

Latin America and the Caribbean: outlook 2011



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ECLAC

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1. The Latin American and Caribbean region performed well in 2010, but slower growth is expected in 2011

- A two-speed recovery is taking place in the international economy in a context that is unprecedented. While Europe and the United States are experiencing slower growth and uncertainty over high levels of public indebtedness, the emerging economies are driving the global recovery.

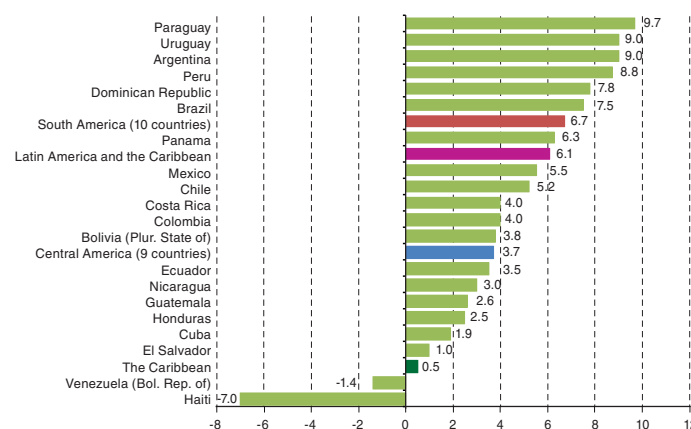
■ **Figure 1 ■**
World GDP: annual growth rates by region
(Percentages)



Source: United Nations, *World Economic Situation and Prospects 2011*, New York, 2011.

- The Latin American and Caribbean region registered growth again in 2010, consolidating the recovery that had begun in the second half of 2009.

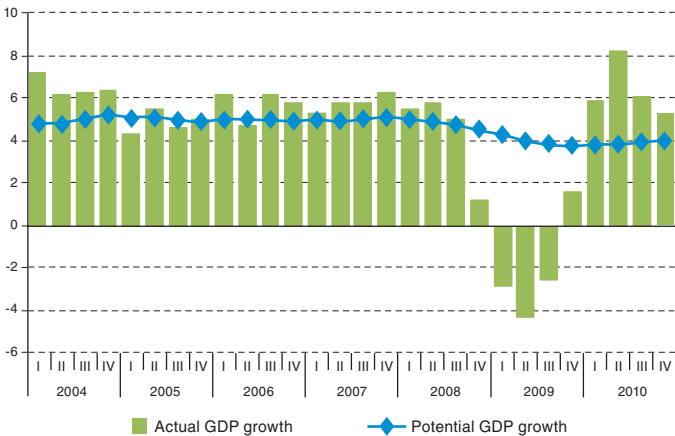
■ **Figure 2 ■**
Latin America and the Caribbean: GDP growth rates, 2010
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- After strong expansion in 2010, a more moderate pace of growth is expected in 2011, owing to both external factors (slowing global growth and international trade) and domestic factors (withdrawal of fiscal stimuli and depletion of idle production capacity).

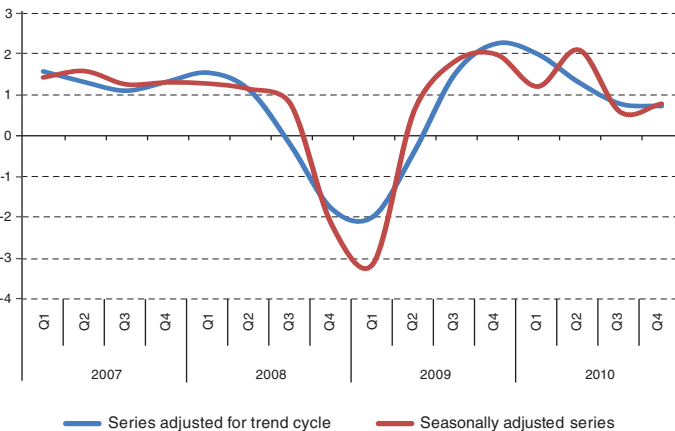
■ **Figure 3 ■**
Latin America (9 countries): actual and potential GDP growth, year-on-year quarterly rates of variation, 2004-2010
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- In fact, the pace of growth had already begun to slow in the second half of 2010.

■ **Figure 4 ■**
Latin America (7 countries): quarter-on-quarter GDP variation, 2007-2010
(Percentages)

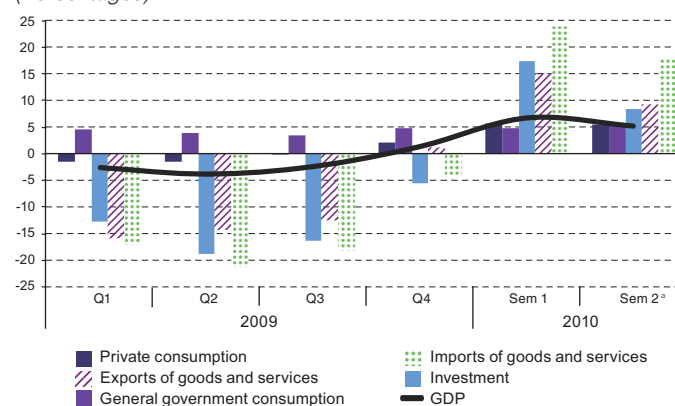


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

2. The region's growth in 2010 was driven by economic policies and rising domestic demand, and was underpinned by the global economic recovery, especially the upturn in international trade

- The economic policies implemented to offset the impact of the global economic and financial crisis helped to drive a recovery in domestic demand.

