberalization, in contrast to well-negotiated trade agreements, does not guarantee market access, instead increasing vulnerability.

Ocampo's overview shows that, despite the significant efforts already made on the part of governments in the region, many hurdles remain before Latin America and the Caribbean can assume a stable and competitive position in the global economy. Political will is essential to consolidating those transformations already in place, correcting misguided policies and forging a path toward international stability and cooperation.

www.eclac.org

www.semana.com/documentos/insercion.doc