Figure 5
Latin America and the Caribbean: year-on-year quarterly variation in supply and demand, 2009-2010
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

^a Estimate.

- The increase in investment was reflected in higher stocks of machinery and equipment and a recovery of inventory levels.

Figure 6
Latin America and the Caribbean: gross fixed capital formation by component, year-on-year rates of variation, 2004-2010
(Percentages, in constant dollars at 2000 prices)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- Stronger economic activity and an upturn in labour market indicators helped to boost private consumption.

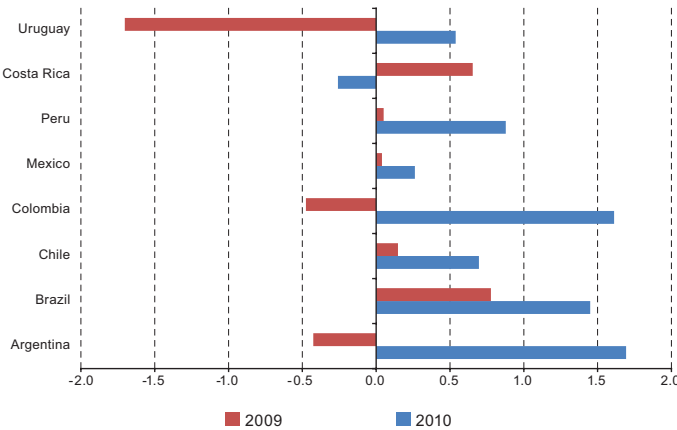
■ **Figure 7 ■**
Latin America and the Caribbean: employment and unemployment
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
* Projection.

- This trend was reinforced by the rise in lending to the private sector in real terms.

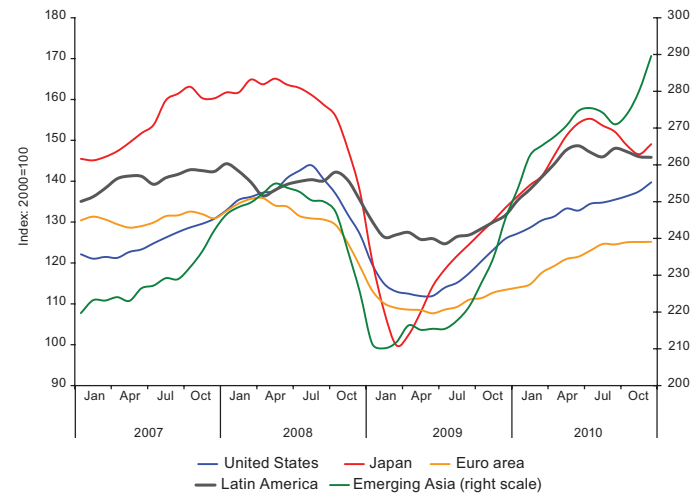
■ **Figure 8 ■**
Latin America (8 countries): variation in credit to the private sector in real terms, November 2009–November 2010
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- Starting in the second semester of 2009, international trade volumes began to recover, especially in emerging Asia.
- By the second quarter of 2010, exports from Latin America and the Caribbean had climbed above pre-crisis levels.
- The slowdown in the global economy projected for 2011 is expected to affect trade flows, however.
- Since Europe and the United States are the region's largest export markets, slower growth in those markets—owing to fiscal and monetary adjustments—could have a significant impact on the outlook for Latin America and the Caribbean.

■ Figure 9 ■

World exports by region, 2007-2010*(Three-month moving average, index: 2000=100)*

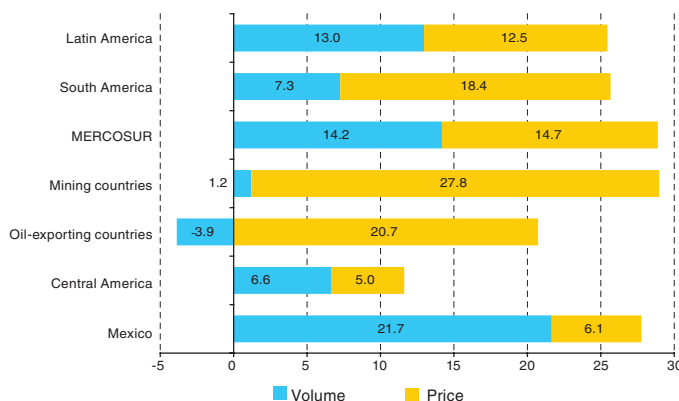
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

3. The region's exports continue to expand owing both to greater volumes and to higher prices

- Within the region, export volumes rose fastest in Mexico and the MERCOSUR countries, but more slowly in Central America and in the mining countries. In hydrocarbon-exporting countries, export volumes actually contracted.
- The rise in commodity prices also contributed to the upturn in export values, especially in South America.

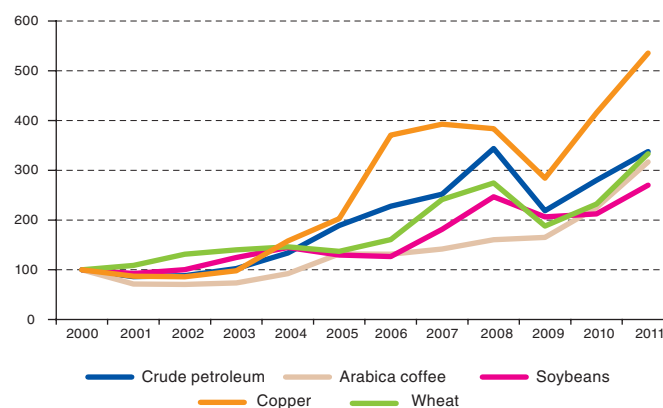
- The commodity prices that are most significant for the region have regained the upward trend observed before the crisis. By early 2011 they reached—and, in the case of copper, exceeded—levels similar to the highs of mid-2008.
- This situation benefited the terms of trade of the South American economies, which are net exporters of these commodities. The inverse occurred in Central America, as a net commodity importer. Mexico has seen a mixed terms-of-trade effect, since—although it is a net oil exporter—the prices of its manufacturing exports are under pressure from competition from China in the United States market.

■ **Figure 10** ■
Latin America and the Caribbean: change in export values in 2010; breakdown by volume and price
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

■ **Figure 11** ■
Selected commodity prices: annual averages, 2000-2011^a
(Nominal dollars; index: 2000=100)

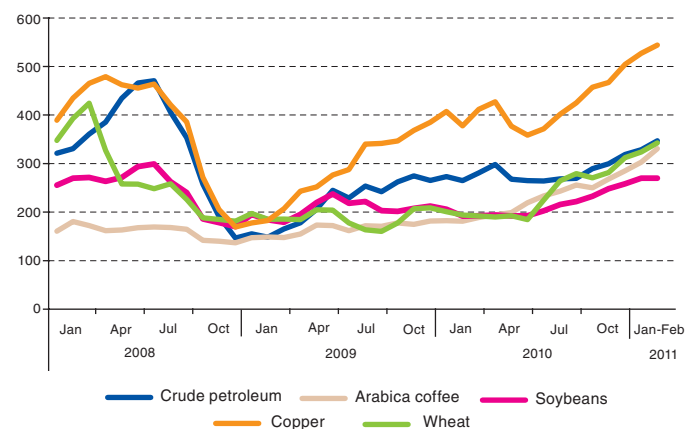


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of World Bank Commodity Price Data (Pink Sheet).

^a The figure for 2011 refers to the average for January and February.

- Commodity prices have continued to rise in the early months of 2011 and this trend is expected to continue, albeit at a slower pace, as the global economy recovers. Hydrocarbon prices may rise more sharply, depending on how the current turmoil in North African countries evolves.
- In addition to current account effects, the rises in commodity prices have contributed to the resurgence of inflationary pressures at both the global and regional levels.

■ **Figure 12** ■
Selected commodity prices: monthly averages,
January 2008–February 2011
(Nominal dollars; index: 2000=100)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of World Bank Commodity Price Data (Pink Sheet).

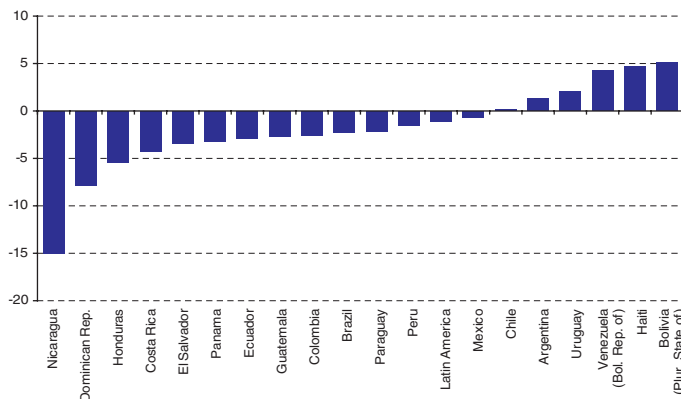
4. Imports are expanding even faster than exports and the current account balance is turning increasingly negative

- Despite rising exports, the current account position is deteriorating as a result of the even faster rise in imports and in profit remittances—especially by international firms involved in natural resource extraction.

- Remittances sent from developed countries by emigrant workers have also risen, but still fall short of pre-crisis levels in annual terms. Although these inflows climbed throughout 2010, they have been relatively unchanged in the past few months. Given the slow growth in the European countries and in branches of the developed countries' economies that employ immigrant labour, particularly the construction sector in the United States, remittances are unlikely to regain pre-crisis levels in 2011.

■ Figure 13 ■

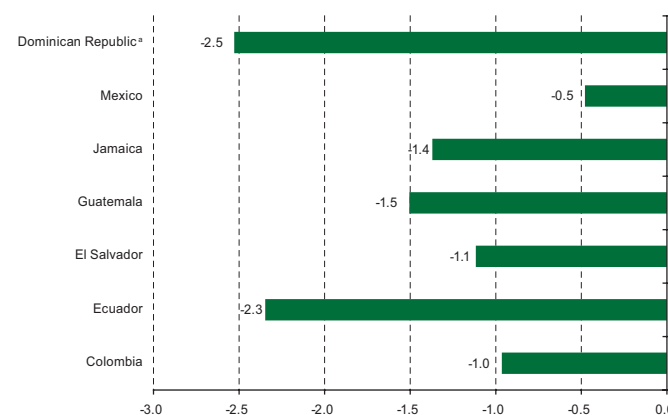
Latin America and the Caribbean: current account balance, 2010
(Percentages of GDP)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

■ Figure 14 ■

Latin America and the Caribbean: difference between workers' remittances in 2010 and the average for 2004-2007
(Percentages of GDP)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of World Bank, World Development Indicators [online database].

* Estimate.

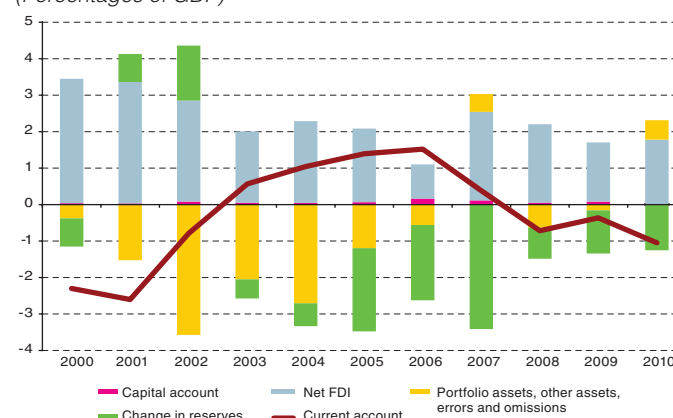
5. The current account deficit was more than offset by capital inflows, which enabled the countries of the region to build up international reserves

- The region's current account deficit, though increased, was comfortably financed by inflows of foreign capital. The region is expected to retain its ready access to international financial markets in 2011.
- The increased capital flows into Latin America have been driven by robust growth in the emerging economies and higher rates of return offered by their assets.

■ Figure 15 ■

Latin America and the Caribbean: current account balance and financial account components, 2000-2010

(Percentages of GDP)

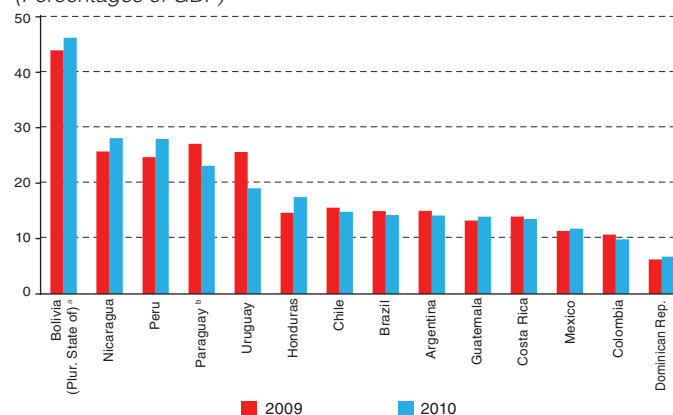


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

■ Figure 16 ■

Latin America and the Caribbean (selected countries): international reserves, 2009-2010

(Percentages of GDP)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

^a Estimate on the basis of official figures from the International Monetary Fund and the Central Bank of Bolivia.

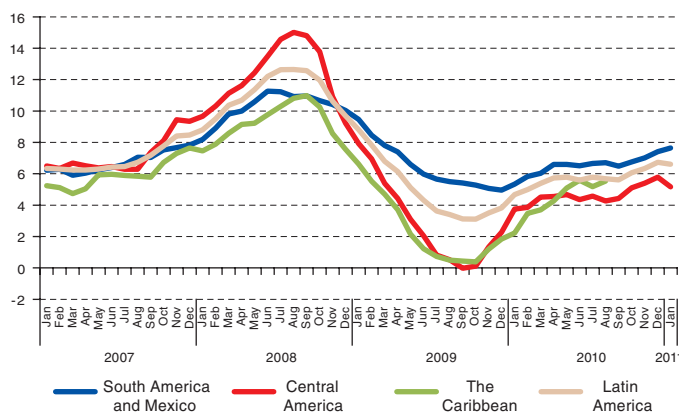
^b Refers to November 2010.

6. Following the countercyclical macroeconomic policies of 2009, fiscal and monetary stimuli were scaled back beginning in late 2010

- After inflation rates remained stable for much of 2010, inflationary pressures emerged again in the last few months of the year.

■ Figure 17 ■

Latin America and the Caribbean: monthly inflation rate, simple average, January 2007-January 2011
(Percentages)

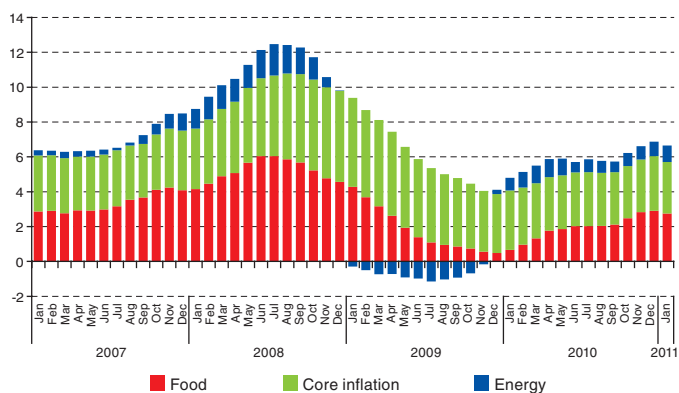


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- Domestic consumer price inflation mainly reflects higher prices for food and for energy and fuel, owing largely to the rise in the international prices of these products. In addition, pass-through of these price hikes to other items of the consumption basket and burgeoning domestic demand in several of the region's economies have pushed up core inflation. These trends have sharpened in the last quarter of 2010 and thus far in 2011. Partial data for February 2011 indicates a rise in core inflation in most of the countries.

■ Figure 18 ■

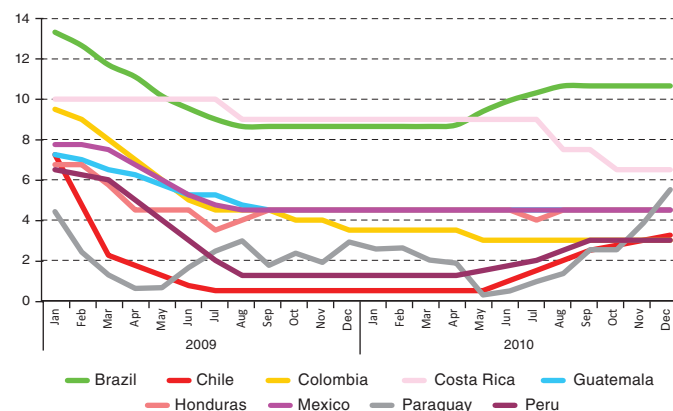
Latin America and the Caribbean: inflation by component, simple average
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- Accordingly, the countries of the region have begun to move towards more neutral policy stances.
- This more cautious monetary policy stance is reflected in an upward trend in benchmark interest rates.
- Monetary policy is also faced with challenges arising from the current context of high international liquidity and strong capital inflows, amid rapid economic expansion.

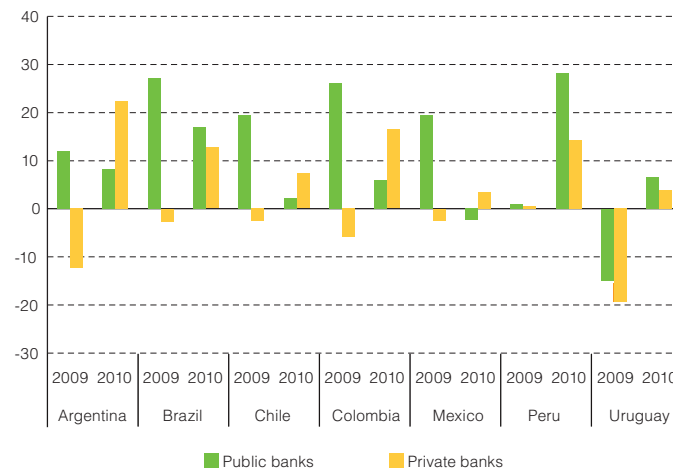
■ **Figure 19 ■**
Latin America (selected countries): monetary policy rates
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- At the same time, a smaller proportion of the growth in lending is coming from public banks.

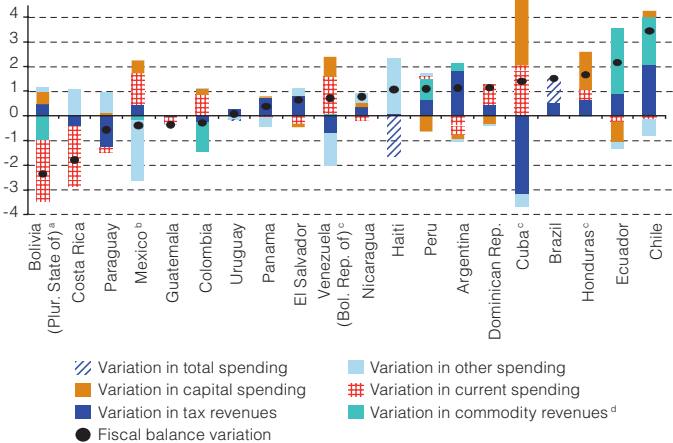
■ **Figure 20 ■**
Latin America (selected countries): real credit growth, November-November
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- In 2010, the performance of the fiscal accounts was shaped largely by the revenue side, mainly by higher levels of economic activity and, in countries specializing in the production and export of natural-resource-intensive goods, by the effect of commodity price rises. Most countries at least partially maintained the fiscal stimulus in 2010.
- After the strong stimulus in 2009 the general strategy for 2010 was a pullback of public policies aimed at stimulating demand, albeit with marked differences between countries.

■ **Figure 21 ■**
Latin America and the Caribbean: fiscal performance by country, variation 2009-2010
(Percentages of GDP)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

^a General government.

^b Public sector.

^c Total spending does not include net lending.

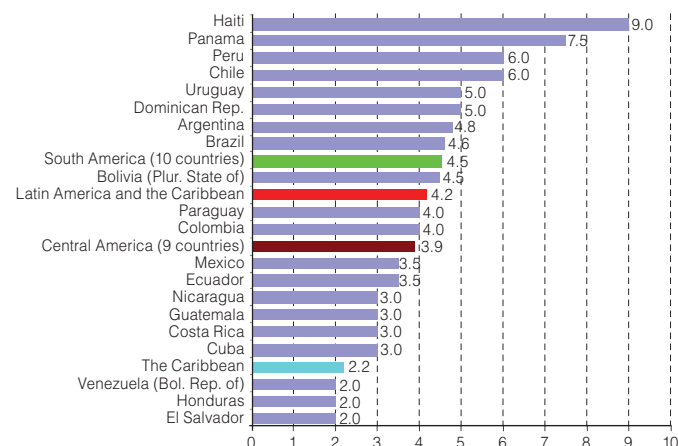
^d Includes both tax and non-tax revenues derived from commodities.

7. The region will continue growing in 2011, albeit at a lower rate

- The region's performance was outstanding in 2010, largely thanks to the impact of the countercyclical policies deployed and the international recovery that year.
- The space for implementation of public policies will be affected not only by the need to rebuild the capacity for countercyclical response, but also by concerns arising from excess global liquidity that could result from monetary policies in the United States.
- These concerns will be the main factor influencing monetary and fiscal policies in those countries of the region that are potential receivers of short-term capital inflows.
- The region's economic growth is projected at 4.2% for 2011.

■ Figure 22 ■

Latin America and the Caribbean: GDP growth, 2011
(Percentages)

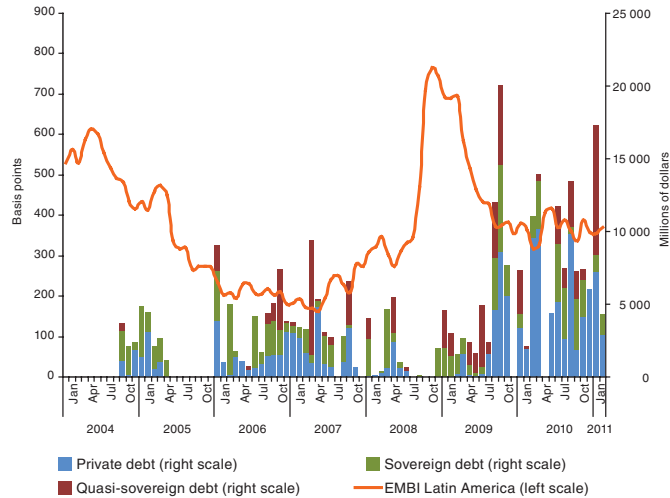


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

8. Currencies in Latin America and the Caribbean are appreciating against the dollar, amid a resurgence of inflationary pressure

- The region has experienced a surge in short-term capital inflows, owing to the high returns and low risk offered by many of its financial assets.

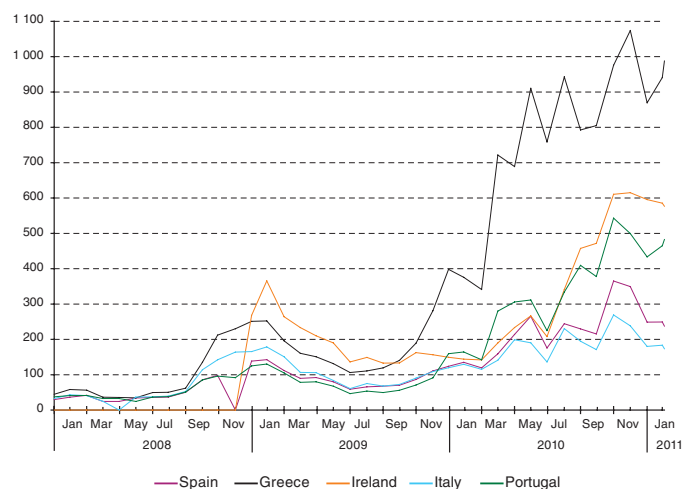
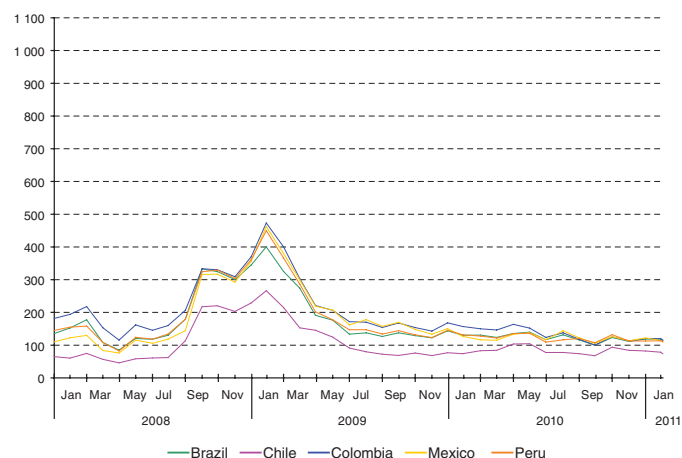
■ **Figure 23** ■
Latin America and the Caribbean: bond issues and risk premiums, 2004-2011
(Millions of dollars and basis points)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of figures from LatinFinance (bonds database), JP Morgan and Merrill Lynch.

- In addition, the debt instruments of almost all countries have been upgraded and their sovereign risk premiums have improved substantially, although they have not yet returned to pre-crisis levels.

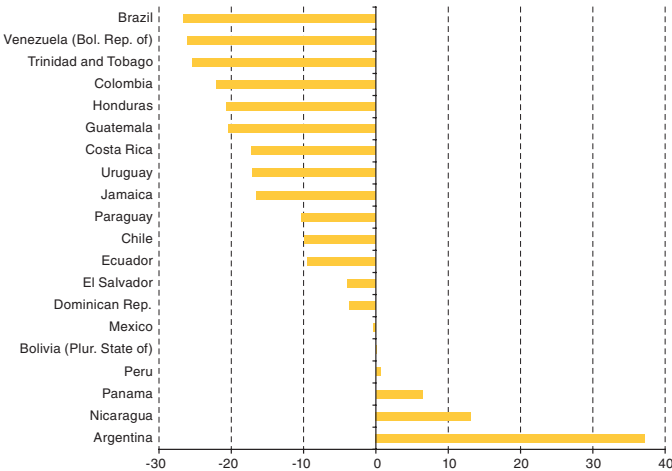
■ **Figure 24 ■**
Risk premiums on five-year credit default swap contracts
(Basis points, end of month)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of figures provided by Bloomberg.

- As a result, many of the countries' currencies have appreciated against the United States dollar.
- Even when calculated against a basket of currencies, real exchange rates were below the long-term average in most of the countries in the region in 2010.
- In 2011, heightened global liquidity will likely entrench this tendency towards real currency appreciation in most of the region's countries.

■ **Figure 25 ■**
Latin America and the Caribbean: real effective exchange rate variation, December 2010 compared with average for 1990-2009 (Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

What are the likely short-term effects?

- The external accounts may be expected to deteriorate, but should not threaten growth in the short term.
- On the contrary, as seen in similar situations, capital inflows will support steady growth in domestic demand.
- At the same time, currency appreciation could help check inflationary pressures. It may even have a positive short-term impact on poverty indicators, because consumption patterns in poorer population segments lean heavily towards tradable goods, which should become cheaper in relative terms.

Beyond the short term, the expected effects are less benign

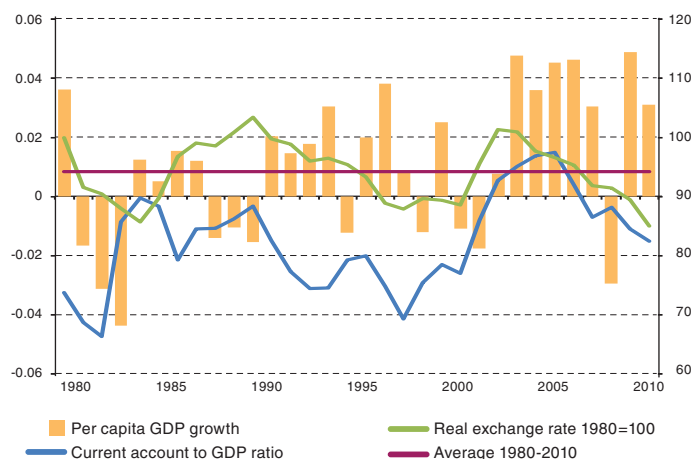
- High global liquidity exerting downward pressure on real exchange rates and upward pressure on commodity prices could encourage both the production of non-tradable goods, which would have a negative impact on the external accounts, and a specialization in the production and export of primary goods.
- Such specialization would make the economies of the region more vulnerable to external shocks and add to the volatility of domestic macroeconomic aggregates.
- A deterioration of the external account would lead to greater indebtedness, increasing the vulnerability of the region's economies to financial shocks, to the extent that further growth is more intensive in external financing.

Recent economic history sheds light on the links between growth, current account balance and the real exchange rate

- Periods of improvement in the region's current account balance have been associated with a rising real exchange rate.
- Despite positive outcomes in terms of economic growth since 2003 (with the exception of 2009), the real exchange rate has fallen steadily, alongside a persistent deterioration in the current account balance.

■ Figure 26 ■

Latin America and the Caribbean: growth, current account balance and real exchange rate, 1980-2011



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

What can the countries of the region do to address this externally generated situation?

- Several of the region's countries have implemented mechanisms aimed at regulating inflows of short-term capital.
- Many central banks have opted to intervene in currency markets in order to try to prevent or at least slow appreciation, while replenishing their reserves.

These measures are appropriate, but they may not be enough

- Such measures should be complemented by a countercyclical strategy encompassing both the fiscal and the financial realms, geared towards easing pressure on domestic demand and preventing credit-market overheating.

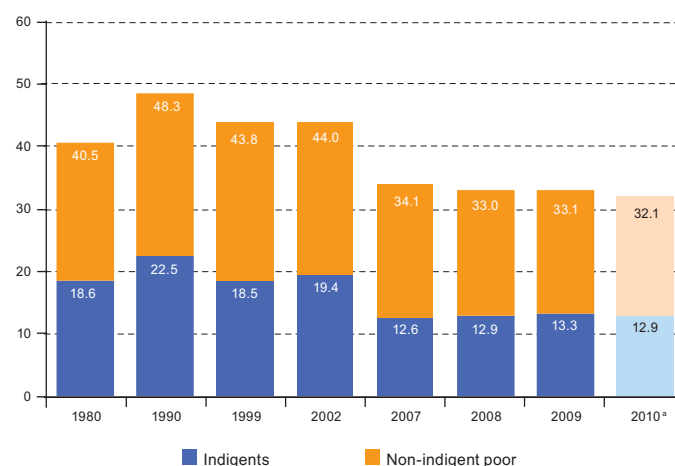
- In a context of abundant international liquidity, renewed inflationary pressures present an additional dilemma for monetary policymakers.
- Therefore, another option would be to take industrial policy measures aimed at making tradable-goods-producing sectors more profitable.
- A lasting solution is unlikely, however, without more coordinated strategies at the international level to narrow global imbalances. At the local level, the challenge is to manage exchange rate appreciation while maintaining a stable fiscal situation and keeping inflation in check.

9. Beyond the current economic situation, the Latin American and Caribbean region is facing challenges of a more structural nature. Advances in macroeconomic policy management and the implementation of countercyclical policy were crucial to the region's ability to weather the crisis better than on past occasions, but the crisis also turned a spotlight on the magnitude of the persistent inequality in Latin America and the Caribbean. This remains the pending challenge for development in Latin America

The region has learned the lessons of the past with regard to macroeconomic policy management and social investment for combating poverty.

- Poverty and indigence rose less than had been expected in 2009 and decreased in 2010.
- This was mainly owed to the fact that the countries directed substantial portions of their stimulus packages towards job preservation and social transfers to the poorest and most vulnerable families.
- Nevertheless, the region's poverty rate stands at around 32%, or 180 million people, of whom 72 million are indigent.

■ **Figure 27 ■**
Latin America: poverty and indigence, 1980-2010
(Percentages)



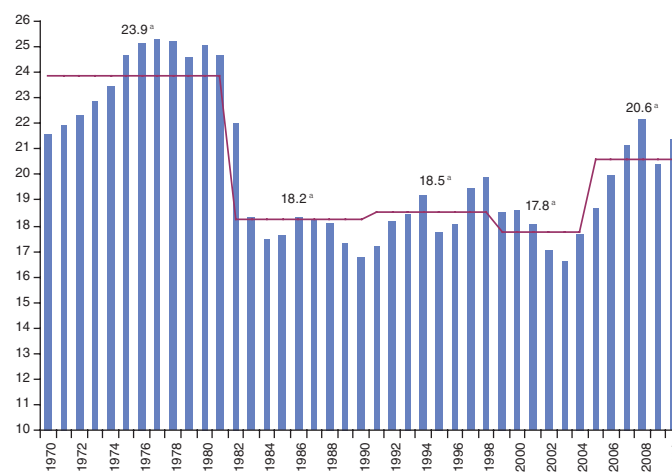
Source: Economic Commission for Latin America and the Caribbean (ECLAC), *Social Panorama of Latin America, 2010* (LC/G.2481-P), Santiago, Chile, 2010.
* Estimate.

10. The crisis represents a turning point, since it broke the continuity of one model and created the opportunity to chart new courses

This means facing up to debts from the past as well as more recent ones:

- Highly unequal income distribution:
 - Latin America continues to be the most unequal region in the world.
- Low rates of investment and saving:
 - Although the regional investment ratio began to rise considerably from 2004 on, it remains well below the figures seen in the 1970s.

■ **Figure 28 ■**
Latin America (19 countries): gross fixed capital formation,
1970-2009
(Percentages of GDP)



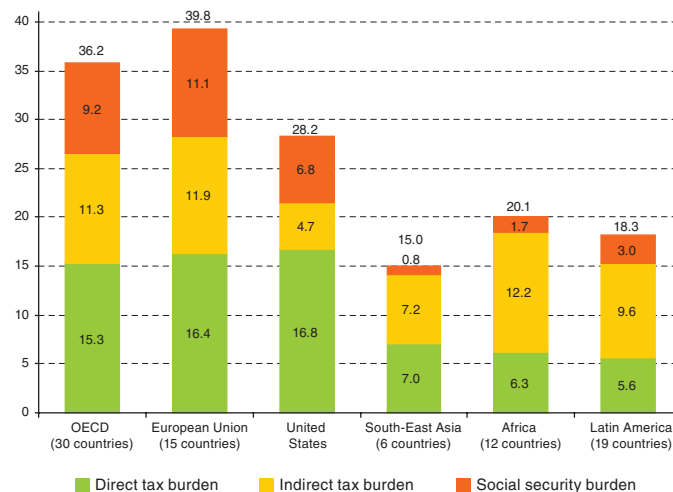
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of figures from the International Monetary Fund and the central banks of the respective countries.

^a Average for the period.

^b Estimate.

- Increasingly uneven production patterns:
 - It is essential to achieve productive convergence. A fresh effort is needed to develop exports with greater value and embedded knowledge, with forward and backward linkages tying the export sectors to the rest of the economy.
- A regressive tax structure:
 - Compared with other regions, the Latin American and Caribbean region has a regressive tax structure and a higher proportion of indirect taxes.

■ **Figure 29 ■**
Latin America and the Caribbean: global comparison
of tax burden
(Percentages of GDP)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures and information provided by the Organization for Economic Cooperation and Development (OECD) and the International Monetary Fund (IMF).

11. In *Time for equality: closing gaps, opening trails*, ECLAC proposed the following objectives:

- Implement macroeconomic policy for inclusive development to lessen volatility, stimulate productivity and create the conditions for inclusion.
 - Reduce structural heterogeneity and productivity gaps with more innovation, greater creation and dissemination of knowledge and increased support for small and medium-sized enterprises (SMEs).
 - Enhance international integration, diversifying exports and increasing competitiveness.
- Reduce territorial disparities, which damage productive, institutional and social development capabilities and hinder the development of national productive linkages.
- Create more and better jobs to increase equality of opportunities and social inclusion.
- Close social gaps by a sustained increase in social spending and the development of more solid social institutions.
- Assign the State a new role as driver of these objectives and forge new fiscal covenants to endow it with the resources needed to implement the necessary public policies.